UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

IN RE BANK OF AMERICA CORP. SECURITIES, DERIVATIVE, AND EMPLOYMENT RETIREMENT INCOME SECURITY ACT (ERISA) LITIGATION	Master File No. 09 MDL 2058 (DC)
	ECF CASE
THIS DOCUMENT RELATES TO:	
All Securities Actions	

LEAD PLAINTIFFS' OMNIBUS OPPOSITION TO DEFENDANTS' MOTIONS TO DISMISS THE CONSOLIDATED CLASS ACTION COMPLAINT

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Court-appointed Lead Plaintiffs the State Teachers Retirement System of Ohio, the Ohio Public Employees Retirement System, the Teacher Retirement System of Texas, Stichting Pensioenfonds Zorg en Welzijn, represented by PGGM Vermogensbeheer B.V., and Fjärde AP-Fonden (collectively, "Plaintiffs"), submit this consolidated memorandum of law in opposition to Defendants' three motions to dismiss the Consolidated Amended Class Action Complaint (the "Complaint") pursuant to Fed. R. Civ. P. 8, 9(b), 12(b)(1)[1] and 12(b)(6).[2]

PRELIMINARY STATEMENT

For many years, Bank of America Corp. ("BoA") sought a presence on Wall Street to validate its position as a leader in the global banking community. In September 2008, BoA was presented with an opportunity to acquire the company it had coveted for years: Merrill Lynch & Co. ("Merrill"). The subprime mortgage meltdown had caused Lehman Brothers ("Lehman") to file for bankruptcy, and banking insiders believed that Merrill was the next investment bank to fall. Accordingly, at the federal government's insistence, Merrill sought a merger partner, and after performing a mere two days of due diligence, BoA agreed to purchase Merrill in a stock-for-stock transaction valued at $50 billion. The planned merger was announced to the public on September 15, 2008.

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[1] Defendants have referenced Fed. R. Civ. P. 12(b)(1) in their notice of motion and the title of their brief but do not appear to make any arguments for dismissal under that rule.

[2] The Defendants named in this action are Bank of America Corp. ("BoA"), Kenneth D. Lewis, BoA's former Chief Executive Officer, President and Chairman of the Board ("Lewis"), Joe L. Price, BoA's Chief Financial Officer ("Price"), Neil A. Cotty, BoA's Chief Accounting Officer ("Cotty" and along with BoA, Lewis and Price, collectively, the "BoA Defendants"); Merrill Lynch & Co. Inc. ("Merrill"); John A. Thain, Merrill's former Chief Executive Officer and Chairman of the Board ("Thain"); members of BoA's Board of Directors, including William Barnet III, Frank P. Bramble, Sr., John T. Collins, Gary L. Countryman, Tommy R. Franks, Charles K. Gifford, Monica C. Lozano, Walter E. Massey, Thomas J. May, Patricia E. Mitchell, Thomas M. Ryan, O. Temple Sloan, Jr., Meredith R. Spangler, Robert L. Tillman, and Jackie M. Ward (collectively, the "BoA Board"); Banc of America Securities LLC, BoA's broker dealer subsidiary ("BAS"), and Merrill Lynch, Pierce, Fenner & Smith Inc., Merrill's broker-dealer subsidiary ("MLPFS" and collectively with BAS, the "Underwriter Defendants").

The gravamen of this case is that Defendants made false and misleading statements and failed to disclose extraordinarily material facts to investors both before and after the shareholder vote approving the most important merger in BoA's history. During the merger negotiations, BoA agreed to allow Merrill to pay up to $5.8 billion in bonuses to its executives and employees on an accelerated basis, before the merger closed, and regardless of Merrill's financial condition. Notwithstanding the fact that the bonus agreement was a material term of the transaction – Thain stated that it was one of the three "main things" the parties negotiated, and the $5.8 billion bonus cap was equivalent to 12% of the total merger consideration – the proxy issued to shareholders failed to disclose this agreement. To the contrary, the proxy represented that Merrill would not pay any bonuses prior to the close of the merger without BoA's consent, without disclosing that such consent had already been given.

In addition, in the two months preceding the shareholder vote, Merrill suffered losses so large that they threatened its own solvency and BoA's ability to complete the transaction. In October 2008 alone, Merrill lost $7 billion and, by the date of the vote, its losses had grown to $15.3 billion. These losses were so massive that BoA lacked the capital to absorb them and, during the weeks leading up to the vote, BoA's most senior executives internally debated terminating the merger by invoking the "material adverse effect" clause ("MAC") in the Merger Agreement. At the same time, BoA was in the midst of suffering its own loss for the quarter of $1.8 billion – the largest quarterly loss in its own history. Once again, however, despite the obvious importance of this information, and notwithstanding Defendants' repeated statements praising the merger and assuring investors about Merrill's and the combined entity's financial condition, Defendants did not disclose Merrill's or BoA's losses to investors at any time before the shareholder vote. Thus, on December 5, 2008, BoA shareholders voted overwhelmingly to

approve the transaction, completely unaware that the merger threatened to render BoA insolvent.[3]

Defendants' egregious violations of the securities laws continued after the vote. Just days later, Defendant Lewis informed U.S. Secretary of the Treasury Henry Paulson ("Secretary Paulson") that, because of Merrill's enormous losses, BoA had determined that a MAC had occurred, and it planned to terminate the merger. Federal Reserve Chairman Benjamin Bernanke ("Chairman Bernanke") told Lewis in no uncertain terms that, if Lewis did so, the market would realize that Lewis's prior statements assuring investors about the due diligence undertaken and the purported benefits of the merger were false. Secretary Paulson bluntly threatened that Lewis and the BoA Board would be terminated. Lewis then agreed to proceed with the merger, but only after BoA secured the Government's commitment to provide a taxpayer bailout totaling $138 billion to backstop Merrill's losses. Although the Merger Agreement and BoA's and Merrill's Definitive Joint Proxy (the "Joint Proxy") assured shareholders that there was no material adverse change in Merrill's financial condition at any time prior to the close of the merger, BoA never disclosed that the opposite was true. Nor did BoA disclose that the only way it could complete the deal was to secure a massive taxpayer bailout. To the contrary, Lewis played fast and loose with the securities laws by not memorializing the deal with the Government because he believed that if he did, BoA would have to publicly disclose it – which, as Lewis stated in one email to the BoA Board, "of course we do not want."

News of Merrill's massive losses began to leak in January 2009, and when BoA finally disclosed the truth about the merger, it caused what *The New York Times* has called "one of the

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[3] During this same time frame, BoA raised almost $10 billion from investors pursuant to a materially false and misleading Registration Statement and Prospectus that similarly failed to disclose and/or misrepresented much of the same information. Consequently, this conduct serves as the basis for Plaintiffs' claims against certain Defendants pursuant to the Securities Act of 1933.

greatest destructions of shareholder value in financial history." Indeed, in just a handful of days in mid-January, BoA's common stock lost more than half its value, destroying more than $50 billion in market capitalization. The aftermath of these disclosures continues to be devastating to BoA, which faces a raft of ongoing criminal and civil investigations arising from its merger-related statements and omissions, including investigations by Congress, the Securities and Exchange Commission (the "SEC") and the New York Attorney General (the "NYAG").

The SEC has sued BoA in this District, alleging, as Plaintiffs do, that BoA violated Section 14(a) of the Securities Exchange Act of 1934 (the "Exchange Act") by failing to disclose the bonus agreement. Tellingly, BoA did not even move to dismiss that case – even though its allegations are substantively identical to those at issue here – and instead settled the SEC Action for $33 million. Judge Rakoff flatly rejected that settlement as inadequate, and the trial in the SEC Action is scheduled to begin on March 1, 2010. Similarly, in a derivative action pending against Lewis and the BoA Board in the Delaware Chancery Court, Vice Chancellor Strine recently rejected virtually identical arguments that Defendants make in their motions here, and held that the facts alleged gave rise to the inference that Lewis and the BoA Board acted in "bad faith" in failing to disclose the bonus agreement and Merrill's losses.

Nevertheless, in their motions, Defendants ask the Court to conclude at the pleading stage, as a matter of law, that none of these facts were material to BoA's shareholders or investors and that, in any event, Defendants had no obligation to disclose any of these facts. According to Defendants, shareholders voting on a merger are not entitled to know that approval of the merger will potentially render the combined company insolvent, or that the target company has secretly been given permission to pay billions of dollars in discretionary bonuses on an accelerated basis. These arguments make a mockery of the federal securities laws.

Contrary to what Defendants contend, the Second Circuit has been crystal clear that a company seeking shareholder approval of a merger must "fully and fairly furnish[] all the objective material facts" related to that transaction so that shareholders can "make an informed investment decision." *Mendell v. Greenberg*, 927 F.2d 667, 674 (2d Cir. 1990). This duty exists up to the date of the shareholder vote – as former Chief Judge Friendly held more than thirty years ago, there is "no doubt' that a defendant is required to disclose "facts arising since [the proxy's] dissemination if these are so significant as to make it materially misleading." *Gerstle v. Gamble-Skogmo, Inc.*, 478 F.2d 1281, 1297 n.15 (2d Cir. 1973). It is absurd to argue, as Defendants do, that the secret bonus agreement and Merrill's massive losses – which caused BoA's own executives to debate terminating the Merger Agreement in the weeks leading up to the vote – was information that investors being asked to approve the merger would not have considered important.

Recognizing the fallacy of this argument, Defendants make a series of additional arguments that should be swiftly rejected. Defendants argue, *inter alia*, that investors were not permitted to rely on the representations in the Merger Agreement and Proxy regarding bonuses and Merrill's financial condition; Defendants followed "customary" disclosure practices in not disclosing this information; the market was supposedly well aware of the secret bonus agreement and Merrill's losses; investors were warned that market conditions were impacting Merrill; and Defendants were not required to disclose Merrill's intra-quarter losses. As set forth herein, each of these arguments is demonstrably incorrect, for they ignore (i) the well-established disclosure obligations that govern proxy solicitations in the context of a merger, (ii) the fact that Defendants made affirmative misrepresentations about these very subjects when soliciting shareholder approval of the merger, and (iii) the market's reaction when investors finally learned about what

Lewis himself called Merrill's "stunning" losses and the secret bonus agreement. At a minimum, these arguments raise fact issues that cannot be resolved at this stage of the litigation.

Defendants' challenges to Plaintiffs' Section 10(b) claims similarly fail. Defendants' principal argument in response to these claims is that they were not required to disclose the taxpayer bailout or the circumstances that required it because Lewis chose not to sign the agreement with the Government before the merger closed – a decision he made for the express purpose of concealing the agreement from BoA's investors. Remarkably, Defendants ask the Court to credit this conduct, and to permit Defendants to escape liability based on an orchestrated, conscious attempt to exploit perceived technicalities in the law. However, the law is not so easily evaded. Whether or not Lewis formally memorialized BoA's agreement with the Government prior to the close of the merger is irrelevant – the bailout agreement was firm, and the securities laws required these material facts to be disclosed.

Defendants' scienter arguments are equally unavailing. Notably, Defendants do not dispute that they knew the undisclosed facts at issue – a concession that, by itself, establishes their scienter for the purposes of the Complaint's Section 10(b) claims. Indeed, Lewis was so conscious of his potential liability to shareholders that, prior to the close of the merger, he asked the Government to "immunize" him from shareholder suits, which it refused to do. Unable to disclaim knowledge of the underlying facts, Defendants instead argue that they did not know they had a duty to disclose them. Even if the Court could plausibly assume that Defendants had "no clue" that they were required to disclose facts of tremendous significance in advance of the most important transaction in BoA's history, ignorance of the law is no defense to liability under Section 10(b). *See, e.g.*, *U.S. v. O'Hagan*, 139 F.3d 641, 647 (8th Cir. 1998).

In sum, Defendants' motions to dismiss the Complaint should be denied in their entirety.

FACTUAL BACKGROUND

A. BoA Hastily Seizes The Opportunity To Acquire Merrill

On the morning of Saturday, September 13, 2008, Merrill CEO John Thain reached out to the man who had "long coveted" and, in his own words, "drooled" over Merrill – BoA's CEO, Ken Lewis. ¶¶59, 63. As Thain realized, Lehman's imminent bankruptcy would almost certainly trigger Merrill's own collapse, as a result of the large "amount of bad assets on [Merrill's] balance sheet." ¶62. In an effort to prevent Merrill from succumbing to the same fate as Lehman, Thain initiated a meeting with Lewis. ¶62. Lewis, who had been rebuffed in his prior attempts to acquire Merrill, jumped at the opportunity, immediately flying to New York to meet with Thain. ¶¶5, 63-64. Within one day, Lewis and BoA agreed to acquire Merrill in one of the largest mergers in Wall Street history. ¶5. BoA agreed to pay $29 per share in stock to acquire Merrill – a total of $50 billion – a price that represented a substantial 70% premium to Merrill's closing price on September 12. ¶¶5, 66.[4]

Unbeknownst to shareholders, the parties spent much of their severely limited time that weekend negotiating the massive bonuses that Merrill executives and employees would receive as part of the deal. ¶¶67-72. Indeed, Thain himself has acknowledged that the bonuses were one of the three "main things" that the parties negotiated, with both Lewis and Thain being kept apprised of the bonus negotiations as they occurred. ¶67. The heated negotiations over the bonuses dragged on for hours, delaying the signing of the Merger Agreement until almost 2 a.m. on Monday, September 15. ¶71.

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[4] Although Defendants claim that Plaintiffs are challenging their "business judgment" in agreeing to the merger at too high of a price (BoA Mem. 1-2), Plaintiffs do not challenge Defendants' right to agree to the merger or the exchange ratio. Instead, Plaintiffs' claims are directly based on the host of materially false and misleading statements and omissions that Defendants made to shareholders in connection with the merger, and thus plead violations of the securities laws, as explained herein.

Ultimately, BoA agreed to allow Merrill to pay up to $5.8 billion of bonuses to its executives and employees before the merger closed. ¶72. This sum was equivalent to 12% of the value of the merger, represented 30% of the value of Merrill's stockholders' equity as of December 26, 2008, and was 26% larger than the amount that BoA had earned during the first half of 2008. ¶72. Moreover, it was $700 million ***more*** than Merrill had planned for its 2008 bonuses before the merger negotiations began. ¶73. The fact that BoA agreed to allow Merrill to pay the bonuses prior to the merger's scheduled closing date of January 1, 2009 – which was ahead of Merrill's normal schedule and contrary to its publicly-stated compensation policy – ensured that Merrill would exercise control over the payments, permitting its executives and employees to reap gigantic bonuses regardless of Merrill's financial performance. ¶¶75-77.

B. The Merger Is Announced

On September 15, 2008, Lewis, Thain, and BoA's CFO, Joe Price, publicly announced the merger. ¶79. In a press release, investor call, and press conference that day, these Defendants recommended the deal to BoA shareholders and investors in glowing terms, stating that it was "the strategic opportunity of a lifetime," would "creat[e] more value for shareholders," and, in sum, was "just a major grand slam homerun." ¶191. They also made a series of statements designed to assuage investor concern over BoA's due diligence and Merrill's financial condition, and assure investors that there had been no pressure from regulators to hastily finalize the deal. ¶79. Analysts and investors relied on these statements to conclude that the Government had exerted no pressure on the parties, BoA had "closely studied" and become "very familiar" with Merrill's financial condition, and that Merrill was "in stronger condition than thought." ¶195.

C. The Secret Bonus Agreement

On September 18, 2008, BoA and Merrill both filed the Merger Agreement with the SEC on Forms 8-K which explained that the Merger Agreement was being disclosed to investors so they could understand the terms of the transaction. ¶82. Although BoA's agreement to allow Merrill to pay up to $5.8 billion in bonuses was an express term of the merger, it was not disclosed in the Merger Agreement. ¶82. To the contrary, the Merger Agreement falsely represented to investors that Merrill could ***not*** pay discretionary bonuses before the merger closed without obtaining BoA's consent. ¶196. Specifically, in a section titled "Company Forbearances," the Merger Agreement provided that "except as set forth in Section 5.2 of the Company Disclosure Schedule or except as expressly contemplated or permitted by this Agreement," from September 15, 2008 through January 1, 2009, Merrill "***shall not*** …, without the prior written consent of [BoA]," undertake any of eighteen enumerated actions, including, "increase in any manner the compensation or benefits" of employees, or "pay any amounts to Employees … ***other than base salary***."[5] ¶196. Nowhere did the Merger Agreement disclose that BoA's "prior written consent" had already been obtained to allow Merrill to pay up to $5.8 billion in discretionary bonuses, that this consent was embodied in the "Company Disclosure Schedule," or that such payment would occur before the merger closed, regardless of Merrill's 2008 financial performance. ¶197. The ironically-named Company Disclosure Schedule, which described the $5.8 billion bonus agreement, was never made public during the Class Period. ¶198.

