Bank of America agreed to pay $33 million to settle a civil lawsuit alleging that it misled shareholders about billions of dollars in bonuses promised to Merrill Lynch & Co. employees when it bought the troubled firm at the height of the financial crisis last year.

The takeover of Merrill cost Bank of America Chief Executive Kenneth Lewis his title as chairman and threw his future at the bank into doubt. The 62-year-old Mr. Lewis, trying to hold on as CEO until his planned retirement in about two years, separately launched on Monday a five-way competition to succeed him with a management shake-up that included hiring former Citigroup Inc. Chief Financial Officer Sallie Krawcheck.

Bank of America, the largest U.S. bank in assets, neither admitted nor denied wrongdoing in settling the lawsuit, describing the agreement with the Securities and Exchange Commission as a “constructive conclusion” to the matter. The case reflects the SEC’s heightened effort to speed up cases, as new SEC Chairman Mary Schapiro and new enforcement director Robert Khuzami take a harder line with companies and individuals under investigation.

The size of the Merrill bonuses sparked outrage on Main Street and became a symbol of outsized compensation to Wall Street executives who had taken excessive risk but were nevertheless getting bailed out by taxpayers. Bank of America insisted that it hadn’t blessed the payments and was pressed by federal regulators into closing the Merrill deal.

The settlement marks a new low point for Mr. Lewis, a man once considered one of the industry’s best deal makers. Last December, just before the Merrill deal closed, American Banker named him “Banker of the Year.” But by the end of January, Bank of America was sparring with federal regulators over the terms of the Merrill bailout which the bank considered to be too onerous. In April, Mr. Lewis lost his chairmanship as investors blamed him for the decision to buy Merrill despite mounting losses. Many of his backers on the bank’s board left amid a regulatory sanction requiring new governance and controls on risk and liquidity management. For John Thain, the former Merrill chairman and CEO ousted by Mr. Lewis shortly after the deal was completed, the settlement offers some measure of vindication. Bank of America had accused Mr. Thain of deciding on his own to pay bonuses to Merrill employees. Mr. Thain had said the bonuses were awarded in consultation with Bank of America. He couldn’t be reached for comment Monday.

The SEC complaint, filed Monday in U.S. District Court in New York, found fault with proxy documents that Bank of America and Merrill sent to their respective shareholders in November 2008 to vote on the $50 billion takeover. The documents said Merrill wouldn’t pay year-end bonuses or other compensation before the deal closed without Bank of America’s consent.

In reality, according to the SEC complaint, Bank of America had already “contractually authorized” Merrill to pay up to $5.8 billion in bonuses, or 12% of the total deal price. That deal was written in a separate document and was never distributed to shareholders voting on the deal, the complaint said.

On Dec. 5, shareholders of both firms approved the sale. Three days later, Merrill’s compensation committee approved $3.6 billion in bonuses. Merrill employees received their bonuses on Dec. 31, one day before the deal closed. Merrill reported a net loss of $27.6 billion for 2008.

The SEC alleges that given the size of the bonuses and Merrill’s deteriorating condition, the alleged separate deal was material information investors should have known about at the time of the vote. Bank of America has said that the decision to pay the bonuses was ultimately Merrill’s.
State and federal investigators are also probing Bank of America over whether it should have disclosed that Merrill’s financial condition had deteriorated as the deal was being finalized. It wasn’t until mid-December, more than a week after shareholders approved the merger, that Mr. Lewis told regulators he might pull out of the deal. The U.S. ultimately provided an additional $20 billion to push the deal forward, making Bank of America the second largest recipient of bank bailout funds after Citigroup.

The $33 million payment is steep for disclosure-related cases where fraud isn’t alleged. In 2004, Wachovia Corp. agreed to a $37 million settlement of allegations that it didn’t sufficiently disclose stock purchases related to a takeover, among other matters. Wachovia didn’t admit or deny any wrongdoing.

On Monday, an SEC official said Bank of America’s taxpayer-funded assistance “was not a factor” in determining the settlement amount.

Mr. Lewis told investors last month that he wants to keep his job until Bank of America repays $45 billion in aid from the U.S. government, adding that he is “the one most capable of getting us to the other side.” While the company’s board still is backing him, partly because of the lack of an obvious successor, some directors have been pressing for a stronger list of CEO candidates that will have time to prove themselves, according to people familiar with the situation.

Ms. Krawcheck, 44, is one of the highest-profile outside hires by Mr. Lewis. She led Citigroup’s wealth-management group before stepping down late last year following months of tension with Chief Executive Vikram Pandit. The global wealth and investment management unit she will run at Bank of America includes much of the former Merrill.

“I wouldn’t be going to Bank of America if I didn’t believe these would be winners through the cycle,” Ms. Krawcheck said in an interview. “It’s clear that as we come out of the recession, there are going to be big opportunities in financial services. These businesses are well-positioned to take advantage of those opportunities.”

