

Wachovia, Fifth Third Face Losses Tied to Hedge Funds

By David Mildenberg

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Bloomberg - Wachovia Corp. and Fifth Third Bancorp, U.S. banks that tried to profit by taking out life insurance on their employees, now face losses because the policies held the same types of investments that led to the global credit crunch.

Wachovia Corp. and Fifth Third Bancorp, U.S. banks that tried to profit from taking out life insurance on their employees, now face losses because the policies held the same types of investments that led to the global credit crunch. Wachovia and Fifth Third reported more than \$600 million of losses in bank-owned life insurance programs, known as BOLI, mainly because of investments in hedge funds managed by Citigroup Inc. **The Falcon funds used at least six trading strategies to provide an alternative to the typical Treasury note and corporate bond holdings of life insurers, said Boyd Page, an Atlanta lawyer who's representing investors in the funds, which slumped more than 50 percent in the past year as the subprime market collapsed.**

"A lot more people are going to take a lot more losses," said Adam Savett, a vice president at New York-based RiskMetrics Group Inc., which studies corporate risk. "We are seeing just the tippy-top of the iceberg."

The BOLI-related losses add to an erosion of capital that's leaving banks including Charlotte, North Carolina-based Wachovia and Fifth Third of Cincinnati with their worst earnings outlook in more than a decade. Total BOLI holdings of U.S. banks topped \$120 billion at the end of 2007, according to data compiled by Michael White Associates LLC in Radnor, Pennsylvania. Bank of America Corp. had \$16.2 billion of BOLI assets as of March 31, followed by Wachovia's \$14.8 billion, regulatory filings show.

Losses from the BOLI programs were reported earlier today by the Wall Street Journal.

Insurance Salesmen

BOLI gained in popularity during the 1990s after accounting changes forced employers to account for retiree medical benefits, said Larry Hicks, a Chicago-based benefits consultant at Hay Group. The life insurance programs allowed companies to set aside pools of capital to pay for employee benefits, with gains piling up tax-free.

Regulators backed the use of BOLI because it allowed banks to boost capital and risk less than they would by making loans, said Edwin Peacock Jr., owner of an insurance agency in Charlotte, North Carolina, who sold BOLI policies.

"When the Office of the Comptroller approved BOLI, it was considered the full employment act for life insurance salesmen," he said.

To increase life insurance returns, Fifth Third put \$612 million into policies sold by Transamerica Life Insurance Corp. in 2004 and 2005. Fifth Third has sued Transamerica and its BOLI adviser, Clark Consulting Corp., to recover \$323 million of losses. Transamerica and Clark Consulting are units of Dutch insurer Aegon NV in The Hague.

45 Cents

Transamerica invested Fifth Third's insurance premiums in Citigroup's Falcon funds, according to an April 18 lawsuit filed by Fifth Third. Cindy Nodorft, a spokeswoman for Transamerica and Clark Consulting, said Fifth Third was free to choose from a number of investment alternatives.

“We are confident the terms of the policy were adhered to,” Nodorft said. “As a result, we believe the complaint is without merit and intend to fully defend it.”

Wachovia spokeswoman Christy Phillips Brown said the BOLI loss was due to the Falcon funds.

New York-based Citigroup, the biggest U.S. bank by assets, has asked Falcon investors to refrain from filing lawsuits in exchange for 45 cents on the dollar to cash out of the funds.