D. Merrill's Undisclosed Losses Prior To The Shareholder Vote

In the weeks following the merger announcement, Defendants continued to reassure investors that the financial condition of both companies was strong, and to recommend the

[5] Throughout this memorandum, all emphasis is added unless otherwise noted.

merger as a means to create shareholder value. For example, on October 7, 2008, BoA issued a press release in connection with a $9.9 billion secondary offering of common stock (the "Offering") which underscored BoA's "strength and stability" and stated that the merger "should significantly enhance our earnings." ¶83. On a related investor call, Price specifically responded to a question regarding the need for any additional capital in connection with the merger by stating that none would be necessary. *Id.* Likewise, when Merrill announced its third quarter results on October 16, Thain stated that Merrill continued to "reduce exposures and de-leverage the balance sheet" in connection with the merger, which would "create an unparalleled global company with pre-eminent … earnings power." ¶84. Analysts relied on these statements to conclude that Merrill had substantially resolved the problems that had caused it to incur large losses in 2007 and the first three quarters of 2008, and projected that Merrill would make a profit of $0.44 to $0.54 per share in the fourth quarter. ¶203.

Contrary to Defendants' public statements, during October and November 2008 – as BoA and Merrill continued to solicit shareholder approval for the merger – Merrill suffered massive losses. It lost $7 billion in October alone, the worst month in Merrill's history, and continued to suffer billions more in losses in November. ¶¶88-89. According to an independent expert analysis of Merrill's weekly loss data conducted by Congress, Merrill had losses of at least another $2 billion by November 14 – and its losses were clearly ***accelerating***. ¶89. By the end of November 2008, with the shareholder vote less than a week away, "internal calculations showed that Merrill had a horrifying pre-tax loss of $13.3 billion, and December was looking even worse." ¶90. In addition, Merrill had determined that "it needed to take a goodwill charge of approximately $2 billion" due to the collapse of its subprime mortgage lending subsidiary. ¶91. Including this $2 billion goodwill impairment, Merrill's losses by the end of November

2008 totaled ***$15.3 billion***. *Id.* These losses – which were not disclosed at any time prior to the close of the merger – were large enough to bankrupt Merrill, and so large that BoA did not have the capital to absorb them. ¶92.

Defendants Lewis, Price, Cotty, and Thain knew of or recklessly disregarded these losses as they occurred. Immediately after announcing the merger, Cotty (BoA's Chief Accounting Officer) became Merrill's interim CFO, and acted as a direct liaison between Merrill and Lewis and Price. ¶93. According to Thain, he discussed Merrill's losses during meetings each Monday with Cotty and, thus, Cotty was "totally up-to-speed on what was happening" throughout the fourth quarter. ¶94. Similarly, Thain stated that BoA's senior executives "were getting [our] daily profit and loss statement" and had full knowledge of Merrill's losses "step by step" during the fourth quarter. ¶95. Indeed, Lewis, who along with Price regularly "updated" BoA's Board on Merrill's losses during weekly conference calls, admitted to Congress that he received "detailed financial reports" regarding Merrill "every week" and that Merrill's losses were "clear" before the shareholder vote. ¶¶97, 99.

Significantly, Merrill's losses in October and November 2008 were so large that, beginning on November 20 – more than two weeks before the shareholder vote – BoA's senior executives repeatedly debated invoking the MAC in the Merger Agreement, which would have permitted BoA to terminate the transaction upon a material adverse change in Merrill's financial condition. ¶101. Certain BoA executives insisted that, even if BoA was not going to invoke the MAC, shareholders should be told of the losses so they could cast their vote with full knowledge of the relevant facts. ¶102. These "debates" continued up until the day of the shareholder vote, and on each occasion, BoA's senior executives made the deliberate "decision not to disclose these escalating losses." ¶¶101-102.

As Merrill was collapsing, BoA's own financial condition was materially deteriorating to the point where BoA would be unable to absorb the losses suffered by Merrill. ¶103. Indeed, by the time of the shareholder vote, BoA had already suffered $800 million in losses, and was projecting a total loss for the quarter of $1.4 billion – the first quarterly loss in its history. *Id.* Further, as BoA's senior executives later acknowledged to federal regulators, BoA was so "very thinly capitalized" that regulators reviewing BoA's financials concluded that it was "clearly not [] well prepared for any further deterioration." *Id.*

E. The Joint Proxy

On November 3, 2008, BoA and Merrill mailed the Joint Proxy and attached Merger Agreement to shareholders and filed it with the SEC. ¶107. The Joint Proxy omitted any mention of the $7 billion in losses that Merrill had suffered by this date. *Id.* Instead, the Joint Proxy represented that that there was "an absence of material changes" in Merrill's financial condition – a representation that the attached Merger Agreement assured investors would remain true "as of" the merger's January 1, 2009 closing date – and stated that the "strong capital position" of the combined company was a "material factor" favoring the merger. *Id.*

The Joint Proxy also omitted any mention of the agreement allowing Merrill to pay up to $5.8 billion in bonuses before the merger closed. ¶108. Instead, it identified the payment of discretionary bonus compensation as an "extraordinary action," and reiterated that "Merrill Lynch will ***not***" make any discretionary bonus payments before the merger closed without BoA's "prior written consent." *Id.* The Joint Proxy further stated that BoA's "written consent" "will not be unreasonably withheld or delayed," indicating that no consent had been given. ¶216. The Joint Proxy also expressly incorporated by reference Merrill's March 2008 Proxy, which informed investors that Merrill's executive bonuses were "paid in January for performance in the prior fiscal year" and provide "an integral link between pay and performance." ¶108.

In the weeks after the Joint Proxy was mailed to shareholders, BoA and Merrill updated it at least twice, without disclosing ***any*** material facts concerning the growing losses at Merrill and BoA, or the bonus agreement. ¶109. In particular, on November 26, 2008 – with the vote less than 10 days away, and while BoA's senior executives were debating internally whether to terminate the merger – BoA supplemented the Joint Proxy with a letter from Lewis to shareholders ("November 26 Letter"). The November 26 Letter recognized investors' "deep concerns about . . . whether financial institutions have enough capital," but assured them that BoA was "one of the strongest and most stable major banks in the world." ¶111. There was no mention in the letter of Merrill's huge losses, BoA's $800 million loss, or the secret bonus agreement.

On December 5, 2008, BoA's shareholders convened in Charlotte to vote on the merger. ¶112. Having heard for months about the benefits of the merger from Defendants – but oblivious to, *inter alia*, Merrill's massive fourth-quarter losses (which were now at least $16 billion), BoA's own weakened financial condition, and the undisclosed bonus agreement – BoA's shareholders voted overwhelmingly to approve the merger. ¶¶112, 174. Immediately after the vote, Lewis represented that the merger was the crowning achievement in BoA's history, stating that it would create the "premier financial services franchise" in the world. ¶112.

F. The Decision To Invoke The MAC, Paulson's Threat, And The Taxpayer Bailout

Two business days after the shareholder vote, Lewis and Price met with the BoA Board to discuss Merrill's alarming financial condition. ¶113. Relying on loss figures circulated among BoA's and Merrill's executives before the shareholder vote, Price told the BoA Board that the magnitude of Merrill's losses was "quite significant." *Id.* Just days later, BoA considered terminating the merger. *Id.* In a meeting on December 17 with Secretary Paulson

and Federal Reserve Chairman Bernanke, just two weeks before the merger was to close, Lewis and Price explained that, given BoA's own financial deterioration, Merrill's losses would devastate BoA's tangible common equity and Tier 1 capital ratios, making it impossible for BoA to absorb these losses and close the merger. ¶115. Lewis further explained that Merrill's massive losses – which he falsely claimed to have only learned of in mid-December, after the shareholder vote – constituted a material adverse change in Merrill's financial condition, and that BoA accordingly planned to terminate the merger. ¶115. Alternatively, Lewis suggested that a taxpayer bailout of BoA, including an asset guarantee of tens of billions of dollars, might salvage the deal, and agreed to provide the Federal Reserve with information on Merrill's and BoA's fourth quarter performance for its consideration. ¶116.

After reviewing Merrill's internal data, senior Federal Reserve officials concluded that Merrill's financial deterioration had been "observably underway the entire quarter," and Lewis's claim of surprise regarding Merrill's losses was "not credible." ¶117. At a minimum, they concluded, it cast serious doubt on the adequacy of BoA's due diligence. ¶¶117, 122. On December 19, 2008, Lewis and Price again informed Secretary Paulson and Chairman Bernanke that BoA planned to invoke the MAC. ¶124. Paulson and Bernanke urged Lewis not to take this step, with Bernanke warning Lewis that invoking the MAC "after three months of review … and public remarks by the management of [BoA] about the benefits of the acquisition would cast doubt in the minds of financial market participants . . . about the due diligence and analysis done by the company, its capability to consummate significant acquisitions, its overall risk management processes, and the judgment of its management." ¶125. When Lewis continued to insist on invoking the MAC during a December 21 follow-up telephone call, Paulson bluntly threatened to fire Lewis and the BoA Board if BoA invoked the MAC. ¶126. The threat

worked. Lewis replied: “That makes it simple. Let’s de-escalate.” ¶127. BoA executives immediately began working with federal regulators to design a bailout package. ¶128.

The following day, Lewis – who privately admitted to Federal Reserve officials that BoA “did not do a good job of due diligence” and recognized that BoA’s shareholders would suffer for “two to three years” from his decision to proceed with the merger – took the astounding step of contacting Chairman Bernanke seeking an “immunity” letter certifying that the Government had “ordered him to proceed” with the merger “for systemic reasons,” which he could “use as a defense” in anticipated shareholder lawsuits. ¶¶122, 128-129. Bernanke denied Lewis’s request. ¶129.

On December 22, 2008, Lewis informed the BoA Board that the U.S. Government had agreed to provide BoA with a taxpayer bailout but that “there was no way the Federal Reserve and Treasury could send us a letter of any substance without public disclosure, ***which, of course, we do not want***.” ¶134. Instead, over the next week, BoA obtained “detailed oral assurances from federal regulators with regard to their commitment” and “documented those assurances with e-mails and detailed notes of management’s conversations with the federal regulators,” but made no public disclosure. ¶135. In fact, according to board minutes, so definitive was the agreement that BoA actually discussed and planned to time the announcement of the taxpayer bailout to coincide with BoA’s earnings release on January 20, 2009. ¶136.

On December 31, 2008 – its last day as an independent company – Merrill paid out the cash component of $3.6 billion in bonuses notwithstanding the fact that it had suffered more than $21 billion in fourth quarter losses and was on the brink of insolvency. ¶138. The merger closed the following day. ¶139. BoA issued a press release in connection with the closing, again

hailing the merger as having created a "premier financial services franchise" and announcing the "$7 billion in pre-tax expense savings" that BoA expected to achieve from the transaction. *Id.*

G. The Truth Is Revealed

Although news of BoA's and Merrill's poor fourth quarter results began to leak to the market on January 12, 2009, it was not until January 15 that *The Wall Street Journal* shocked investors with news that BoA would receive billions in taxpayer assistance to allow it to close its acquisition of Merrill. ¶¶141-43. In response, BoA moved its earnings call from January 20 to January 16. ¶143. During the call, BoA announced that: (i) Merrill had suffered a fourth quarter loss of more than $21 billion before taxes; (ii) BoA had suffered its own $1.8 billion loss; (iii) the U.S. Government was extending a $138 billion taxpayer bailout to BoA; and (iv) BoA was slashing its dividend from $0.32 to $0.01 per share to preserve capital. ¶¶139, 145.

As Lewis himself admitted, "the magnitude of the loss . . . at Merrill Lynch ***really stunned people***." ¶149. Indeed, Moody's downgraded BoA's credit ratings due to "the disclosure of substantial losses at Merrill Lynch" and Fitch downgraded Merrill's rating to "F" due to its "massive losses" and inability to "survive[] absent assistance provided by the U.S. Treasury." ¶150. On January 17, 2009, *The New York Times* and *The Wall Street Journal* reported that BoA's management had contemplated invoking the MAC after the shareholder vote, but was dissuaded by the Government from doing so, and that BoA's own weakened financial condition contributed to the need for the taxpayer bailout. ¶151.

In direct response to all of these disclosures, BoA shares lost more than half of their value, falling from a close of $12.99 on January 9, the trading day preceding the first corrective disclosure, to $5.10 on January 20 – a market capitalization loss of approximately ***$50 billion***. *The New York Times* described the loss as "one of the greatest destructions of shareholder value in financial history." ¶¶17, 154. Then, just before midnight on January 21, the *Financial Times*

disclosed Merrill's "unusual" accelerated bonus payments. ¶155. BoA stock fell an additional 15% on this news. ¶¶161, 268.

H. The Aftermath

The events surrounding the Merrill acquisition continue to impose substantial costs on BoA and its shareholders. Numerous government investigations have ensued – including investigations by Congress, the SEC, the NYAG, the North Carolina Attorney General, the TARP Inspector General, the FBI and the Department of Justice. These investigations have publicized further evidence of Defendants' violations of the federal securities laws. ¶¶162, 176. For example, as of September 8, 2009, the NYAG's investigation found "at least four instances in the fourth quarter of 2008 where [BoA] and its senior officers failed to disclose material non-public information to its shareholders," (i) "at least $14 billion" of Merrill's "losses prior to shareholder approval of the merger"; (ii) "a goodwill charge of more than $2 billion" which "was known of by November" 2008 but nevertheless lumped into Merrill's "purportedly 'surprising'" losses after the shareholder vote; (iii) BoA's determination that "it had a legal basis to terminate the merger because of Merrill's losses," which it reversed only "when the jobs of its officers and directors were threatened by senior federal regulators"; and (iv) Merrill's "accelerated bonus payments." ¶174.

The SEC brought a civil action, *SEC v. Bank of America Corp.*, 09-CV-06829 (JSR) (S.D.N.Y) ("SEC Action"), against BoA pursuant to Section 14(a) and Rule 14a-9, for making materially false and misleading statements in the Joint Proxy by failing to disclose the bonus agreement. Rather than contest these allegations, BoA agreed to settle the SEC Action for a $33 million fine. However, Judge Rakoff rejected the proposed settlement, holding that it was "neither fair, nor reasonable, nor adequate." ¶¶20, 175. BoA did not move to dismiss the SEC's

complaint, and instead answered on October 3, 2009. SEC Action, Dkt No. 43 ("Answer to Amended Complaint"). The SEC Action is continuing.

In April 2009, BoA shareholders – expressing their fury over Lewis's conduct in connection with the merger – voted to strip Lewis of his position as Chairman of the BoA Board, "the first time that a company in the Standard & Poor's 500-stock index had been forced by shareholders to strip a CEO of chairman duties." ¶19. Under fire for his conduct in connection with the merger, Lewis announced his intent to resign by the end of 2009.[6] The BoA Board has also been substantially overhauled, with at least ten members resigning. ¶¶19, 168. As Thain recently ruminated while discussing BoA's actions and their consequences: "One take away for you all is that it's really always better to just tell the truth." ¶177.[7]

ARGUMENT

I. PLEADING STANDARDS UNDER RULE 12(b)(6)

A Rule 12(b)(6) motion must be denied if the complaint in question "contain[s] sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'" *Ashcroft v. Iqbal*, 129 S.Ct. 1937, 1949 (2009).[8] In reviewing a complaint under Rule 12(b)(6), the court

[6] Dan Fitzpatrick and JoAnn S. Lublin, *Bank of America Chief Resigns Under Fire*, Wall Street Journal, Oct. 2, 2009.

[7] Defendants attempt to escape liability by paternalistically arguing that they knew best, as Merrill has contributed to BoA's profits as of September 30, 2009. See BoA Mem. 2, 9. There is, of course, no "innocence by hindsight" defense to violations of the federal securities laws, as BoA's performance more than nine months after the end of the Class Period is irrelevant to whether Defendants' statements and omissions were materially false and misleading ***at the time they were made***. Further, as noted above, the repercussions from the merger continue to adversely impact BoA, which remains subject to a slew of civil and criminal investigations.

[8] A court may consider, in addition to the complaint, exhibits, incorporated documents, and materials "that are integral to the plaintiff's claims, even if not explicitly incorporated by reference, and matters of which judicial notice may be taken, [including] the contents of documents that are required by law to be filed with the SEC." *In re Gildan Activewear, Inc. Sec. Litig.*, 636 F. Supp. 2d 261, 268 n.3 (S.D.N.Y. 2009), *recons. denied*, No. 08 Civ. 5048 (HB), 2009 WL 4544287 (S.D.N.Y. Dec. 4, 2009) (quotation and citations omitted). However, extraneous documents and "matters outside the pleadings" are not proper elements of a 12(b)(6) motion, and should be excluded from a court's review. *See* Fed. R. Civ. P. 12(d). Here, the BoA Defendants attached sixty-four exhibits to the instant motion to dismiss. The Court should exclude the news articles annexed to the Declaration of Jonathan E. Goldin, dated November 24, 2009 (and exhibits thereto) ("Goldin Dec.") that the BoA Defendants have picked from a handful of days within the months-long Class Period and set forth as proof of what investors knew at given times. *See* Goldin

must take all factual allegations as true and "draw[] all reasonable inferences in the plaintiff's favor." *Serby v. Town of Hempstead*, No. 08-0186-CV, 2009 WL 3416179, at *1 (2d Cir. Oct. 22, 2009). Ultimately, "the issue is not whether the plaintiff [] will prevail but whether the plaintiff is entitled to offer evidence to support its claims." *VTech Holdings Ltd. v. PricewaterhouseCoopers LLP*, 348 F. Supp. 2d 255, 261 (S.D.N.Y. 2004).

