

**UNITED STATES OF AMERICA**  
before the  
**SECURITIES AND EXCHANGE COMMISSION**

**SECURITIES EXCHANGE ACT OF 1934**  
**Release No. 73243 / September 29, 2014**

**ACCOUNTING AND AUDITING ENFORCEMENT**  
**Release No. 3588 / September 29, 2014**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-16177**

**In the Matter of**

**BANK OF AMERICA  
CORPORATION,**

**Respondent.**

**ORDER INSTITUTING  
CEASE-AND-DESIST PROCEEDINGS  
PURSUANT TO SECTION 21C  
OF THE SECURITIES EXCHANGE  
ACT OF 1934, MAKING FINDINGS,  
AND IMPOSING A CEASE-AND-  
DESIST ORDER**

**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 (“Exchange Act”) against Bank of America Corporation (“BAC” or “Respondent”).

**II.**

In anticipation of the institution of these proceedings, BAC has submitted an Offer of Settlement (the “Offer”), which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over it and the subject matter of these proceedings, which are admitted, BAC consents to the entry of this Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order (the “Order”), as set forth below.

### III.

On the basis of this Order and BAC's Offer, the Commission finds<sup>1</sup> that:

#### A. Summary

1. The federal securities laws require public companies to make and keep books and records in reasonable detail to, among other things, accurately and fairly reflect transactions in which they engage. The federal securities laws also require public companies to devise and maintain a system of internal accounting controls sufficient to, among other things, provide reasonable assurances that transactions are recorded as necessary to permit preparation of financial statements in conformity with United States Generally Accepted Accounting Principles ("GAAP"). These laws seek to ensure the integrity and accuracy of information that is eventually disclosed to investors.

2. As part of its acquisition of Merrill Lynch & Co., Inc. ("Merrill") on January 1, 2009, BAC assumed (or acquired) a \$52.5 billion portfolio of structured notes and other financial instruments (the "Notes") that Merrill issued.<sup>2</sup> At the time of acquisition, BAC recorded the Notes at fair value, which was a \$5.9 billion discount to the Notes' par value due to an adverse change in Merrill's creditworthiness.

3. As of March 31, 2014, 87 percent of the Notes had either matured or been repurchased by BAC. Because BAC recorded the Notes at a discount to par when acquired, BAC realized losses on the Notes upon their maturation or when BAC redeemed them at par.

4. For purposes of calculating regulatory capital,<sup>3</sup> applicable rules required BAC to deduct the realized losses on the Notes as they occurred. From January 1, 2009 through March 31, 2014, however, BAC failed to deduct certain realized losses on the Notes when it calculated and reported its regulatory capital.

5. From the first quarter of 2009 to the fourth quarter of 2013, the realized losses that BAC incurred on the Notes increased over time as more Notes either matured or were redeemed. Therefore, with each passing fiscal quarter and year starting in 2009, BAC overstated its Basel I and

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<sup>1</sup> The findings herein are made pursuant to BAC's Offer of Settlement and are not binding on any other entity or person in this or any other proceeding.

<sup>2</sup> Generally, a structured note is a debt obligation where the return typically is not based on an interest rate like a bank note but instead pays a return based on an embedded derivative component. For example, with a structured note, the note holder will receive her principal at a fixed maturity but may or may not receive income based on the performance of a defined security, index or asset class over a period of time.

<sup>3</sup> "Regulatory capital" is the amount of capital that a banking organization must maintain as required by, among others, the Board of Governors of the Federal Reserve System ("FRB"). Regulatory capital requirements were put into place to ensure that banking organizations have sufficient capital to sustain operating losses while still honoring withdrawals and so that they do not take on excessive leverage. Regulatory capital typically is expressed in the form of ratios (certain calculations or categories of regulatory capital *over* risk-weighted assets).

Basel III regulatory capital by a greater amount in each of its Form 10-Q and Form 10-K filings with the Commission.<sup>4</sup>

6. BAC overstated its regulatory capital in all Form 10-Q filings that it made with the Commission from 2009 to 2013 (15 filings). BAC also overstated its regulatory capital in all Form 10-K filings that it made with the Commission for fiscal years 2009 through 2013 (5 filings).

7. By year-end 2013, BAC overstated its Basel I regulatory capital by \$3.714 billion. In mid-April 2014, BAC internally discovered the regulatory capital overstatements and, after analyzing the issue, BAC disclosed the overstatements in a Form 8-K filing that it made with the Commission, dated April 28, 2014.

8. To ensure it properly deducted the realized losses that it incurred on the Notes from its regulatory capital starting in 2009, BAC should have made and kept accurate books and records and also should have devised and maintained a system of internal accounting controls sufficient to provide reasonable assurances that transactions were recorded as necessary to permit preparation of financial statements in conformity with GAAP.