Mr. Lewis gave expanded duties to newcomer Thomas Montag, the head of global sales and trading at Merrill when it was bought by Bank of America. Mr. Montag, now head of global markets at the giant bank, also will be in charge of global corporate and investment banking.

Mr. Montag ran the part of Merrill that piled up the brunt of the company’s $15.31 billion net loss in the fourth quarter, and he was owed a guaranteed payout of $39.4 million for 2008.

At Bank of America, Mr. Montag’s global markets business has been one of the best performers through the first two quarters, and he has worked to keep key people in top positions amid a rocky integration of the two firms. There was recent concern that he might leave, which contributed to Mr. Lewis’s decision to give him a bigger job, according to one person familiar with the matter. Through a spokesman, Mr. Montag declined to comment.

Mr. Montag and Ms. Krawcheck likely face an uphill battle for the CEO job against longtime Bank of America executives Brian Moynihan, Barbara Desoer and Joe Price, all of whom are viewed within the bank as contenders for Mr. Lewis’s job. Mr. Moynihan, a lawyer who held the job being taken by Ms. Krawcheck, now will run the huge consumer bank and credit-card business at Bank of America, essentially the heart of the company.

The new duties will give Mr. Moynihan experience in nearly every part of Bank of America’s business. He joined the bank as part of a 2004 merger with FleetBoston Financial Corp. Ms. Desoer is keeping her current job as president of home loans and insurance, including the former Countrywide Financial Corp., while Mr. Price remains chief financial officer. Through a spokesman, all three declined to comment. The board could also still turn to an outside candidate if the internal choices do not work out.

Liam McGee, who ran the bank’s consumer and small-business banking unit, is leaving Bank of America, the company announced. One person familiar with the discussions said it had become clear to Mr. McGee that he wouldn’t become CEO. Mr. McGee couldn’t be reached for comment Monday, but a spokesman for the bank said “it was his decision” to leave.

In a statement, Mr. Lewis said the changes bring “new talent . . . new perspectives” to Bank of America and “also position a number of senior executives to compete to succeed me at the appropriate time.”

— Robin Sidel and Chad Bray contributed to this article.
A Federal District judge on Monday overturned a settlement between the Bank of America and the Securities and Exchange Commission over bonuses paid to Merrill Lynch executives just before the bank took over Merrill last year.

The judge said that Bank of America “materially lied” in shareholder communications about the bonuses.

The $33 million settlement “does not comport with the most elementary notions of justice and morality,” wrote Jed S. Rakoff, the judge assigned to the case in federal court in Lower Manhattan. The ruling directed both the agency and the bank to prepare for a possible trial that would begin no later than Feb. 1.

The case involved $3.6 billion in bonuses that were paid by Merrill Lynch late last year, just as that firm was about to be merged with Bank of America. Neither company provided details of the bonuses to their shareholders, who voted on Dec. 5 to approve the merger.

The judge focused much of his criticism on the fact that the fine in the case would be paid by the bank's shareholders, who were the ones that were supposed to have been injured by the lack of disclosure.

“It is quite something else for the very management that is accused of having lied to its shareholders to determine how much of those victims’ money should be used to make the case against the management go away,” the judge wrote.

In a statement, the S.E.C. said on Monday: “As we said in our court filings, we believe the proposed settlement properly balanced all of the relevant considerations. We will carefully review the court’s most recent order.”

A spokesman for the bank, Lawrence Di Rita, said the bank disagreed with the judge's ruling.

“Bank of America believes the facts demonstrate that proper disclosure was made to shareholders about Merrill bonuses,” Mr. Di Rita said in an e-mail message. “We are prepared to prove that through litigation. We will consider all our legal options over the coming days.”

The judge also criticized the S.E.C., which has been trying to step up the effectiveness of its investigations unit. The judge quoted Oscar Wilde’s “Lady Windermere’s Fan” in the end of his ruling to say that a cynic is someone “who knows the price of everything and the value of nothing.”

The proposed settlement, the judge continued, “suggests a rather cynical relationship between the parties: the S.E.C. gets to claim that it is exposing wrongdoing on the part of the Bank of America in a high-profile merger; the bank's management gets to claim that they have been coerced into an onerous settlement by overzealous regulators. And all this is done at the expense, not only of the shareholders, but also of the truth.”

The case before Judge Rakoff is just one of several investigations into the bank’s deal with Merrill. Andrew M. Cuomo, the attorney general of New York, is also investigating the bank’s disclosures of bonuses and of Merrill’s surprise losses late last year. The House Committee on Government Oversight and Reform is also looking into the merger.

It is not the first time Judge Rakoff has ruffled feathers in the business world. In 2003, for example, he refused to approve what he saw as a low settlement the S.E.C. had negotiated with WorldCom, the phone company that collapsed in an $11 billion accounting fraud.

Rewarding — and punishing — the right parties was at the fore of the judge's thinking in that case. Shareholders of WorldCom had already lost out. So when the judge forced the S.E.C. to increase the $500 million fine it was levying against WorldCom to $750 million, he also demanded that the money be paid out to the company’s shareholders, rather than to the agency.