As set forth below, Plaintiffs have easily satisfied the pleading standards for each of their claims.

II. THE COMPLAINT ADEQUATELY ALLEGES CLAIMS UNDER SECTION 14(a) OF THE EXCHANGE ACT

Count V of the Complaint states a claim under Section 14(a) of the Exchange Act and Rule 14a-9 against Defendants for their materially false and misleading statements and omissions regarding, *inter alia*: (i) the bonus agreement; (ii) Merrill's debilitating losses; (iii) BoA's increasing financial instability; and (iv) the events that led BoA to debate prior to the shareholder vote whether to invoke the MAC and terminate the transaction. Count VI states claims for control person liability for the primary violations alleged in Count V. Defendants seek to dismiss both these claims on grounds that Plaintiffs have failed to meet the pleading standards of Rule 9(b) and the Private Securities Litigation Reform Act of 1995 ("PSLRA"), that Plaintiffs do not allege actionable false statements and omissions, and that Plaintiffs do not have standing to assert a claim under Section 14(a) because, purportedly, the claim is a derivative claim belonging to BoA. For the reasons set forth below, the Complaint adequately alleges Defendants' violations of Section 14(a).[9]

Dec. Exs. 29-33, 37, 41. Referenced nowhere in the complaint, these articles are patently "matter[s] outside the pleadings," Fed. R. Civ. P. 12(d), and are not the proper subject of judicial notice.

[9] Other than Thain, Defendants do not challenge, and thus concede, that Plaintiffs have otherwise adequately alleged the elements of a Section 20(a) claim in Count VI. Although Thain argues that Plaintiffs have not sufficiently alleged his "culpable participation" (Thain Mem. 10), culpable participation is not an element of a Section 20(a)

A. Pleading Standards And Elements Of A Claim Under Section 14(a) And Rule 14a-9 Of The Exchange Act

A plaintiff pleads a violation of Section 14(a) and Rule 14a-9 by alleging that: (1) a proxy statement contained a material misrepresentation or omission, which (2) caused plaintiffs' injury, and (3) that the proxy solicitation itself, rather than the particular defect in the solicitation materials, was an essential link in the accomplishment of the transaction. *Mills v. Electric Auto-Lite Co.*, 396 U.S. 375, 385 (1970).

Congress enacted Section 14(a) to "ensur[e] full and fair disclosure to shareholders" so that they may be "able to make an informed choice when they are consulted on corporate transactions." *Mills*, 396 U.S. at 381-85; *see also J.I. Case & Co. v. Borak*, 377 U.S. 426, 431 (1964) ("The purpose of [Section] 14(a) is to prevent management or others from obtaining authorization for corporate action by means of deceptive or inadequate disclosure in proxy solicitation"). A proxy statement "should honestly, openly and candidly ***state all the material facts***, making no concealment of the purposes for the proposals it advocates. Unlike poker where a player must conceal his unexposed cards, the object of a proxy statement is to put all one's cards on the table face-up." *Mendell*, 927 F.2d at 670. Rule 14a-9, promulgated under Section 14(a), aims to "preserv[e] for all shareholders who are entitled to vote . . . the right to make decisions based on information that is not false or misleading." *United Paperworkers Int'l Union v. Int'l Paper Co.*, 985 F.2d 1190, 1197-98 (2d Cir. 1993). The Supreme Court has repeatedly recognized Rule 14a-9's "broad remedial" and "prophylactic" purposes when ruling upon its scope and applicability. *See, e.g.*, *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 448 (1976) ("[P]articularly in view of the prophylactic purpose of the Rule and the fact that the

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claim. *See In re Parmalat Sec. Litig.*, 497 F. Supp. 2d 526, 532 (S.D.N.Y. 2007). However, even if required, Plaintiffs have more than adequately alleged culpable participation by Thain. *See* Section III.C., *infra*.

content of the proxy statement is within management's control, it is appropriate that . . . doubts be resolved in favor of those the statute is designed to protect.").

In the proxy solicitation context, "[a]n omitted or concealed fact is material when 'there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote.'" *Mendell*, 927 F.2d at 673 (citation omitted). The materiality of an alleged misstatement or omission "necessarily depends on all relevant circumstances of the particular case." *Ganino v. Citizens Utils.*, 228 F.3d 154, 162 (2d Cir. 2000); *In re Nortel Networks Corp. Sec. Litig.*, 238 F. Supp. 2d 613, 627 (S.D.N.Y. 2003) ("Allegations of materiality should not be considered in isolation.") (citation omitted). Consequently, whether an undisclosed fact is material is a mixed question of law and fact that is ordinarily entrusted to a jury. *See TSC Indus.*, 426 U.S. at 450; *In re Pfizer Inc. Sec. Litig.*, 584 F. Supp. 2d 621, 636 (S.D.N.Y. 2008) ("[M]ateriality is a flexible, fact based determination, generally a matter for the finder of fact."). Only where the facts at issue are "so obviously unimportant to a reasonable investor that reasonable minds could not differ on the question of their importance" is dismissal on materiality grounds justified. *Ganino*, 228 F.3d at 162; *In re NovaGold Res. Inc. Sec. Litig.*, 629 F. Supp. 2d 272, 292 (S.D.N.Y. 2009).[10]

B. Section 10(b) Pleading Standards Do Not Apply To Section 14(a) Claims

Defendants improperly conflate the pleading standards for Section 14(a) claims and Section 10(b) claims, arguing that, with respect to both claims, Plaintiffs must meet the heightened pleading standards for fraud under Rule 9(b) and the PSLRA, and, as such, plead scienter. BoA Mem. 30-33. They are wrong.

[10] Notably, Plaintiffs are not required to allege that the putatively material fact would have caused the investor to vote or act differently. *See TSC Indus.*, 426 U.S. at 449.

Section 14(a) claims, which sound in negligence, must be pled in accordance with Rule 8(a), not Rule 9(b). *Gerstle*, 478 F.2d at 1300, 1301 n.20 (holding that plaintiffs who "represent the very class who were asked to approve a merger on the basis of a misleading proxy statement and are seeking compensation from the beneficiary who is responsible for the preparation of the statement . . . are not required to establish any evil motive or even reckless disregard of the facts"); *Wilson v. Great American Indus., Inc.*, 855 F.2d 987, 995 (2d Cir. 1988) ("[P]reparation of a proxy statement by corporate insiders containing materially false and misleading statements or omitting a material fact is sufficient to satisfy the *Gerstle* negligence standard."); *Salit v. Stanley Works*, 802 F. Supp. 728, 733 (D. Conn. 1992) (for Section 14(a) claims, plaintiffs need not allege an "intent to deceive").

Section 21D(b)(1) of the PSLRA, which applies to all Exchange Act claims, requires plaintiffs to "specify each statement alleged to have been misleading [and] the . . . reasons why the statement is misleading." 15 U.S.C. §78u-4(b)(1)(B); *DCML LLC v. Danka Bus. Sys. PLC*, No. 08 Civ. 5829, 2008 WL 5069528, at *1 (S.D.N.Y. Nov. 26, 2008). However, because Section 14(a) has no state of mind element, Section 21D(b)(2) of the PSLRA, 15 U.S.C. §78u-4(b)(2), which concerns state of mind pleading requirements, does not apply to Section 14(a).

Defendants argue that Plaintiffs' Section 14(a) claims should nonetheless be subject to the Rule 9(b) pleading standard – and that Plaintiffs should also be required to plead scienter – because these claims: (i) are raised in the same complaint in which some of the Defendants are also sued for fraud; and (ii) employ the terms "material," "false" and "misleading" – terms which, of course, appear repeatedly in Rule 14a-9 itself. 17 C.F.R. §240.14a-9(a).[11] BoA Mem.

[11] Rule 14a-9 provides, in relevant part: "[n]o solicitation subject to this regulation shall be made by means of any proxy statement, form of proxy . . . or other communication, written or oral, containing any statement which, at the time and in light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or

30-31. Defendants are incorrect. A plaintiff may plead securities law violations based on negligence and fraud in the alternative. *Garber v. Legg Mason, Inc.*, 537 F. Supp. 2d 597, 612 (S.D.N.Y. 2008) (Chin, J.), *aff'd*, No. 08-1831-CV, 2009 WL 3109914 (2d Cir. Sept. 30, 2009) ("sound[s] in fraud" exception does not apply to securities claim where plaintiff plausibly differentiates negligence claim from fraud claims in complaint, including by expressly disclaiming reliance on fraud theory).[12]

Here, Plaintiffs have differentiated between their fraud-based Exchange Act claims, *see* Compl. §XI, and their negligence-based Exchange Act claims, *see* Compl. §XII, the latter disclaiming any reliance on fraud and occupying a separate section of the Complaint. *See* ¶¶327, 333(g), 335, 347. Moreover, Plaintiffs do not bring Section 10(b) claims against every Defendant who faces a Section 14(a) claim. Thus, Plaintiffs' Section 14(a) claims do not sound in fraud and do not have to meet the pleading requirements of Rule 9(b).

Furthermore, contrary to Defendants' claim, scienter is not grafted onto Plaintiffs' Section 14(a) claims even assuming *arguendo* that Rule 9(b) applies. Rule 9(b) only requires that a plaintiff "state with particularity the circumstances constituting fraud or mistake." As Judge Rakoff recently stated, "[w]hen they [the *Rombach* court] are saying you have to plead fraud with particularity, it doesn't mean you have to plead with particularity an element that is not an element of the complaint. It just means, for example, the misrepresentations would have

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necessary to correct any statement in any earlier communication with respect to the solicitation of a proxy for the same meeting for subject matter which has become false or misleading."

[12] *See also Rombach v. Chang*, 355 F.3d 164, 171 (2d Cir. 2004) ("[T]he same course of conduct that would support a Rule 10b-5 claim may as well support a Section 11 claim or a claim under Section 12(a)(2)"); *In re Refco, Inc. Sec. Litig.*, 503 F. Supp. 2d 611, 631-32 (S.D.N.Y. 2007) (holding that "sounds in fraud" exception did not apply where plaintiffs differentiated fraud-based and negligence-based securities claims by disclaiming fraud and "carefully structur[ing]" the complaint "so as to draw a clear distinction between negligence and fraud claims," and finding plaintiffs' pleading of "a massive fraud" did not affect their "right to plead in the alternative that defendants violated provisions requiring only negligence"); *In re Prestige Brands Holding, Inc.*, No. 05 Civ. 06924, 2006 WL 2147719, at *8 (S.D.N.Y. July 10, 2006) ("[P]laintiffs disclaim any intention to plead fraud except with respect to the Rule 10b-5 claims . . . and of course they are not required to. . . . A representation of fact in a prospectus may be material, false and misleading without regard to the motive or intent of the author").

to be spelled out in 9(b) detail as opposed to the more general detail that [R]ule 8 would require." Hr'g Tr. at 63:24-64:5, *Louisiana Mun. Police Employees' Ret. Sys. v. Merrill Lynch & Co.*, No. 08-9063 (JSR) (S.D.N.Y. Feb. 19, 2009), attached as Ex. A to the Declaration of Sharan Nirmul ("Nirmul Decl."), submitted herewith; *see also In re Livent, Inc. Noteholders Sec. Litig.*, 151 F. Supp. 2d 371, 430 (S.D.N.Y. 2001) ("Since misrepresentation is all that is required to sustain a claim under § 11, [plaintiffs] would be unduly burdened if the Court were to dismiss their separately standing negligence claims just because the predominant theory the complaint expresses is one of fraud. Such a conclusion would undermine Rule 8(e)(2), which provides that '[a] party may . . . state as many separate claims or defenses as the party has regardless of consistency . . . .'").[13]

As a last resort, Defendants argue that even if this Court were to determine that scienter is not an element of Plaintiffs' Section 14(a) claim, Plaintiffs should be forced to plead a "strong inference of negligence." BoA Mem. at 31-32. Negligence, however, is not a "state of mind." *Beck v. Dobrowski*, 559 F.3d 680, 681-82 (7th Cir. 2009) (Posner, J.). In *Beck*, Judge Posner soundly concluded that "[t]here is no required state of mind for a violation of 14(a)," because "negligence is not a state of mind; it is a failure, whether conscious or unavoidable . . . to come up to the specified standard of care." *Id.* (citations omitted). In light of this "basic principle [that] is sometimes overlooked," the court held that PSLRA Section 21D-(b)(2) did not apply to Section 14(a) claims. *Id.*[14] *Beck* accords with Judge Friendly's decision in *Gerstle*, in which the

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[13] Here, there can be no serious dispute that the allegations in the Complaint satisfy Rule 9(b). The Complaint clearly sets forth each statement alleged to be false and misleading and explains the reasons why those statements are misleading.

[14] Thus, *Beck* became the first circuit court to substantively analyze the issue. *Compare Beck*, 559 F.3d at 681-82 (analyzing treatises, PSLRA and cases in support of ruling that "[t]here is no required state of mind for a violation of section 14(a)" because "negligence is not a state of mind") *with Little Gem Life Sciences, LLC v. Orphan Med. Inc.*, 537 F.3d 913, 917 (8th Cir. 2008) (rejecting argument that negligence is not a state of mind due to the simple absence of extant case law in support of the proposition) *and Knollenberg v. Harmonic, Inc.*, 152 Fed. App'x. 674, 683 (9th Cir. 2005) (stating without analysis that "a Section 14(a) plaintiff must plead with particularity facts that

Second Circuit rejected a heightened pleading requirement for claims involving a misleading proxy, noting that, "a broad standard of culpability here will serve to reinforce the high duty of care owed…in the preparation of a proxy statement seeking [shareholders'] acquiescence in this sort of transaction." *Gerstle*, 478 F.2d at 1300.[15]

C. The Bonus Allegations State A Claim Under Section 14(a)

1. The Joint Proxy Contained False Statements Regarding The Payment Of Bonuses

The Joint Proxy and Section 5.2(c) of the Merger Agreement affirmatively represented that Merrill "***shall not***" "without the prior written consent of [BoA] . . . increase in any manner the compensation or benefits of any" employee or "pay any amounts to Employees not required by any current plan or agreement (***other than base salary*** in the ordinary course of business)." ¶ 215. Similarly, the Joint Proxy stated that awarding discretionary bonus compensation was an "extraordinary action" that Merrill "***will not***" take before the merger closed without BoA's "prior written consent." ¶¶214-220. These statements were materially false and misleading because, as set forth above, BoA had already agreed to allow Merrill to pay up to $5.8 billion in bonuses prior to the close of the merger. The law is clear that once Defendants chose to speak about the subject of bonuses, they had "a duty to be both accurate and complete." *See Caiola v. Citibank, N.A., New York*, 295 F.3d 312, 331 (2d Cir. 2002); *In re Credit Suisse First Boston Corp. Sec.*

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give rise to a strong inference of negligence"). The stated rationale for the Eighth Circuit's ruling in *Little Gem* is no longer valid now that the Seventh Circuit has analyzed the question and determined that negligence is not a state of mind within the meaning of the PSLRA. *Beck*, 559 F.3d at 682-83. And the Ninth Circuit's *ipse dixit* statement of law in *Knollenberg* should be accorded little to no persuasive weight.. At least one court in this District has assumed – without analysis – that PSLRA Section 21D(b)(2) does apply to Section 14(a) claims premised on negligence, *see, e.g., Bond Opportunity Fund v.Unilab Corp.*, No. 99 Civ. 11074, 2003 WL 21058251, at *4 (S.D.N.Y. May 9, 2003) but the persuasive force of this summary declaration is questionable.

[15] Even if this Court were to conclude that Plaintiffs are required to plead a "strong inference of negligence," or even a strong inference of scienter to support their Section 14(a) claims, as set forth below in Section III.C, Plaintiffs' allegations manifestly meet these heightened standards as to those Defendants sued under Section 10(b).

Litig., No. 97 Civ. 4760 (JGK), 1998 WL 734365, at *6 (S.D.N.Y. Oct. 20, 1998) ("a defendant may not deal in half-truths") (citations omitted).

Accordingly, because the secret bonus agreement effectively contradicted the stated terms of the Merger Agreement and Joint Proxy, disclosure of the secret bonus agreement was necessary to render these statements not misleading. *See Mendell*, 927 F.2d at 678 (statement in proxy that officer would not "acquire an equity interest" in the company was materially misleading where company "had in fact planned prior to issuance of the proxy statements to give [officer] stock"); *In re Bristol-Myers Squibb Co. Sec. Litig.*, 586 F. Supp. 2d 148, 160-61 (S.D.N.Y. 2008) (where company represented that it would "vigorously pursue" its legal rights, it was required to disclose that it had already "bargained away" one of those rights in negotiations with another company).