9. As a result of its failure to do so, BAC violated Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act.

10. In response to the Commission's investigation, BAC provided substantial cooperation to Commission staff. BAC also has voluntarily undertaken steps to remediate and address, among other things, the inadequate books and records and internal accounting control deficiencies that are the subject of this proceeding.

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<sup>4</sup> GAAP requires banking organizations to disclose regulatory capital ratios and requirements in notes to the financial statements. Basel I was the first international uniform framework developed to calculate regulatory capital and became effective in 1988. Basel III, which became effective for certain banking organizations, including BAC, beginning with the quarter ended March 31, 2014, is the latest international uniform framework developed to calculate regulatory capital. Though disclosure and compliance with Basel III regulatory capital ratios only became effective for these banking organizations effective January 1, 2014, many public banking organizations started disclosing Basel III figures and ratios much earlier than required in light of investor interest in how banking organizations' capital ratios would change under the new requirements. BAC first started disclosing its estimated Basel III regulatory capital ratios in its Form 10-Q filing for the third quarter of 2012. Under Regulations G and S-K, these Basel III estimated ratios were considered to be "non-GAAP" measures until BAC was required by regulatory rules to comply with the Basel III capital ratio minimums.

## **B. Respondent**

11. **Bank of America Corporation** is a bank holding company incorporated in Delaware and a financial services holding company under the Gramm-Leach-Bliley Act. BAC's common stock is registered with the Commission under Section 12(b) of the Exchange Act and trades on the New York Stock Exchange under the symbol "BAC." BAC's principal offices are located in Charlotte, North Carolina.

## **C. Facts**

### *The Overstatements*

12. When BAC acquired Merrill on January 1, 2009, it acquired three types of Notes with a total par value of \$52.5 billion. At the time BAC acquired the Notes from Merrill, the Notes had a fair value below par due to a decline in Merrill's creditworthiness. Pursuant to GAAP, BAC recorded the Notes at then-fair value—a \$5.9 billion discount to par.

13. Even though BAC acquired the Notes at a discount to par, BAC assumed liability on the Notes to redeem them at par upon their maturation or when BAC otherwise repurchased them. Because BAC acquired the Notes at a discount but redeemed them at par, BAC realized losses on the Notes upon redemption or maturity.

14. When calculating regulatory capital, BAC was required to include these realized losses that were recognized in GAAP equity.<sup>5</sup> When calculating its regulatory capital from 2009 through 2013, however, BAC failed to do so. In other words, BAC improperly excluded certain realized losses related to the initial \$5.9 billion discount when calculating its regulatory capital, which resulted in the regulatory capital overstatements.

15. As more Notes matured or BAC repurchased more Notes over time, BAC incurred more realized losses. Therefore, with each passing fiscal quarter and year starting in 2009, BAC overstated its regulatory capital by a greater amount in its Form 10-Q and Form 10-K filings.<sup>6</sup>

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<sup>5</sup> Calculation of regulatory capital begins with total common shareholders' equity followed by adjustments as required by the regulatory capital rules and frameworks.

<sup>6</sup> As the regulatory capital amounts were only disclosed in the notes to the financial statements, the overstatements of regulatory capital that BAC made had no effect on the company's consolidated balance sheet, consolidated statements of income, comprehensive income, changes in shareholders' equity or cash flow statements.

16. As a result of its inaccurate books and records and its deficient internal accounting controls, BAC overstated its Basel I regulatory capital in its Form 10-Q and Form 10-K filings. At the end of each year, these overstatements were as follows:<sup>7</sup>

<b><u>Form 10-K</u></b> <b><u>(for fiscal year)</u></b>	<b><u>Overstatement</u></b> <b><u>(in billions)</u></b>
2009	\$0.888
2010	\$1.491
2011	\$2.131
2012	\$2.823
2013	\$3.714

17. Correspondingly, by fiscal year end 2013, BAC overstated the following Basel I ratios by the following percentages in its Form 10-K filing:

<b><u>Ratio</u></b>	<b><u>Overstatement</u></b>
Tier 1 Common Capital	0.3%
Tier 1 Capital	0.2%
Total Capital	0.3%
Tier 1 Leverage	0.2%

18. In addition to disclosing its regulatory capital under the Basel I framework, BAC also first disclosed its regulatory capital under the Basel III framework starting in its Form 10-Q filing for the third quarter of 2012. Therefore, BAC made additional Basel III regulatory capital overstatements in four Form 10-Q filings (third quarter of 2012 through third quarter of 2013) and in two Form 10-K filings (for fiscal years 2012 and 2013).