Moreover, the Joint Proxy incorporated Merrill's March 2008 Proxy, which further advised investors that Merrill's executive bonuses were "paid in January for performance in the prior fiscal year" and depended on Merrill's financial performance. ¶219. Because the bonus agreement contradicted these terms by permitting Merrill to pay up to $5.8 billion in bonuses in December regardless of Merrill's financial performance, disclosure of the bonus agreement was necessary to render these statements not misleading as well. *See Novak v. Kasaks*, 216 F.3d 300, 311 (2d Cir. 2000) (SEC filings were "materially misleading in that the disclosed policy no longer reflected actual practice"); *In re Dynex Capital Inc. Sec. Litig.*, No. 05 Civ. 1897 (HB), 2009 WL 3380621, at *8 (S.D.N.Y. Oct. 19, 2009) ("[S]tatements by a defendant that it 'generally' adheres to a particular policy become misleading when in fact there is no such policy or the policy is something else altogether.").

2. Defendants Were Independently Obligated To Disclose The Secret Bonus Agreement Because It Was A Material Term Of The Merger

As the Second Circuit has held, Section 14(a) and Rule 14a-9 carry with them a broad, affirmative duty that requires disclosure of "all the objective material facts relating to the transaction" in the proxy itself. *Mendell*, 927 F.2d at 674. This broad disclosure duty exists because a proxy is an express request for shareholders to authorize a transaction – in this case the largest merger in BoA's history – and thus must disclose all ***material*** facts related to that transaction. "Only when the proxy statement fully and fairly furnishes all the objective material facts as to enable a reasonably prudent stockholder to make an informed investment decision is the federal purpose in the securities laws served." *Id.* at 674; *Mills*, 396 U.S. at 381-85.

Here, the undisclosed bonus agreement was a material term of the Merger Agreement. It was one of the three "main things" the parties negotiated, and it was indisputably material to BoA's shareholders' assessment of the merger consideration and decision to authorize the transaction. ¶67. Indeed, the magnitude of the bonuses authorized – an amount equivalent to 12% of the merger consideration – alone establishes their materiality. ¶¶6, 197. Moreover, although the Joint Proxy represented that BoA had the power to prevent Merrill from paying discretionary bonuses prior to the close of the merger, BoA had already bargained away this right. *Bristol-Myers*, 586 F. Supp. 2d at 160-61.

In addition, the acceleration of the bonus payments to December – before Merrill's fourth quarter and year-end results were announced in January and before the merger closed – was material because it allowed Merrill to pay billions of dollars of bonuses despite its catastrophically poor financial performance during 2008. Indeed, Merrill informed shareholders in its own March 2008 Proxy that bonuses were "paid in January" precisely because this schedule ensured that Merrill's "financial performance" was the "dominant consideration" in

setting bonus amounts. ¶70. By accelerating the bonus payments to December, Merrill's publicly stated bonus policy became materially false and misleading. Since "a reasonable shareholder would consider [these facts] important in deciding how to vote," Defendants had a duty to disclose them in the Proxy. *Mendell*, 927 F.2d at 673.

Furthermore, as the SEC has specifically alleged in its own Action against BoA, SEC regulations independently required disclosure of the bonus agreement. ¶171. Consistent with Section 14(a)'s broad disclosure duty, Item 601(b)(2) of SEC Regulation S-K expressly mandates that any disclosure document that attaches a "plan of acquisition" (such as the Merger Agreement) must also attach any "schedule . . . [that] contain[s] information which is material to an investment decision and which is not otherwise disclosed" in the plan. If any schedules are omitted, the disclosure document must "contain a list briefly identifying the[ir] contents." 17 C.F.R. §229.601(b)(2). In this case, because the Company Disclosure Schedule constituted a schedule that "contain[s] information which is material" under Item 601, Defendants were required to attach it to the September 18, 2008 Forms 8-K and the Joint Proxy or, at minimum, summarize its contents. Again, it is undisputed that Defendants failed to do either. *See, e.g.*, *In re Scholastic Corp. Sec. Litig.*, 252 F.3d 63, 70-71 (2d 2001) (actionable duty to disclose under the Exchange Act exists when SEC regulation requires disclosure).

3. The Undisclosed "Exceptions" Set Forth In The Merger Agreement Did Not Obviate Defendants' Obligations To Disclose The Secret Bonus Agreement

Defendants claim that, as a matter of law, "no reasonable investor could have read" the statements in the Merger Agreement and Joint Proxy to "represent[] that Merrill would not pay any bonuses prior to the closing," because those statements were qualified by certain undisclosed "exceptions," including the non-public Company Disclosure Schedule. BoA Mem. 14. Defendants are wrong for several reasons.

First, as explained above, Section 14(a) requires "full" and affirmative disclosure of all material facts; thus, the omission of the bonus agreement, by itself, triggers liability. *See Mendell*, 927 F.2d at 675 ("[W]hat is required to be disclosed is all material objective facts relating to the transaction."). If Defendants' interpretation of the securities laws were correct, it would render the proxy rules irrelevant because any merger term could be changed or withdrawn by undisclosed "exceptions."[16]

Second, it defies reason to contend that a generic reference to "certain exceptions" and the unpublished Company Disclosure Schedule somehow could have informed a reasonable investor that BoA had already secretly agreed to let Merrill funnel up to $5.8 billion in bonuses to its employees before the merger closed, such that "no reasonable investor" would have relied on the statements regarding bonuses in the Joint Proxy and Merger Agreement that Merrill would "not" pay bonuses before the merger closed. Indeed, the Ninth Circuit recently rejected this precise argument in *Glazer Capital Mgmt., L.P. v. Magistri*, 549 F.3d 736, 741 (9th Cir. 2008). The defendants in that case argued, just as Defendants here contend, that no reasonable investor would have relied on the terms of a merger agreement because the terms were made "subject to a disclosure schedule." *Id.* In flatly rejecting this argument, the court held that the "mere fact . . . that the merger agreement . . . included reference to a non-public disclosure schedule would not, as a matter of law, prevent a reasonable investor from relying on its terms." *Id.* The Ninth Circuit's holding applies with equal force here.

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[16] Defendants' citation to *Resnik v. Swartz*, 303 F.3d 147 (2d Cir. 2002), is inapposite. First, *Resnik* did not involve a merger, and thus has nothing to do with disclosure duties in the merger context. Second, *Resnik* did not concern highly material facts of the sort at issue here. Instead, *Resnik* concerned the mere failure to disclose the estimated present value of stock options issued to the company's outside directors. *Id.* at 149. Third, the court held that the material facts concerning the stock option grants were fully and accurately disclosed, and the proxy made no misleading statements on the subject of options. *Id.* at 153 (proxy statement "makes [] clear" that stock options would be granted, "fully stated" the terms on which they would be granted, and made "no suggestion" that they lacked present value).

Third, the exceptions to which Defendants point were wholly inadequate to inform a "reasonable" investor of the existence of the undisclosed bonus agreement. *See* BoA Mem. 13. Specifically:

- The reference to the so-called "Company Disclosure Schedule" was meaningless because the substance of the Disclosure Schedule was not disclosed or described in any detail.
- The mention that the Merger Agreement "contemplated" that Merrill would use its "reasonable best efforts" to retain employees was similarly meaningless. Nowhere did the "best efforts" clause mention bonuses – let alone affirmatively state that billions of dollars would be paid prior to the closing regardless of Merrill's financial performance in 2008.
- The statement that BoA could provide its "prior written consent" to pay bonuses was materially misleading because, in fact, BoA had already given its written consent.

In sum, these exceptions provide no basis to conclude – as a matter of law – that a reasonable investor would have taken the representations that Merrill "shall not" and "will not" pay bonuses before the merger closed to mean that Merrill "shall" and "will" do so or that BoA had already agreed in writing to the payment of billions of dollars in bonuses before the merger closed. *See Glazer*, 549 F.3d at 741.

4. BoA's Shareholders And Investors Were Entitled To Rely Upon The Joint Proxy's Statements Relating To Bonuses

Defendants next argue that shareholders should not have relied on the Merger Agreement's and Joint Proxy's statements relating to the payment of bonuses because they were only "contractual allocations of risk" that existed for the benefit of BoA and Merrill, and were not factual representations to investors. BoA Mem. 14. This argument is belied by Defendants' own words in the Joint Proxy, which recommended to shareholders that they "read the merger agreement carefully and in its entirety" precisely because "it is the legal document governing the merger." Goldin Dec., Ex 1 at 76. Further, the September 18, 2008 Forms 8-K which were attached to the Merger Agreement stated that they were filed for the express purpose of "provid[ing] investors with information regarding the terms of the Merger Agreement." Goldin

Dec., Ex. 17 (Sept. 18, 2008 BoA 8-K at Item 1.01). Defendants cannot encourage investors to rely upon their SEC filings and then simultaneously claim that no reasonable investor would have taken them seriously.

Glazer rejected the very same arguments Defendants make here. In that case, the plaintiffs alleged that a publicly disclosed merger agreement was misleading because it contained the false representation that one of the companies was in compliance with the Foreign Corrupt Practices Act ("FCPA"). 549 F.3d at 741. The defendants argued, *inter alia*, that representations in the merger agreement were not actionable because they were part of a private contract, rather than factual representations to investors. *Id.* at 741. The Ninth Circuit rejected this argument, holding that the "mere fact" that the statements appeared in a merger agreement did not prevent a reasonable investor from relying on them, particularly since the merger in question was "a very significant event for the company" and "intense investor interest in the details of the merger" was to be expected. *Id.*[17]

The SEC also has rejected the same arguments in prior cases. SEC Release No. 34-51283, 2005 WL 1074830 (Mar. 1, 2005) ("Titan Report"). In 2003, Titan Corporation and Lockheed Martin entered into a merger agreement which included a representation by Titan that it had not undertaken any actions that violated the FCPA. *Id.* Though investigations had been commenced by the SEC and Department of Justice regarding Titan's compliance with the FCPA, the relevant representation remained unchanged. In finding that the misstatement could give rise to liability under Sections 14(a) and 10(b) of the Exchange Act, the SEC stated that "the

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[17] In their motions, Defendants go to great lengths to try to distinguish *Glazer*, claiming that Merrill's promise not to pay bonuses was characterized in the Merger Agreement as a "covenant," whereas the representation in *Glazer* was characterized as a "representation and warranty." BoA Mem. 15 n.2. Semantics aside, this is a distinction without a difference. As described above, investors were explicitly invited to read the Merger Agreement and consider its terms when making an investment decision. That a term was described as a "covenant" rather than a "representation" would not matter to an investor trying to determine the scope of the arrangement for which he was being asked to cast his vote.

inclusion of [a contractual representation] in a disclosure document filed with the Commission ... constitutes a disclosure to investors," and thus "a reasonable investor could conclude that the statements made in the representation describe the actual state of affairs and the information could be material." *Id.* Accordingly, "if additional material facts exist, such as those contradicting or qualifying the disclosure of the original representation," a company would also be required to disclose those facts. *Id.*

In sum, Defendants' argument that shareholders and investors were not entitled to rely on the language in the Merger Agreement is not credible and contrary to law.

5. The Market Was Unaware Of The Secret Bonus Agreement

Defendants also ask the Court to conclude – again, as a matter of law – that even though they failed to disclose the bonus agreement, "[n]o one was misled" because: (i) there was limited media speculation that Merrill might pay year-end bonuses, without stating when they might be paid; (ii) Merrill disclosed its quarterly compensation expense accruals for earlier quarters, an unidentified portion of which concerned bonuses; and (iii) Merrill's March 2008 Proxy showed that bonuses were paid in 2007 even though Merrill had suffered losses. BoA Mem. 16-20. In essence, Defendants make a "truth-on-the-market" argument, contending that the market knew of the bonus agreement. Defendants' arguments must fail.

First, the reaction of the market alone establishes that the information relating to Merrill's bonuses was not disclosed before January 21, 2009. Immediately after *The Financial Times* broke the news of Merrill's bonus payments, BoA's common stock dropped 15%, and analysts and the financial press expressed shock over the "unusual" and "ridiculous" decision to allow Merrill to pay billions of dollars of bonuses "much earlier than expected." On the following day, the Associated Press reported that Thain had resigned "under pressure from Bank of America . . . after reports that he rushed out billions of dollars in bonuses to Merrill Lynch employees in his

final days as CEO there, while the brokerage was suffering huge losses and just before Bank of America took it over." *See* ¶¶155-61. Given these facts, Defendants' arguments that the market somehow "knew" that Merrill would pay billions of dollars in bonuses prior to the close of the merger, despite its massive losses, must be rejected. *Ganino*, 228 F.3d at 166-68 (market response after facts emerged precluded truth on market defense); *In re Alstom S.A. Sec. Litig.*, 406 F. Supp. 2d 433, 453 (S.D.N.Y. 2005) (omission material where "financial professionals were taken by surprise").

Second, as the Second Circuit has recognized, Section 14(a) requires that a proxy disclose – within its four corners – all material facts regarding the proposed transaction precisely because investors are ***not*** required to decipher speculative news reports or reverse-engineer accounting accruals to infer the existence of material merger terms that contradict the proxy's express statements. *See Kronfeld v. Trans World Airlines, Inc.*, 832 F.2d 726, 736 (2d Cir. 1987) ("There are serious limitations on a corporation's ability to charge its stockholders with knowledge of information omitted from a document such as a proxy statement or prospectus on the basis that the information is public knowledge and otherwise available to them.").[18]

Third, even if the Court wished to consider this "intensively fact-specific" issue which is rarely an appropriate basis for dismissal, Defendants' proffered sources do not reveal the facts at issue "with a degree of intensity and credibility" necessary to negate the Joint Proxy's false statements as a matter of law. *Ganino*, 228 F.3d at 167 (citation omitted). Significantly, none of these sources reveal that BoA had already agreed to allow Merrill to pay up to $5.8 billion in bonuses before the merger's close ***even though Merrill was going bankrupt***. Nor did Merrill's financial statements disclose the bonuses: Merrill's most senior human resources executive

[18] *See also United Paperworkers*, 985 F.2d at 1199 ("Corporate documents that have not been distributed to the shareholders entitled to vote on the proposal should rarely be considered part of the total mix of information reasonably available to those shareholders").

testified before the NYAG that Merrill's compensation expense accruals did not allow a reader to even "guess" the amount of Merrill's "annual bonus funding [] because there are so many other line items that go into the aggregate expense," such as salaries, prior bonus awards that vest over multiple quarters, and numerous other benefits expenses. ¶172.

Defendants also cite articles which actually show the lack of definitive information in the market regarding the timing and amount of Merrill's 2008 bonuses. The October 27 *Bloomberg* article – which other cited articles simply re-published – specifically stated that "Whether what you see [in compensation expense accruals] is what they're going to pay, ***you can't tell yet***," and noted, "[b]onus awards are typically determined at the ***end of the year***, with payments made in December or January." *See* Goldin Decl., Ex. 31 at 2-3. Such indeterminate, speculative reports could not undermine Defendants' definitive statements on the matter: Merrill's March 2008 Proxy expressly stated that bonuses, if any, would be paid "in January," and thus reinforced the other proxy solicitations which indicated that no bonuses would be paid before the merger closed on January 1.[19] Courts routinely recognize that such speculative, incomplete, and vague reports cannot establish a truth-on-the-market defense. *See Lapin v. Goldman Sachs Group, Inc.*, 506 F. Supp. 2d 221, 238-239 (S.D.N.Y. 2006) (even though news articles "raised some concern in the market," they did not completely negate company's assurances); *RMED Int'l v. Sloan Supermarkets, Inc.*, 185 F. Supp. 2d 389, 402 (S.D.N.Y. 2002) (no truth-on-the-market where news articles did not reveal "the very information" at issue).

Defendants also make much of the fact that the market purportedly knew Merrill paid bonuses in 2007 despite suffering large losses. This argument is irrelevant. Plaintiffs do not

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[19] Defendants baldly assert in a footnote that "no reasonable investor could have viewed the timing of the bonuses as material." BoA Mem. 24 n.15. This argument ignores the fact that Defendants explicitly told investors that the January payment schedule was important because it ensured that the "dominant consideration" in making bonus payments was Merrill's financial condition. Moreover, this is a fact issue.

allege that Merrill violated the law by paying bonuses despite suffering losses. To the contrary, Plaintiffs allege that the Merger Agreement and Joint Proxy were materially false and misleading because they failed to disclose a material term of the agreement; namely, that BoA had agreed to allow Merrill to pay up to $5.8 billion in bonuses prior to the close of the merger.

Thus, at a minimum, the Complaint sets forth numerous facts which make clear that this "truth-on-the-market defense" cannot be decided on a motion to dismiss, or, in the alternative, must be decided in Plaintiffs' favor. *Ganino*, 228 F.3d at 167; *Lapin,* 506 F. Supp. 2d at 238 (S.D.N.Y. 2006) (the "burden of establishing the truth-on-the-market defense is extremely difficult, perhaps impossible, to meet ***at the summary judgment stage***") (alterations and quotation marks omitted).

6. Defendants' Remaining Excuses For Failing To Disclose The Bonus Agreement Should Be Rejected

Defendants' remaining arguments are equally unavailing and should be rejected. First, Defendants argue that it is "common practice to use nonpublic disclosure schedules to qualify" representations in merger-related disclosure documents. BoA Mem. 21, 32. Not so. It is absolutely not "common practice," nor is it legal, to keep ***material*** terms of a merger "nonpublic" – especially where, as here, those undisclosed terms contradict statements in the Merger Agreement. *Titan Report*, SEC Release No. 34-51283, 2005 WL 1074830, at *2-*3 (Mar. 1, 2005); *accord Glazer*, 549 F.3d at 741. Moreover, there is no "everyone else is doing it" defense to the securities laws, and what constitutes a "customary" or "common" practice raises fact issues that cannot be decided on a motion to dismiss.

Next, Defendants contend that they cannot be held liable for falsely representing in Merrill's March 2008 Proxy that bonuses would be paid in January because "no reasonable shareholder" would have considered those statements applicable to a merger announced six

months later. BoA Mem. 24. This argument ignores the material fact that Defendants themselves told investors that the March 2008 Proxy "is considered to be a part of" the Joint Proxy, and that they should read the "important information" in the March 2008 Proxy. Joint Proxy, attached as Ex. 1 to the Goldin Dec., at 123-24. *See In re ZZZZ Best Sec. Litig.*, 864 F. Supp. 960, 976 (N.D. Cal. 1994) (documents incorporated by reference are republished and remain "alive" in the marketplace).

Finally, Defendants argue that disclosure of the bonus agreement was not required because Merrill ultimately paid ***only*** $3.6 billion in bonuses (an amount which was still obviously material) despite suffering $21 billion in fourth quarter losses, and because disclosure would have caused "substantial disappointment" among Merrill's executives and employees once they learned that their bonuses were ***reduced*** to $3.6 billion. BoA Mem. 5. The fact that the bonuses paid were less than the bonus cap does not absolve Defendants for failing to disclose a term of the Merger Agreement that was clearly material. Moreover, employee "disappointment" is no defense to the federal securities laws – even where, as here, this disappointment arises from the news that a failing company has decided to award its executives and employees "only" $3.6 billion in discretionary year-end bonuses.

D. Defendants' Failure To Disclose Merrill's And BoA's Massive Losses Before The Shareholder Vote Violated Section 14(a)

As set forth above, by the date of the shareholder vote, Merrill had lost over $15 billion – losses that were so severe that BoA's senior executives internally discussed terminating the merger pursuant to the material adverse change clause at least three separate times before the vote. ¶¶91, 100-102, 210. Moreover, BoA itself had suffered $800 million in losses and was projecting a total loss for the quarter of $1.4 billion (the first quarterly loss in its history) – losses which left it "very thinly capitalized" and "clearly not [] well prepared for any further

deterioration." ¶103. As set forth below, Defendants' failure to disclose these facts prior to the shareholder vote violated Section 14(a) and Rule 14a-9.

1. Section 14(a) Required Defendants To Disclose Merrill's Massive Losses Before The Vote

Although Defendants contend otherwise, the securities laws do not permit a defendant to remain silent in the weeks leading up to one of the largest mergers in corporate history when it knows that approval of the transaction will leave the combined company on the brink of insolvency. Merrill's and BoA's crippling losses were highly material facts that were required to be disclosed prior to the shareholder vote. Indeed, as set forth above at Section II.C.2, Section 14(a) and Rule 14a-9 required Defendants to disclose "all material objective facts relating to the transaction." *Mendell*, 927 F.2d at 674-75. As the SEC has made clear, this duty mandates disclosure of any material information that becomes known ***after*** the issuance of a proxy, but before the shareholder vote. *See* SEC Release No. 34-23789, 1986 WL 722059, at *5 (Nov. 10, 1986) ("When there have been material changes in the proxy soliciting material or material subsequent events . . . , an additional proxy card, along with revised or additional proxy solicitation material, should be furnished to security holders."); SEC Release No. 34-16343, 1979 WL 173161, at *5 (Nov. 15, 1979) ("It is of overriding importance . . . that shareholders be given timely and accurate information of material changes" under Rules 14a-1 and 14a-9).[20]

Although Defendants profess otherwise, it is beyond dispute that Merrill's and BoA's losses were extraordinarily material. Indeed, Merrill's losses were so large that they threatened BoA's solvency if the merger were approved. As Vice Chancellor Strine recently recognized at the hearing on Defendants' motion to dismiss in *In re Bank of America Corp. Shareholder*

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[20] *See also Katz v. Pels*, 774 F. Supp. 121, 126 (S.D.N.Y. 1991) (plaintiffs need only allege that a proxy misrepresented or omitted material information); *Allyn Corp. v. Hartford Natl. Corp.*, No. H 81-912, 1982 WL 1301 at *14 (D. Conn. Mar. 30, 1982) (same); *SEC v. Kalvex, Inc.*, 425 F. Supp. 310, 314-15 (S.D.N.Y. 1975).

Derivative Litigation, C.A. No. 4307-VCS (Del. Ch. 2009) ("*Del. Derivative Action*"), the very fact that BoA's highest ranking executives repeatedly debated terminating the transaction in the weeks leading up to the vote by itself establishes the materiality of this information:

> [Lewis and the BoA Board] knew this [Merrill's pre-vote losses] was material . . . If [Lewis] is seriously pondering the declaration of a MAC at the same time that the stockholders are voting, that, in itself, many people would want to know, and to rule on a motion to dismiss that that wouldn't be material to a reasonable stockholder, much less the objective financial information about the deterioration that was known, I just don't know how to do that.

Hr'g. Tr. 120:19-121:15, *Del. Derivative Action*, Nirmul Decl. Ex. C.

Remarkably, Defendants argue that Merrill's losses were immaterial as a matter of law because the market was aware of: (i) Merrill's previously-reported losses in earlier quarters; (ii) BoA's and Merrill's vague disclosures about adverse market conditions; and (iii) general media reports about the state of the markets. *See* BoA Mem. 40-43. Each of these arguments can be disposed of swiftly.[21]

First, while materiality is a question of fact that cannot be decided at the pleading stage, *see, e.g.*, *Ganino*, 228 F.3d at 167; *Mendell*, 927 F.2d at 673, should the Court wish to delve into this fact issue, then Defendants' argument is unmoored from reality. The fact that BoA's senior executives were debating whether Merrill's losses constituted a materially adverse change in its financial condition prior to the vote establishes that these losses, in the minds of BoA's own management, were both material and entirely unexpected. Hr'g Tr. at 120:19-121:15, *Del. Derivative. Action*, Nirmul Decl., Ex. C. Indeed, as of mid-October 2008, analysts' consensus expectations were for Merrill to earn a fourth quarter ***profit*** of $0.44 to $0.54 per share, but by November 3, Merrill's losses had already reached historic proportions. ¶203.[22] Thus, when the

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[21] Defendants do not argue that BoA's losses were immaterial as a matter of law.

[22] The BoA Defendants claim that Merrill's losses in previous years were purportedly in line with its fourth quarter loss (but only if you painstakingly manipulate the numbers as they explain in a footnote) which thereby rendered

stunning news of Merrill's losses was revealed in January 2009, credit rating agencies immediately downgraded BoA and Merrill (¶¶150, 266), and BoA's stock price plummeted on extremely heavy trading volume. ¶¶264-65. As courts routinely hold, such facts establish that this information was both material and previously undisclosed. *See, e.g.*, *Lapin*, 506 F. Supp. at 231, 236; *In re Vivendi Universal, S.A., Sec. Litig.*, 381 F. Supp. 2d 158, 182 (S.D.N.Y. 2003).

Second, vague risk disclosures and news reports about "stress" and "disruption" in the general "financial system" utterly failed to disclose the cold, hard fact that – contrary to investors' expectations - Merrill had lost more than $15 billion in the two months preceding the vote. Defendants never warned that Merrill was effectively insolvent or that completing the merger would jeopardize the solvency of the combined company. Courts uniformly hold that vague "warnings" do not immunize a defendant from liability for the failure to disclose concrete, existing facts. *See Heller v. Goldin Restructuring Fund, L.P.*, 590 F. Supp. 2d 603, 618 (S.D.N.Y. 2008) (securities laws provide "no protection to someone who warns his hiking companion to walk slowly because there might be a ditch ahead when he knows with near certainty that the Grand Canyon lies one foot away") (*citing In re Prudential Sec. Inc. Ltd. P'ships Litig.*, 930 F. Supp. 68, 72 (S.D.N.Y. 1996)); *Edison Fund v. Cogent Inv. Strategies Fund, Ltd.*, 551 F. Supp. 2d 210, 226 (S.D.N.Y. 2008) ("If a party is aware of an actual danger or cause for concern, the party may not rely on a generic disclaimer in order to avoid liability"); *Lapin*, 506 F. Supp. 2d at 238 (rejecting argument that news articles and general disclaimer disclosed facts at issue).[23]

Merrill's fourth quarter 2008 losses immaterial as a matter of law. BoA Mem. at 41 and n. 32. The previous losses are irrelevant to the question of the materiality of these losses to BoA's shareholders weighing the benefits of the merger, where Defendants had falsely assured BoA's shareholders that Merrill's balance sheet was de-risked and projected that Merrill stood to make a profit in the fourth quarter.

[23] Defendants also contend that Merrill's $15.3 billion in pre-vote losses were immaterial because "they were principally mark-to-market adjustments as opposed to cash losses." BoA Mem. 43, n.33. The fact that Defendants

Third, Defendants argue that, even if Merrill's and BoA's losses were material, they were not required to disclose those losses because there is no duty to disclose intra-quarter results or forecasts. *See* BoA Mem. 34-36. This argument completely misses the mark. Unlike all of Defendants' cited authorities, this is not a mere projections case where a company is accused of not keeping its investors appraised of mid-quarter losses that might not be in line with investor expectations for the entire quarter. Quite the opposite, this is a case where BoA and Merrill placed their contemporaneous financial condition directly at issue in connection with a proposed merger, which was slated to be voted upon before the quarter closed. For shareholders tasked with determining whether the proposed merger with Merrill was in their best interests, Merrill's mounting losses, which threatened BoA's solvency, were obviously material. Absent disclosure of these losses, Defendants' proxy solicitations were misleading. As even one of Defendants' cited authorities explicitly held, although a company may not have the obligation to update shareholders mid-quarter under normal circumstances, "[t]he exception to this rule is where the initial disclosures that were argued to have triggered the duty to update involve information about events that could 'fundamentally change the natures of the companies involved,'" such as a merger. *Blum v. Semiconductor Packaging Mats. Co., Inc.*, No. C.A. 97-7078, 1998 WL 254035, at *2 (E.D. Pa. May 5, 1998) (citation omitted).[24]

Lewis, Price, and Cotty debated invoking the MAC based on these losses, by itself, establishes that the losses were highly material regardless of whether they were mark-to-market or cash losses. *See, e.g., SEC v. National Student Marketing Corp.*, 457 F. Supp. 682, 709 (D.D.C. 1978) (holding that losses discovered just before a merger closing were material, and therefore should have been disclosed to shareholders, because the board of directors considered the losses "significant and important in their deliberations. The adjustments would be no less important in the deliberations of the reasonable investor.").

[24] That the BoA Defendants would disclaim any duty to disclose Merrill's massive loss in the context of this merger is particularly disingenuous given they were charged with such a duty in the 1999 merger of BankAmerica with Nationsbank. *See In re BankAmerica Corp. Sec. Litig.*, 78 F. Supp. 2d 976 (E.D. Mo. 1999). In that deal, BankAmerica failed to disclose during the solicitation period of the merger with Nationsbank that BankAmerica had suffered $372 million in losses just prior to the vote due to its relationship with a high-risk hedge fund, among other large exposures. *Id.* at 984. The court concluded that the plaintiffs had adequately alleged a direct claim under Section 14(a) because the defendants had a duty to disclose the losses since they were "certainly material." *Id.* at

2. SEC Regulations Required Defendants To Disclose The Highly Material Losses

As noted above, a duty to disclose exists when an SEC regulation requires disclosure of particular information. Here, Defendants had a regulatory duty to comply with Schedule 14A, which describes the information that must be included in a proxy statement and specifically requires that the issuer disclose the information required by Item 303 of Regulation S-K. *See* Item 13, 17 C.F.R. § 240.14a-101. In turn, Item 303 of Regulation S-K requires disclosure of: (i) "known trends or any known demands, commitments, events or uncertainties that will result in or that are reasonably likely to result in the registrant's liquidity increasing or decreasing in any material way"; (ii) "known material trends, favorable or unfavorable, in the registrant's capital resources"; and (iii) "known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations." 17 C.F.R. §229.303.

When the Proxy was filed on November 3, Defendants knew that Merrill had already suffered $7 billion of losses, which was the largest monthly loss in Merrill's history, and that these losses were accelerating. ¶¶89, 106. By November 14, weeks before the vote, and certainly by the day of the vote, this trend had become so pronounced that BoA's senior executives feared for BoA's own solvency if the merger were approved. ¶¶89, 246. There can be no question that this information (i) materially affected BoA's and Merrill's "liquidity," "capital," and "income" within the meaning of Item 303, (ii) was exactly the sort of information that BoA shareholders needed in order to cast an informed vote, and (iii) was information that Item 303 requires be disclosed. *See Scholastic*, 252 F.3d at 70-71 (actionable duty to disclose under the Exchange Act exists when Item 303 requires disclosure).

993-94. Thus, the BoA Defendants were specifically instructed on a standard of care for disclosures in a previous case and clearly ignored it here.

In response, Defendants contend that they complied with their Item 303 obligations by incorporating by reference BoA's and Merrill's third quarter Forms 10-Q. BoA Mem. 38-39. This is not true. Schedule 14A permits incorporation by reference *only* if "[t]he material incorporated by reference substantially meets the requirements of this Item or the appropriate portions of this Item." Item 13(c)(3), 17 C.F.R. § 240.14a-101. In other words, incorporation by reference is sufficient only if the information accurately discloses the trends *as they exist at the time of the Proxy*. Here, the disclosures in the Forms 10-Q of market problems that "could lead to losses or defaults" and "will continue to have an adverse impact" failed to satisfy Schedule 14A for two reasons. First, these disclosures were current only through September 2008, not as of the time of the vote. Second, these disclosures were patently insufficient to inform investors of the massive losses suffered by Merrill in October and November 2008 that threatened the very survival of the combined entity.

3. Defendants' Positive Statements About The Merger Prior To The Shareholder Vote Were Materially False And Misleading

As alleged above, prior to the vote, Defendants made numerous positive statements about the merger and specifically assured investors that Merrill had not experienced a MAC and that the capital position of the combined entity would be "strong." ¶¶80, 191, 192, 199, 211-13. These statements were rendered materially false and misleading by Defendants' failure to disclose Merrill's and BoA's losses, and the fact that BoA executives were "actively and seriously consider[ing]" terminating the merger before the vote.

As noted above, a defendant who chooses to speak on a particular subject has "a duty to be both accurate and complete." *Caiola*, 295 F.3d at 331. Thus, with respect to statements that remain "alive" in the market, there exists an obligation to update these statements as soon as they become "misleading as the result of intervening events." *In re Time Warner Sec. Litig.*, 9 F.3d

259, 267 (2d Cir. 1993); *see also In re IBM Corporate Sec. Litig.* ("*IBM*"), 163 F.3d 102, 110 (2d Cir. 1998) ("[a] duty to update may exist when a statement, reasonable at the time it is made, becomes misleading because of a subsequent event").[25] In the context of a proxy filing, the duty to update applies with special force, because a proxy invites shareholders to authorize significant corporate transactions in direct reliance on the proxy's terms. Thus, the proxy implicitly represents that its contents will be accurate at least as of the date of the vote, and that investors may rely on those contents to make significant investment decisions on that date. As Judge Friendly held in *Gerstle*:

> we cannot suppose that management can lawfully sit by and allow shareholders to approve corporate action on the basis of a proxy statement without disclosing facts arising since its dissemination if these are so significant as to make it materially misleading, and we have no doubt that Rule 14a-9 is broad enough to impose liability for non-disclosure in this situation.

Gerstle, 478 F.2d at 1297 n.15; *see also* 17 C.F.R. §240.14a-9 (in every new proxy solicitation, the issuer is required "to correct any statement in any earlier communication with respect to the solicitation of a proxy for the same meeting or subject matter which has become false or misleading"); SEC Release No. 34-16343, 1979 WL 173161, at *14-15 (it is "of overriding importance . . . that shareholders be given timely and accurate information of material changes" occurring since the proxy was filed).[26]

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[25] *See also Weiner v. Quaker Oats Co.*, 129 F.3d 310, 316 (3d Cir. 1997) ("[T]here can be no doubt that a duty exists to correct prior statements, if the prior statements were true when made but misleading if left unrevised.") (*quoting In re Phillips Petroleum Sec. Litig.*, 881 F.2d 1236, 1245 (3d Cir. 1989)).