19. By fiscal year end 2013, BAC overstated the following Basel III ratios (pro-forma on a fully phased-in basis) by the following percentages in its Form 10-K filings:<sup>8</sup>

<b><u>Ratio</u></b>	<b><u>Overstatement</u></b>
Common Equity Tier 1 Capital—Standardized Approach	0.3%
Common Equity Tier 1 Capital—Advanced Approach	0.4%

<sup>7</sup> The dollar amounts associated with the regulatory capital overstatement that BAC made in its Form 10-Q filings are not provided in this Order.

<sup>8</sup> BAC overstated its Basel III regulatory capital (pro-forma on a fully phased-in basis) by \$4.369 billion in its Form 10-K filing for fiscal year end 2013.

### How the Overstatements Occurred

20. A number of groups within BAC had some involvement with regulatory capital calculation and reporting. Shortly after the acquisition of Merrill, a transition team created a schedule that tracked cumulative gains and losses on certain liabilities. In creating that schedule, BAC correctly understood that pre-acquisition declines in fair value on the Notes relating to Merrill's own creditworthiness should not be included as an adjustment in BAC's regulatory capital calculation. That schedule did not, however, contemplate or account for the fact that those Notes would mature or otherwise be redeemed over time.

21. BAC used this schedule each quarter, correctly excluding the difference in value of the Notes at par and their fair value at the time of acquisition from its regulatory capital calculation. The flaw in this process was that BAC continued to make this adjustment in BAC's regulatory capital calculation even after some of the Notes had matured or otherwise been redeemed, resulting in a recurring overstatement of regulatory capital. In other words, BAC never recognized and reflected in its regulatory capital calculations the fact that some of the Notes had matured or were redeemed, which were events that caused BAC to incur realized losses on the Notes. It was this oversight that led BAC to incorrectly exclude—or to *improperly not include*—these realized losses for purposes of calculating regulatory capital.

22. In sum, BAC's regulatory capital overstatements arose from the rote application of this process—quarter after quarter, year after year—since the acquisition of Merrill in January 2009.

23. From 2009 through 2013, therefore, BAC did not adequately consider whether its internal process for computing its regulatory capital was operating as intended or required. As a result, BAC failed to make and keep accurate books and records, and failed to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that transactions were recorded as necessary to permit preparation of financial statements in conformity with GAAP, over this time period.

### Identification of the Overstatements

24. BAC released its earnings for the first quarter ending March 31, 2014 on April 16, 2014. In the days that followed, BAC's Corporate Tax Department was reviewing the earnings release and made certain inquiries, which led to the identification of the error. Between April 21, 2014 and April 28, 2014, BAC worked to analyze and resolve the issue.

25. On April 28, 2014, BAC issued a press release announcing a downward revision to the company's previously disclosed regulatory capital amounts and ratios, and also filed a Form 8-K with the Commission disclosing the company's revised regulatory capital amounts and ratios. In its press release, BAC explained that at "the FRB's request, the company is suspending its previously announced 2014 capital actions, including the \$4.0 billion common stock repurchase authorization and the planned increase in the quarterly common stock dividend from \$0.01 per common share to \$0.05 per share."

26. Since discovery and disclosure of the computation error, BAC is developing improved documentation and spreadsheet controls, as well as enhanced internal controls around automation of processes, relating to its calculation and reporting of regulatory capital amounts and ratios.

#### **D. Violations**

27. As a result of the conduct described above, BAC violated Section 13(b)(2)(A) of the Exchange Act, which requires public companies to “make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer.”

28. As a result of the conduct described above, BAC violated Section 13(b)(2)(B) of the Exchange Act, which requires public companies to “devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that . . . (ii) transactions are recorded as necessary (I) to permit preparation of financial statements in conformity with generally accepted accounting principles or any other criteria applicable to such statements, and (II) to maintain accountability for assets.”

#### **IV.**

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in BAC’s Offer.

Accordingly, pursuant to Section 21C of the Exchange Act, it is hereby ORDERED that:

A. BAC cease and desist from committing or causing any violations and any future violations of Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act.

B. BAC shall, within twenty (20) days of the entry of this Order, pay a civil money penalty in the amount of \$7,650,000 to the Securities and Exchange Commission. If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. 3717. Payment must be made in one of the following ways:

- (1) BAC may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
- (2) BAC may make direct payment from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>; or

- (3) BAC may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center  
Accounts Receivable Branch  
HQ Bldg., Room 181, AMZ-341  
6500 South MacArthur Boulevard  
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying BAC as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Michael J. Osnato, Chief, Complex Financial Instruments Unit, Division of Enforcement, Securities and Exchange Commission, 200 Vesey Street, Suite 400, New York, New York 10281.

By the Commission.

Brent J. Fields  
Secretary