[26] Relevant authorities are universally in accord. *See General Time Corp. v. Talley Indus.*, 403 F.2d 159, 163 (2d Cir. 1968) ("[W]e assume that Rule 14a-9 may be read as authorizing a court to require a further statement and an opportunity to revoke proxies where a proxy statement, correct at the time of its issuance, has become misleading as a result of subsequent developments."); *Lebhar Friedman, Inc. v. Movielab, Inc.*, Civ. No. 86 Civ. 9965 (SWK) 1987 WL 5793, at *4 (S.D.N.Y. Jan. 13, 1987) (obligation to disclose before the shareholder vote "new information . . . which is material and whose omission would render the existing statement false or misleading"); SEC Release No. 34-16343, 1979 WL 173161, at *4 ("Even in a situation wherein a statement when made was true and correct, and is rendered incorrect due to a change in circumstances or other subsequent event, appropriate action should be taken to correct the misstatement prior to the meeting."); SEC Release No. 34-23789, 1986 WL 722059, *5. ("When there have been material changes in the proxy soliciting material or material subsequent events (in contrast

One particular scenario that triggers a duty to update is when a change in attitude regarding a corporate transaction is "sufficiently significant as to render prior or subsequent public disclosures materially misleading." *DeCicco v. United Rentals, Inc.*, 602 F. Supp. 2d 325, 345 (D. Conn. 2009); *Kamerman v. Steinberg*, 123 F.R.D. 66, 72-73 (S.D.N.Y. 1988) (tender offeror had duty to disclose facts that "cast serious doubt on the continued vitality" of the offer). This is because such critical pronouncements remain "alive" in investors' minds: investors will naturally believe that a corporation intends to go ahead with the plans it publicizes unless informed to the contrary. As the Third Circuit has held, these announcements contain "an implicit representation by the company that it will update the public with news of any radical change in the company's plans." *In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1433-34 (3d Cir. 1997) (Alito, J.).

For example, in *Time Warner*, the defendant company had originally "publicly hyped" its intention to raise capital by pursuing "strategic alliances," only to later determine that it would raise capital through a rights offering, which would have the effect of diluting the rights of existing shareholders and would drive down the stock price. 9 F.3d at 267-68. The Second Circuit held that the change in strategy rendered the corporation's original "hype" of strategic alliances misleading, thereby obligating the company to update its statements to reflect the new strategy. *Id.* ("[W]hen a corporation is pursuing a specific business goal and announces that goal as well as an intended approach for reaching it, it may come under an obligation to disclose other approaches to reaching the goal when those approaches are under ***active and serious consideration***").

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to routine updating), an additional proxy card, along with revised or additional proxy soliciting material, should be furnished to security holders … to permit security holders to assess the information and to change their voting decisions if desired.")

Similarly, *In re Gulf Oil/Cities Service Tender Offer Litigation*, 725 F. Supp. 712 (S.D.N.Y. 1989) – which was explicitly approved by the Second Circuit in *Time Warner*, 9 F.3d at 267 – involved a 1982 tender offer by Gulf Oil Company for the stock of Cities Service Company. The defendants' initial public statements regarding the deal expressed Gulf's "enthusiastic commitment" to the acquisition, calling it a "unique opportunity" for the company to "realize long-term strategic goals" and underscoring that the defendants were "view[ing] this transaction with a great deal of optimism." *Id.* at 747. Yet, Gulf's management soured on the deal a month before the tender offer was ultimately terminated. In ruling for the plaintiffs, who had committed their shares to the tender, former Chief Judge Mukasey stated that, under applicable Second Circuit case law, "***even contingent plans of a company may be sufficiently material to warrant disclosure***," and held that: "When objectively verifiable factors cause a significant change in a party's attitude toward a merger – a 'sharp break from . . . prior public positions' . . . – the securities laws may require that previously disclosed intentions be corrected." *Id.* at 746, 748 (*citing Kamerman*, 123 F.R.D. at 71).

Here, Defendants made numerous "continuing representations" both in their announcements of the merger and their expressed views as to its benefits for BoA, and their representations as to the financial condition of both companies and the combined entity, including:

- Lewis called the merger a "major grand slam home run" and the "strategic opportunity of a lifetime" that would "creat[e] more value for shareholders." ¶191.
- Lewis also reassured analysts that the 70% premium that BoA would pay for Merrill was justified because Merrill had "dramatically" lowered its risk profile and thus would be able to withstand the economic crisis. ¶80.
- Price also stated that BoA's $9.9 billion Offering "covered [its] anticipated needs from a Merrill standpoint" ¶199.

- In the Proxy, Defendants further assured shareholders that BoA had a "strong capital position" and that one of the principal reasons for the merger was the "strong capital position, funding capabilities and liquidity" of the combined company. ¶¶212, 213.
- Significantly, the Joint Proxy and attached Merger Agreement also "warranted" that Merrill had undergone no "material adverse change" as of the date of the Joint Proxy, and that this warranty would remain true "as of the Effective Time [*i.e.*, the closing of the merger on January 1] as though made on and as of" that date. ¶211.

Each of these statements was unquestionably false or misleading by the time of the shareholder vote.[27] For example, contrary to Defendants' statements that the combined entity would have a "strong" capital position and that the merger would create more value for shareholders, in reality Merrill's losses were large enough to bankrupt it, and BoA did not have the capital to absorb them. Likewise, contrary to Defendants' statement that Merrill had dramatically reduced its risk profile, Merrill's risk profile remained toxic. Further, while Price had stated that BoA's $9.9 billion Offering covered BoA's capital needs arising from the merger, BoA still required a massive capital injection (which came in the form of a $138 billion taxpayer bailout) to absorb Merrill's losses. Similarly, in contrast to the Joint Proxy's representation that BoA had a "strong capital position," in truth, BoA's capital position was "very thin." Finally, contrary to Defendants' representations that there were no "material adverse changes" to Merrill's financial condition through the date of the shareholder vote, in fact Merrill's losses were so catastrophic that BoA's highest executives had repeatedly internally debated terminating the merger precisely because Merrill had suffered a MAC. Because shareholders reasonably believed that Defendants' earlier statements, which described both Defendants' evaluation of the merger and terms on which it would be effected, would remain true at least through the shareholder vote, Defendants' failure to update these statements rendered them misleading.

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[27] As set forth herein, Plaintiffs have sufficiently alleged falsity of these statements at the time they were made.

Not only did Defendants fail to update and correct their prior representations, but they continued to issue new false statements touting the merger just days before the shareholder vote. Indeed, BoA published the November 26 Letter at the same time that BoA's most senior executives were actively debating terminating the merger because BoA lacked the capital to absorb Merrill's losses, falsely reassuring investors that that BoA had "more than adequate capital" and was "one of the strongest and most stable major banks in the world." Defendants' failure to disclose the objective facts of Merrill's and BoA's losses, as well as their "active and serious consideration" of invoking the MAC to terminate the merger, *Time Warner*, 9 F.3d at 267-68, violated their duties to update as described above. *See City of Sterling Heights Police and Fire Retirement Sys. v. Abbey Nat'l*, 423 F. Supp. 2d 348, 360 (S.D.N.Y. 2006) (Chin, J.) (actionable misstatements and omissions where defendants remained silent about risky exposures while issuing reassuring statements).

4. False Statements Are Not Immaterial Puffery

Defendants contend that a number of the aforementioned misstatements are "puffery," and thus immaterial as a matter of law.[28] BoA Mem. 57-58. They are wrong. Like all materiality issues, puffery determinations are fact-intensive and should only be made on a motion to dismiss when "reasonable minds could not differ on the question of their importance."

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[28] The purportedly "puffing" statements include statements during the September 15, 2008 Investor Call and Press Conference by Lewis that, through BoA's due diligence, he knew that Merrill had "dramatically reduc[ed] [its] marks" and thus had a "much lower risk profile," that the merger would "creat[e] more value for shareholders," and that the combined companies would be "just an incredible combination," as well as Thain's claims that "[t]his is a transaction that makes tremendous strategic sense. We think it gives us great opportunities, both on the Bank of America side and on the Merrill Lynch side" and "I think this is going to be a very attractive transaction from a shareholder point of view[.]" BoA Mem. 57; ¶192. In addition, Lewis told investors that the merger was "just a major grand slam home run" and "this was the strategic opportunity of a lifetime . . . . So we are very, very pleased with this." BoA Mem. 57, 65; ¶¶180, 191. Similarly, in the press release issued that day, Defendants praised the merger as "creat[ing] a company unrivalled in its breadth of financial services and global reach," a "great opportunity for our shareholders," and creating "the leading financial institution in the world with the combination of these two firms." BoA Mem. 57; ¶193. Finally, in the Proxy, Defendants claimed that the BoA had a "strong capital position, funding capabilities and liquidity." BoA Mem. 61; ¶212.

Goldman v. Belden, 754 F.2d 1059, 1067 (2d Cir. 1985); *Abbey v. 3F Therapeutics, Inc.*, No. 06 Civ. 409 (KMW), 2009 WL 4333819, at *9, (S.D.N.Y. Dec. 2, 2009). At a minimum, there is a fact issue as to whether Defendants' unequivocally positive statements about the merger were material. As the Supreme Court stated in *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083, 1090-91 (1991), "there is no room to deny that a statement of belief by corporate directors about a recommended course of action, or an explanation of their reasons for recommending it" can be material to investors. "[C]onclusory terms in a commercial context are reasonably understood to rest on a factual basis that justifies them as accurate, the absence of which renders them misleading." *Id.* at 1090, 1093. Thus, even descriptions of merger terms like "high" or "fair" value can be actionable upon a showing that the speaker did not hold the belief espoused or that opinion lacked a reasonable basis in fact. *Id.* at 1093; *see also In re Sprint Corp. Sec. Litig.*, 232 F. Supp. 2d 1193, 1214-15 (D. Kan. 2002) (the mere packaging of a false or misleading statement as a belief or opinion does not automatically insulate the speaker from liability under the federal securities laws).

Here, Defendants made specific representations about the financial condition of Merrill, BoA and the combined companies in the context of a grave economic crisis in order to justify purchasing Merrill at a 70% premium over its stock price, including that the merger would "creat[e] more value for shareholders," that the combined company would be "more valuable" and that Merrill had "dramatically reduc[ed] [its] marks." ¶¶180, 192. These representations were critical to shareholders' evaluation of the merger. *See Virginia Bankshares*, 501 U.S. at 1093; *Gulf Oil*, 725 F. Supp. at 746 (finding actionable statements that transaction was "unique opportunity" and "we view this transaction with a great deal of optimism"); *Novak*, 216 F.3d at 315 (phrases like "in good shape" and "under control" are actionable); *In re Vivendi Universal,*

S.A. Sec. Litig., No. 02 Civ. 5571 (RJH), 2004 WL 876050, at *7 (S.D.N.Y. Apr. 22, 2004) (finding actionable representation that company was "on track" to meet earnings results).[29] In fact, far from being nonactionable, the federal securities laws actually mandate that such statements of opinion about a merger be updated when the executives' attitudes change. *Gulf Oil*, 725 F. Supp. at 746.

Moreover, the materiality of a statement depends on its context. *See Casella v. Webb*, 883 F.2d 805, 808 (9th Cir. 1989) ("What might be innocuous 'puffery' or mere statement of opinion standing alone may be actionable as an integral part of a representation of material fact when used to emphasize and induce reliance upon such a representation."); *Scritchfield v. Cornell*, 274 F. Supp. 2d 163, 175-76 (D.R.I. 2003) (statements "are properly interpreted only by reference to the relevant circumstances"). In the context of the BoA-Merrill merger, it cannot be said that, as a matter of law, a reasonable investor would not have considered Defendants' representations that BoA had a "strong capital position" and that Merrill had "lowered its risk profile" important. After promoting the merger in these terms as the justification to approve it, Defendants cannot now claim that they were merely "vague statements of optimism or

[29] *See also Shapiro v. UJB Fin. Corp.*, 964 F.2d 272, 281-282 (3d Cir. 1992) ("adequate," "cautious," "conservative"); *In re Computer Assocs. Class Action Sec. Litig.*, 75 F. Supp. 2d 68, 73 (E.D.N.Y. 1999) ("business fundamentals are strong"). For this reason, Defendants' reliance on cases like *Grossman v. Novell*, 120 F.3d 1112 (10th Cir. 1997) and *Lasker v. N.Y. State Elec. & Gas Corp.*, 85 F.3d 55 (2d Cir. 1996) is misplaced. Defendants' affirmative and verifiable representations about the value of the merger were far more substantial than the representations of "substantial success" and "commitment to earnings opportunities" involved in those cases. *Grossman*, 120 F.3d at 1121; *Lasker*, 85 F.3d at 59. Similarly, not only were the representations here more concrete than those in *Kane v. Madge Networks, N.V.*, No. C-96-20652-RMW, 2000 WL 33208116, at *2 (N.D. Cal. May 26, 2000), *aff'd*, *Kane v. Zisapel*, 32 Fed. App'x 905 (9th Cir. 2002), but additionally, to the extent that *Kane* held that corporate insiders' positive statements about a merger are presumptively immaterial, as Defendants contend, it is contrary to the Supreme Court's holding in *Virginia Bankshares*.

expressions of opinion."[30] BoA Mem. 49; *see Virginia Bankshares*, 501 U.S. at 1093-94 (recognizing that statements in the merger context are particularly important to shareholders).[31]

Defendants additionally argue that their representation that Merrill had "dramatically" reduced its risk profile was literally true, that they disclosed to investors that they still held some risky assets, and never "guaranteed" that there would not be any further losses. BoA Mem. 65-66. However, Plaintiffs do not allege that Defendants "guaranteed" there would not be any further losses. Rather, Plaintiffs allege that by emphasizing the "dramatic" reduction in risk that Merrill had supposedly undertaken, Defendants misleadingly created the false impression that Merrill was a far stronger and more stable entity than was actually the case, and did so in the context of their efforts to justify the 70% premium BoA had agreed to pay. Thus, Defendants' representations regarding Merrill's risk reduction, "taken together and in context, would have misled a reasonable investor." *McMahan & Co. v. Wherehouse Entm't, Inc.*, 900 F.2d 576, 579 (2d Cir. 1990).

5. The PSLRA Safe-Harbor Does Not Protect Defendants' Pre-Vote Statements Regarding Merrill's Financial Condition

Defendants also argue that certain of their statements were forward-looking and accompanied by meaningful cautionary language, and were thus protected by the PSLRA "safe harbor" provision. *See* BoA Mem. 58, 61.[32] Once again, Defendants are incorrect.

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[30] For these same reasons, *Leykin v. AT&T Corp.*, 423 F. Supp. 2d 229 (S.D.N.Y. 2006) (*cited at* BoA Mem. 61) is inapposite.

[31] Moreover, given BoA's severely deficient due diligence efforts prior to September 15, 2008, Lewis's statements concerning the benefits of the merger lacked any reasonable factual basis. ¶193. For that reason alone, these statements cannot be considered immaterial puffery. *See Hall v. The Children's Place Retail Stores, Inc.*, 580 F. Supp. 2d 212, 229 (S.D.N.Y. 2008) (positive statements about license agreement are not puffery where company had no reasonable basis for them).

[32] These statements include Lewis's statements on September 15 that the Merger would "creat[e] more value for shareholders" or would "create what will be the leading financial institution in the world," (BoA Mem. 58; ¶¶191-92); Price's statement on October 6 that BoA had "considered the Merrill deal" in evaluating its capital position and that BoA believed the offering "covered our anticipated needs from a Merrill standpoint," (BoA Mem. 61; ¶199);

The PSLRA safe harbor, which codified the common-law "bespeaks caution" doctrine, provides that a forward-looking statement is not actionable if it was (1) "accompanied by meaningful cautionary statements," ***and*** (2) not known to be false at the time of issuance. 15 U.S.C. §78u-5(c)(1); *Milman v. Box Hill Sys. Corp.*, 72 F. Supp. 2d 220, 231 (S.D.N.Y. 1999); *Lormand v. US Unwired, Inc.*, 565 F.3d 228, 244 (5th Cir. 2009). However, neither the safe harbor, nor the bespeaks caution doctrine, protects misstatements of *historical* or current fact. *See P. Stolz Family P'ship L.P. v. Daum*, 355 F.3d 92, 97 (2d Cir. 2004); *Vivendi,* 381 F. Supp. 2d at 183 ("By definition, the safe-harbor provision applies to protect only 'forward looking' statements, and not to misrepresentations of historical or current facts."). Moreover, when statements contain "mixed" representations of both future projections and current fact, the aspect of the statement that relates to current fact receives no protection. *In re Stone & Webster, Inc., Sec. Litig.*, 414 F.3d 187, 213 (1st Cir. 2005).

First, Defendants do not – and could not – contend that the PSLRA safe harbor immunizes them from liability for their material omissions, because the PSLRA safe harbor is available only for ***affirmative*** statements. *See In re NTL Inc. Sec. Litig.*, 347 F. Supp. 2d 15, 35 (S.D.N.Y. 2004) (safe harbor does not apply to material omissions or misstatements of historical fact); *Grossman*, 120 F.3d at 1123 ("By definition, the 'bespeaks caution' doctrine applies only to affirmative, forward-looking statements.") (citation omitted).

Second, several of the statements at issue were expressed as statements of contemporaneous fact, and thus do not qualify for PSLRA safe-harbor protection. For example, Lewis's September 15, 2008 statements that the merger constituted a "major grand slam home run" and the companies "are more valuable" together are statements of present fact related to (i)

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and BoA's statement in the Joint Proxy that it had a "strong capital position, funding capabilities and liquidity," as would the combined company (BoA Mem. 61; ¶¶212-13).

the transaction, (ii) the price at which the transaction was executed, and (iii) the present values of BoA and Merrill compared to that of the combined company. Unlike in many of the cases cited by Defendants, these statements are not earnings projections or forecasts. *See*, *e.g.*, *In re Aegon N.V. Sec. Litig.*, No. 03 Civ. 0603 (RWS), 2004 WL 1415973, at *11 (S.D.N.Y. Jun. 23, 2004) (*cited at* BoA Mem. 68).

Moreover, even if viewed as forward-looking, none of these statements qualify for the safe harbor protection because they were not accompanied by meaningful cautionary language. Cautionary language must "precisely address" the substance of the specific statement that is at issue. *In re Prudential Sec. Inc. Ltd. P'ships Litig.,* 930 F. Supp. 68, 72 (S.D.N.Y. 1996); *see also Vivendi*, 381 F. Supp. 2d at 183 (internal citation and quotation omitted); *NTL*, 347 F. Supp. 2d at 36 n. 119; *Schottenfeld Qualified Assoc. v. Workstream, Inc.*, No. 05 Civ. 7092 (CLB), 2006 WL 4472318, at *3 (S.D.N.Y. May 4, 2006) (finding insufficient cautionary language that "refers to the most general of economic risks").[33] Generic, boilerplate statements are insufficient. *In re Veeco Instruments, Inc., Sec. Litig.*, 235 F.R.D. 220, 235 (S.D.N.Y. 2006).

Here, Defendants warned on September 15 of generalized "risks and uncertainties" and that "various factors 'may cause actual results or earnings to differ materially from such forward-looking statements.'" BoA Mem. 59-60. These boilerplate warnings were simply insufficient to warn investors that as of the date of the vote BoA was so unconvinced regarding the fundamental wisdom of the merger that they were discussing scrapping the deal entirely, nor did they warn that Merrill's losses could render it bankrupt and force BoA to the brink of insolvency. For the same reasons, the boilerplate "forward-looking statements warning" (similar to that described

[33] *Fort Worth Employers' Ret. Fund v. Biovail Corp.*, 615 F. Supp. 2d 218 (S.D.N.Y. 2008) (*cited at* BoA Mem. 60) is not to the contrary because that case concerned disclosures which clearly addressed the facts at issue. *See also In Re Duane Reade Inc. Sec. Litig*, No. 02 Civ. 6478 (NRB), 2003 WL 22801416, at *6 (S.D.N.Y. Nov. 25, 2003) (*cited at* BoA Mem. 60) ("defendants released specific cautionary statements regarding front-end sales, new store opening costs and inventory shrink" at the heart of the alleged fraud).

above), which accompanied Price's claims on October 6 that BoA had "considered the Merrill deal" and that the Offering "covered [BoA's] anticipated needs from a Merrill standpoint," was entirely insufficient. This standard warning provided no notice to investors that Merrill's ballooning losses threatened to cripple both companies.[34]

Furthermore, Defendants cannot avail themselves of the PSLRA "safe harbor" provision where the risks they allegedly warned of had already materialized. *See Rombach*, 355 F.3d at 173; *Prudential,* 930 F. Supp. at 172. Here, by the time investors received the cautionary language contained in the Joint Proxy (BoA Mem. 61-62), Merrill had ***already*** suffered $7 billion in losses, and was on its way to suffering more than $15 billion in losses by the date of the vote. Nor could any warnings protect the November 26 Letter, which assured investors as to the strength of BoA's capital position when in reality, senior executives at BoA had acknowledged that the bank was "very thinly capitalized" and the federal regulators looking at BoA's financials had determined that BoA was "clearly not [] well prepared" for further deterioration." ¶103.

Finally, contrary to Defendants' claims (BoA Mem. 60), no amount of cautionary language can protect Defendants' statements if they were made with actual knowledge of their falsity. *See Lormand*, 565 F.3d at 244; *In re SeeBeyond Techs. Corp. Sec. Litig.*, 266 F. Supp. 2d 1150, 1166 (C.D. Cal. 2003).[35] A forward-looking statement is "false" if it is made without a reasonable basis. *See, e.g.*, *IBM*, 163 F.3d at 109; *Time Warner*, 9 F.3d at 266. Therefore,

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[34] Defendants cannot rely upon the risk warnings contained in the October 7, 2008 Prospectus Supplement to absolve them of liability under Section 14(a) (*see* BoA Mem. 60) because (1) Plaintiffs' claims under Section 14(a) do not include misstatements or omissions in the October 7, 2008 Prospectus Supplement, and (2) the October 7, 2008 Prospectus Supplement was not incorporated by reference into the Joint Proxy. *See Desai v. General Growth Props., Inc.*, No. 09 C 487, 2009 WL 2971065, at *4 (N.D. Ill. Sept. 17, 2009) ("To determine whether a statement was accompanied by meaningful cautionary language, courts consider cautionary statements that either accompanied the forward-looking statement or were incorporated by reference.").

[35] *See also Milman*, 72 F. Supp. 2d at 231; *NovaGold*, 629 F. Supp. 2d at 291; *South Ferry LP No. 2 v. Killinger,* 399 F. Supp. 2d 1121, 1130-35 (W.D. Wash. 2005), *vacated in part*, 542 F.3d 776 (9th Cir. 2008).

"actual knowledge" of falsity means that the speaker knew that the prediction lacked a reasonable basis. *See In re Indep. Energy Holdings PLC Sec. Litig.*, 154 F. Supp. 2d 741, 757 (S.D.N.Y. 2001), *abrogated on other grounds by Initial Pub. Offerings Sec. Litig.*, 241 F. Supp. 2d 281 (S.D.N.Y. 2003). Thus, for example, contrary to Defendants' claims (BoA Mem. 66), Lewis knew that his statement that Merrill "had the liquidity and capacity to see [the crisis] through" (¶185) lacked a reasonable basis because he knew that BoA had not performed adequate due diligence. As Plaintiffs argue in Sections III.C. 1-3, *infra*, the Complaint amply demonstrates that certain Defendants. actually knew that their other statements were false.

6. Investors Were Entitled To Rely On Defendants' Representations In The Merger Agreement And Joint Proxy That A MAC Had Not Occurred

As they did with respect to the representations in the Merger Agreement and Joint Proxy regarding bonuses, Defendants argue that shareholders were not entitled to rely on the false statements in those documents which "warranted" that Merrill had undergone no "material adverse change" as of the date of the Joint Proxy, and that this would remain true "as of the Effective Time [*i.e.*, the closing of the merger on January 1]." ¶¶88, 207; *see also* Goldin Dec., Ex. 1 at 98, 163, 190 Specifically, Defendants argue that this critical representation was only a "contractual allocation of risk" that existed solely for the benefit of BoA and Merrill, and that no reasonable shareholder would have relied on it. *See* BoA Mem. at 14, 52. Defendants further argue that no reasonable shareholders would have relied on these provisions because the Joint Proxy warned that the MAC representations were "subject to important qualifications and limitations agreed to between the parties." BoA Mem. 52. These arguments should be rejected for the reasons set forth above at Sections II.C. 3-4. *See, e.g., Glazer*, 549 F.3d at 74.

E. Additional False And Misleading Statements And Omissions Prior To Vote

1. Adequacy Of BoA's Due Diligence

Plaintiffs allege that when Lewis and Price announced the merger on September 15, they made a series of false statements regarding the due diligence BoA purportedly conducted on Merrill before agreeing to the deal, including that: (i) BoA's due diligence of Merrill was "very, very extensive"; (ii) BoA's financial advisor, J.C. Flowers, had "very comprehensively" analyzed Merrill's marks; and (iii) BoA's due diligence had determined that Merrill had a "much lower risk profile" because it had "dramatically reduc[ed] [its] marks." ¶¶179-81. In response to direct questions by analysts about the adequacy of the due diligence, Lewis and Price assured investors that BoA was extremely familiar with Merrill's risk profile as BoA and Merrill shared a "very similar methodology valuations" and "very similar marks." ¶¶179, 181. These statements were highly material to investors, particularly given the abbreviated merger discussions, and the questions surrounding Merrill's financial condition at the time of the announcement.

As the Complaint alleges, contrary to these statements, Lewis later admitted to federal regulators that "they [BoA] did not do a good job of due diligence" before agreeing to purchase Merrill for a hefty premium, and federal regulators themselves concluded, after reviewing the same Merrill internal risk management reports that BoA had purportedly reviewed during its due diligence, that BoA's due diligence had been grossly inadequate. ¶¶117, 122, 182, 184. In fact, Chairman Bernanke himself testified that, when Lewis informed him that he was going to invoke the MAC, he told Lewis that doing so would cast doubt in the minds of financial market participants . . . about the due diligence and analysis done by the company." ¶125.

Thus, these statements are actionable. *See Freedman v. Value Health, Inc.*, 958 F. Supp. 745, 757 (D. Conn. 1997); *In re Cendant Corp. Sec. Litig.,* 60 F. Supp. 2d 354, 371 (D.N.J.

1999) (false statements regarding extent of due diligence actionable). Further, because Defendants' statements were "without a basis in fact," they were at a minimum, negligent. *In re Oxford Health Plans, Inc., Sec. Litig.*, 187 F.R.D. 133, 141 (S.D.N.Y. 1999) (quoting *IBM*, 163 F.3d at 109).

In response, Defendants contend that shareholders and investors should not have believed these statements because they were aware that the due diligence "was conducted over a single weekend." BoA Mem. 63. However, the due diligence assurances were made in direct response to questions by analysts who expressed concern about this exact point, namely, the abbreviated discussions. ¶179. In response to these questions, Defendants provided the market with specific reasons why this was not a concern, including reliance on financial advisors who were familiar with Merrill, as well as their own pre-existing familiarity with Merrill's books and methodology. ¶¶179-181. After repeatedly assuring investors that they should *not* be concerned about the compressed time period, Defendants cannot now point to those same circumstances to shield themselves from liability.[36]

Defendants also claim that their statements regarding BoA's due diligence were "too general" for investors to rely on and that their statements did not act as a "guarantee" against later losses. BoA Mem. 63-64. But the Complaint does not allege that the statements were guarantees; the Complaint alleges that they were specific and objectively verifiable statements about BoA's due diligence process, which had already been completed, including: (i) what areas were reviewed ("asset valuations, trading positions," and "marks"); (ii) BoA's familiarity with

[36] *Olkey v. Hyperion 1999 Term Trust, Inc.*, 98 F.3d 2, 5 (2d Cir. 1996) (*cited at* BoA Mem. 63) is inapposite. Though that case did direct courts to look at the challenged statements in context (when applying the "bespeak[s] caution" doctrine to forward-looking statements), it held that the statements would only be immunized when the *exact* risk of which the plaintiff complained was disclosed. *See id.* at 5. Nowhere do Defendants contend that they "warned" investors that their due diligence was inadequate and, in any event, the bespeaks caution doctrine does not apply to representations of historical fact.

Merrill's business and exposures (BoA and Merrill shared "very similar methodology valuations" and "very similar marks" and dealt with "the same counterparties"); and (iii) Merrill's risk profile (Merrill had "dramatically reduc[ed] their marks" and had "a much lower risk profile."). ¶¶179-81. These are precisely the kind of statements that are regularly found to be both material and actionable by the courts. *See, e.g.*, *In re McKesson HBOC Sec. Litig.*, 126 F. Supp. 2d 1248, 1266 (N.D. Cal. 2000) (representations regarding the types of materials reviewed during the diligence process are actionable); *In re Moody's Corp. Sec. Litig.*, 599 F. Supp. 2d 493 (S.D.N.Y. 2009), *corrected on denial of recons.*, 612 F. Supp. 2d 397 (S.D.N.Y. 2009) (statements actionable where they "were neither 'vague' nor 'non-specific pronouncements' that were incapable of 'objective verification'") (citation omitted).[37]

Third, Defendants' efforts to characterize their statements as non-actionable "opinions" also must fail. BoA Mem. 62, 64. As discussed above, the mere fact that a statement is phrased in non-quantifiable terms does not render it inactionable; rather, a statement is misleading if it is not "consistent with reasonably available data." *Novak*, 216 F.3d at 309. Here, Federal Reserve officials reviewing the ***same materials*** that BoA was required to review as part of its due diligence process concluded that BoA's due diligence had been poor, because those materials clearly showed Merrill's instability and exposure to tens of billions of dollars of toxic assets. ¶117. Indeed, these officials concluded based on these facts that Lewis's claim of surprise at the size of Merrill's losses was "not credible," and that "[a]t a minimum, it calls into question the adequacy of the due diligence process [BoA] has been doing in preparation for the takeover."

[37] *ECA and Local 134 IBEW Joint Pension Trust of Chicago v. JP Morgan Chase Co.,* 553 F.3d 187 (2d Cir. 2009) and *San Leandro Emergency Medical Profit Sharing Plan v. Phillip Morris Cos., Inc.*, 75 F.3d 801 (2d Cir. 1996) are inapposite. In *ECA,* the court held that statements regarding the risk management and integrity were the same general boilerplate issued by every company. 553 F.3d at 206. Here, however, Lewis's and Price's statements were far from boilerplate, as explained above. Moreover, the statements at issue in both *ECA* and *San Leandro* dealt with the defendants' policies and goals. 75 F.3d at 811. Here, Lewis's and Price's statements were historical representations about a process that had already occurred.

Id. This is more than sufficient evidence, at the pleading stage, to show that Defendants' representations about their due diligence were false.[38]

Moreover, even assuming, *arguendo*, that Lewis may have believed that BoA's due diligence was adequate on September 15, Plaintiffs clearly allege that, as Merrill's losses continued to spiral out of control, Lewis no longer believed that opinion to be accurate. As such, Lewis came under a duty to correct his earlier statements. *See Burlington*, 114 F.3d at 1431; *Overton v. Todman & Co., CPAs, P.C.*, 478 F.3d 479, 486-87 (2d Cir. 2007).

Finally, Defendants contend that Plaintiffs plead "fraud by hindsight" by relying on the analysis of BoA's and Merrill's internal documents conducted by regulators at the Federal Reserve after the Merger Agreement was signed. *See* BoA Mem. 64. Defendants are mistaken. "[T]he Second Circuit has explicitly recognized that plaintiffs may rely on post-class period data to confirm what a defendant should have known during the class period." *Vivendi*, 2004 WL 876050, at *6 (*citing, e.g., Scholastic,* 252 F.3d at 72).

2. False Statements Regarding Merrill's Capacity To Withstand The Financial Crisis

Plaintiffs allege that, in response to questions concerning why BoA had agreed to pay such a substantial premium for Merrill, Lewis justified the price by representing that "probably . . . Merrill had the liquidity and the capacity to see this [the financial crisis] through" and "more likely than not, they would have seen this through and come out on the other side." ¶185. These statements were false because they were made without a reasonable basis. *See, e.g., Oxford Health*, 187 F.R.D. at 141 ("An opinion may . . . be actionable . . . if it is without a basis in fact

[38] To the extent that Defendants claim that the falsity of their "opinions" depends on a showing of both "objective" and "subjective" falsity, this is incorrect. A statement of opinion is false if it is made without reasonable basis, *or* is not reasonably believed at the time it is issued. *See IBM*, 163 F.3d at 109; *Zemel Family Trust v. Philips Int'l Realty Corp.,* No. 00-CV-7438 MGC, 2000 WL 1772608, at *8 (S.D.N.Y. Nov. 30, 2000) (*citing Herskowitz v. Nutri/System, Inc.*, 857 F.2d 179, 184 (3d Cir. 1988)); *Oxford Health Plans,* 187 F.R.D. at 141. In any event, Plaintiffs have demonstrated that Defendants' were aware that BoA's due diligence was inadequate – therefore, whatever standard is used, Plaintiffs have stated a claim.

. . . [or if] the speakers were aware of any facts undermining the accuracy of these statements."). In reality, Merrill did not have the liquidity and capacity to see the financial crisis through. Indeed, Thain, Merrill's CEO, has testified that Merrill would have been effectively insolvent as of September 15, 2008 but for the proposed merger. ¶¶62, 186. This is, in fact, exactly why regulators pressured the parties to complete the deal quickly. ¶65. Furthermore, because BoA did not do an adequate job of due diligence (as Lewis knew and acknowledged to regulators), Lewis did not have a reasonable basis for believing this statement to be true. ¶¶182-183.

In response, Defendants first make the red-herring argument that this statement is inactionable because "a statement about what might have happened if things were different is incapable of being true or false when made." BoA Mem. 66. But this is simply not so. "Securities laws approach matters from an *ex ante* perspective." *Burlington*, 114 F.3d at 1429 n.16. Regardless of how opinions turn out, the relevant inquiry is whether they were "reasonable ***at the time they were made***." *Id.* Here, there was no reasonable basis for Lewis's statement, given the clear testimony of Merrill's CEO concerning its financial condition. Moreover, the representation was not a projection about a hypothetical future, but was instead a ***current*** representation about Merrill's then-existing financial condition. *See Stone & Webster,* 414 F.3d at 213 ("The mere fact that a statement contains some reference to a projection of future events cannot sensibly bring the statement within the safe harbor if the allegation of falsehood relates to non-forward-looking aspects of the statement.").[39]

[39] Defendants argue that Lewis's statements are inactionable because "Plaintiffs fail to plead particularized facts sufficient to support an inference of fraudulent intent." BoA Mem. 66. This is incorrect. *See IBM*, 163 F.3d at 109 (opinions are false if made without reasonable basis). Moreover, though scienter is not necessary for a Section 14(a) claim, as set forth below in Section III.C.3-5 in connection with their Section 10(b) claims, Plaintiffs have alleged sufficient facts to give rise to a strong inference that Lewis's statements were made with fraudulent intent.

3. Statements Regarding Regulator Pressure and Thain's Self-Interest

Lewis also made false and misleading statements regarding the merger negotiations on September 15, 2008. ¶¶187-90. In this respect, an analyst specifically asked whether federal regulators had pressured the parties to get the deal done quickly. ¶187. In response Lewis said, "there was absolutely no pressure." ¶187. In reality, federal regulators, including Secretary Paulson, exerted significant pressure to finalize the Merger Agreement before the markets opened on Monday, September 15, 2008. ¶¶65, 188. Specifically, while the deal was being negotiated, Secretary Paulson was in constant communication with Thain and made it clear that he "was adamant the deal had to be done by Monday morning," and told Thain, "John, you'd better make sure this happens." *Id.*

Defendants do not contest these facts, nor do they contest the materiality of the statement. Rather, they claim that ***Lewis*** personally was not pressured by the Government to get the deal done by Monday morning. BoA Mem. 66-67. This argument is irrelevant, because the Complaint does not allege that Lewis falsely stated that there was no pressure ***solely*** on him or BoA to complete the deal – rather, he falsely stated that there was "absolutely no pressure" to complete the deal. Moreover, it is simply not credible that BoA (and Lewis) completed its due diligence and agreed to buy Merrill for a 70% premium in the span of 36 hours without being aware of the U.S. Government's insistence that the deal be done quickly.

Second, Lewis's denial of Thain's pursuit of his own self-interest during the merger negotiations was also false and misleading when made. ¶¶189-90. Indeed, Thain attempted to secure himself a $40 million bonus as part of the secret bonus agreement that delayed the signing of the Merger Agreement until 2 a.m. Monday morning. ¶¶67-68, 78, 190. Lewis later admitted that Thain's self-interested attempts to secure large bonuses for himself and his executives were

"petty kind of things and selfish things" that took over the negotiations and ruined the celebratory toast he had hoped to enjoy. ¶78.

Defendants largely ignore these facts. Instead, their principal argument is that Lewis was responding only to a question regarding Thain's ***role*** in the combined company and his statement cannot possibly be read in a broader fashion. BoA Mem. 67. This attempt to narrow Lewis's statement must fail as it is entirely based upon making a factual finding from materials outside the Complaint, particularly where the transcript of the conference call set forth in these extraneous materials does not support Defendants' inference.[40] Moreover, Lewis's statement is an actionable assertion of fact – a false one at that given Thain's efforts to secure a $40 million bonus – and not a statement of Lewis's opinion, as Defendants contend. *See* BoA Mem. 67.

F. Defendants' Remaining 14(a) Arguments Have No Merit

1. Defendants' Statements Constituted Proxy Solicitations

It is clear that the following communications from BoA and Merrill to investors prior to the filing of Proxy and Merger Agreement constituted proxy solicitations: (i) the September 15, 2008 Press Release; (ii) the September 15, 2008 Investor Call and Press Conference; (iii) the September 18, 2008 Forms 8-K; and (iv) Merrill's October 16, 2008 Press Release. ¶329.[41]

First, because the Joint Proxy specifically incorporated by reference the above-mentioned documents, the statements contained therein are solicitations. *See* 17 C.F.R. §240.14a-101 Note D (material incorporated into a proxy statement constitutes the proxy statement).

Second, Thain's statements on September 15 and October 16, 2008 were solicitations under the proxy rules. ¶¶191, 192, 202. The SEC broadly defines "solicitation" to "include…

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[40] In fact, the transcript does not provide the question to which Lewis was responding. *See* Goldin Decl., Exhibit 13, Page 3 ("Unidentified Audience Member: John, (inaudible) you say?").

[41] Only Thain and Merrill raise the issue, while the BoA Defendants concede that all of these communications were proxy solicitations under the proxy rules.

[any] communication to security holders under circumstances reasonably calculated to result in the procurement, withholding or revocation of a proxy." 17 C.F.R. §240.14a-1(*l*)(iii). The Second Circuit has held that this broad definition applies "not only to direct requests to furnish, revoke or withhold proxies, but also to communications which may indirectly accomplish such a result or constitute a step in a chain of communications designed ultimately to accomplish such a result." *Long Island Lighting Co. v. Barbash*, 779 F.2d 793, 796 (2d Cir. 1985); *Capital Real Estate Investors Tax Exempt Fund Ltd. P'ship v. Schwartzberg,* 929 F. Supp. 105, 110 (S.D.N.Y. 1996) ("*Capital Real Estate*") (same); *Krauth v. Exec. Telecard, Ltd.*, 870 F. Supp. 543, 547 (S.D.N.Y. 1994) (same). Thus, "[i]f the issuer makes a recommendation or makes other statements that reasonably portray the transaction in a favorable light – [*i.e.*,] presents the transaction in a manner objectively likely to predispose security holders toward or against it – it must comply with the proxy rules." *Capital Real Estate*, 929 F. Supp. at 114; *Winiger v. SI Management L.P.*, 32 F. Supp. 2d 1144, 1148 (N.D. Cal. 1997) (same).[42]

Thain's statements on September 15 and October 16, 2008 indisputably "portrayed the transaction in a favorable light" and were "a step in the chain of communications designed to" ultimately procure shareholder approval of the merger. For example, Thain's statements on September 15 emphasized his favorable view of the merger, stating that the merger "makes tremendous strategic sense," provides both companies with "great opportunities," and creates "the leading financial firm in the world," and described the merger as "a very attractive transaction from a shareholder point of view." ¶¶191-92. Likewise, Thain's statement on October 16, 2008 regarding Merrill's continued efforts to reduce exposures to risky assets and de-leverage the balance sheet presented the merger in a favorable light. ¶202. As such, these

[42] At a minimum, the question of whether the communications described above were proxy solicitations is a question of fact that cannot be resolved at the pleading stage. *See Long Island Lighting Co.*, 779 F.2d at 796.

statements were proxy solicitations and are actionable under Section 14(a). *See, e.g.*, *Bender v. Jordan*, 439 F. Supp. 2d 139, 166 (D.D.C. 2006) (letter was solicitation even though it did not "explicitly urg[e] a vote" because it "lauded the 'imagination and courage'" of proposed slate of directors); *Winiger*, 32 F. Supp. 2d at 1148; *Mason-Dixon Bancshares, Inc. v. Anthony Invs., Inc.*, No. Civ.A. CCB-96-3836, 1997 WL 33482710, at *5 (D. Md. Mar. 3, 1997); *Capital Real Estate*, 929 F. Supp. at 107, 110 (press release was proxy solicitation where it "focus[ed] on the premium" inherent in merger offer and announced defendant's belief that offer was "excellent").[43]

2. Merrill And Thain Are Liable For The False Statements And Omissions In The Proxy

Defendants Merrill and Thain argue that because they owed a fiduciary duty only to Merrill's shareholders, they owed no disclosure duty to BoA's shareholders. Merrill Mem. at 3-5, 13-14. This argument ignores the fact that, by its express terms, Section 14(a) imposes the broad disclosure duties described above on "any person" who solicits "any proxy" – regardless of whether such person owes a fiduciary duty to the shareholders being solicited. *See, e.g.*, *SEC v. Falstaff Brewing Corp.*, 629 F.2d 62, 69 (D.C. Cir. 1980) (individual seeking to become the majority shareholder in a company was liable under Section 14(a) even though he had no fiduciary duty). Consistent with the plain language of Section 14(a), courts routinely hold that a party to a merger is liable to its counterparty's shareholders for any false or misleading statement or omission made in a joint proxy statement. *See Gerstle, 478 F. 2d at 1284* (Skogmo, the acquirer, liable to target GOA's shareholders)*; In re AOL Time Warner, Inc. Sec. & ERISA*

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[43] Thain did not "merely describe the merger" to BoA and Merrill shareholders; instead Thain actively encouraged BoA and Merrill shareholders to approve the merger. *See* Merrill Mem. at 12. As a result, the Merrill Defendants' reliance on *Smallwood v. Pearl Brewing Co.*, 489 F.2d 579 (5th Cir. 1974) is misplaced. *See Winiger,* 32 F. Supp. 2d at 1148. Moreover, because Thain made these statements in his capacity as Merrill's CEO, Merrill is liable for Thain's solicitations.

Litig., 381 F. Supp. 2d 192, 232 (S.D.N.Y. 2004) (AOL liable to Time Warner shareholders); *Freedman*, 135 F. Supp. 2d at 339 (Value Health liable to Diagnostek shareholders); *McKesson HBOC,* 126 F. Supp. 2d at 1266 (N.D. Cal. 2000) (HBOC directors liable to McKesson shareholders). As these authorities make clear, the relevant inquiry is whether Defendants Merrill and Thain permitted their names to be used in connection with misleading solicitations to BoA's shareholders, which they did.[44] No fiduciary relationship is required and, in fact, Section 14(a) contemplates that such a relationship will often be absent in the merger context.[45]

Merrill also argues that it owed no disclosure duty to BoA's shareholders because it made no affirmatively misleading statement in the Joint Proxy that was "unique" to Merrill. Merrill Mem. at 13-14. However, neither Section 14(a) nor Rule 14a-9 requires that the statements at issue be "unique" to one particular merger partner. Even if this requirement existed, the misleading statements concerning an "absence of material adverse changes" in Merrill's financial condition, Merrill's agreement to "not" pay bonuses, and the combined company's "strong" capital position put Merrill's financial condition directly at issue.

Merrill and Thain speciously argue that "placing a duty on Merrill to disclose information to [BoA]'s shareholders that is equally known to BoA would create an irreconcilable tension with the duty that Merrill owed to its own shareholders in connection with the merger." Merrill Mem. 4-5, 15; Thain Mem. 9. In essence, these Defendants argue that the securities laws allow

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[44] Thain argues that the Joint Proxy was not "joint" because Merrill and BoA filed the same Proxy separately. Thain Mem. at 8-9 & n.4. The Joint Proxy was clearly "joint" because it contained both companies' logos, a cover letter signed jointly by Lewis and Thain, the recommendations of both companies' Boards, and the same text. *See, e.g.*, *Tracinda Corp. v. DaimlerChrysler AG*, 364 F. Supp. 2d 362, 393 n.7 (D. Del. 2005), *aff'd*, 502 F.3d 212 (3d Cir. 2007) (Chairman of DaimlerBenz liable because his "name figures prominently into the Proxy/Prospectus"); *AOL Time Warner*, 381 F. Supp. 2d at 232 (rejecting argument that AOL defendants were not liable to Time Warner shareholders where proxy contained both companies' logos and signatures of both CEOs).

[45] *Chiarella v. United States*, 445 U.S. 222 (1980), is not to the contrary. That case concerned one *particular* situation which gives rise to a duty to disclose; it did not purport to identify all situations in which disclosure duties arise, and had nothing to do with Section 14(a) or Rule 14a-9.

one company to mislead its counterparty's shareholders while soliciting their approval of a merger. The plain language of Section 14(a) and the cases cited above make clear the law is exactly the opposite: both parties soliciting shareholder approval of a merger have a duty to their counterparty's shareholders to disclose all material facts relating to the transaction, and to otherwise speak accurately and completely.

3. Section 14(a) Permits Plaintiffs To Bring Their Claims Directly

Finally, in a last-ditch effort to evade liability, Defendants contend that, according to Delaware law, Section 14(a) claims brought on behalf of shareholders who "did not buy, sell, or exchange their shares" must be pleaded derivatively. BoA Mem. 70. Delaware law, however, does not govern the question of whether Plaintiffs' Section 14(a) claim is derivative or direct. In *J.I. Case & Co.* v. *Borak*, the Supreme Court held that Section 14(a) claims can be direct, derivative ***or*** both and squarely rejected the argument that the question of rights and remedies under Section 14(a) was dictated by state law. *See* 377 U.S. at 431 (noting that "federal law. . . control[s]"). The Court emphasized the danger of permitting state law to govern: "if the law of the State happened to attach no responsibility to the use of misleading proxy statements, the whole purpose of the section [14(a)] might be frustrated." *Id.* at 434-35.

Thus, under federal law, plaintiffs may choose to plead their claims directly under Section 14(a), and courts award such relief as they believe appropriate. *Mills*, 396 U.S. at 388-89. In the forty-five years since *Borak*, courts have been clear that Section 14(a) claims can be brought both directly and derivatively.[46] The Ninth Circuit explained:

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[46] Courts frequently permit Section 14(a) claims in the merger context to proceed directly, without any inquiry into what state law would allow. *See Mills*, 396 U.S. at 385; *Mendell*, 927 F.2d at 679; *AOL Time Warner*, 381 F. Supp. 2d at 232, 241; *Tracinda v. DaimlerChrysler AG*, 197 F. Supp. 2d 42, 72-73 (D. Del. 2002); *Cendant*, 60 F. Supp. 2d at 378. Even in *Borak*, the plaintiff-shareholder challenged a proxy that had been used to solicit a merger, and the Supreme Court was unconcerned as to whether the claim was pleaded directly or derivatively. *See Borak*, 377 U.S. at 431.

> While it is true that [*Borak*] suggests that the primary injury pursuant to a deceptive proxy flows from damage done to the corporation, it is also true that *Borak* explicitly recognizes the right of a shareholder to bring both direct and derivative actions . . . . We therefore hold that in light of . . . Borak, ***a shareholder who alleges a deceptive or misleading proxy solicitation is entitled to bring both direct and derivative suits.*** The former action protects the shareholders' interest in "fair corporate suffrage."

Yamamoto v. Omiya, 564 F.2d 1319, 1325-1326 (9th Cir. 1977).

Courts routinely permit claims based on mergers to be brought directly under Section 14(a).[47] *See, e.g.*, *McKesson*, 126 F. Supp. 2d at 1262-68 (shareholders of acquiring company may advance direct Section 14(a) claims for accounting fraud at target company).[48] Here, Plaintiffs allege that they were "denied the opportunity to make an informed decision" due to a false proxy. ¶349. Thus, Plaintiffs have alleged that they were denied "fair corporate suffrage," and have stated a direct claim under Section 14(a). *See Edge Partners, L.P. v. Dockser*, 944 F. Supp. 438, 440-41 (D. Md. 1996) ("Inasmuch as Plaintiff has adequately alleged § 14(a) violations, it may bring a direct cause of action . . . ").

Tellingly, Defendants do not cite a single Section 14(a) case that holds that the availability of direct claims arising from a merger is governed by state law.[49] Rather, Defendants chiefly rely on *In re J.P. Morgan Chase & Co. Shareholder Litigation*, 906 A.2d 766 (Del.

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[47] Outside the merger context, as well, courts regularly allow federal Section 14(a) claims to proceed directly, even while simultaneously scrutinizing parallel state claims to determine if state law requires those claims to be pled derivatively. *See, e.g.*, *Washtenaw County Employees Ret. Sys. v. Wells Real Estate Inv. Trust, Inc.*, No. 1:07-cv-862-CAP, 2008 WL 2302679, at *3-4 (N.D. Ga. Mar. 31, 2008); *Bender v. Jordan*, 439 F. Supp. 2d 139, 164, 172 (D.D.C. 2006); *City of St. Clair Shores Gen. Emples. Ret. Sys. v. Inland West Retail Real Estate Trust, Inc.*, 635 F. Supp. 2d 783, 793-94, 797-98 (N.D. Ill. 2009). Other courts have carefully examined standing requirements for direct and derivative claims under Section 14(a) without making even the slightest reference to state law. *Stahl v. Gibraltar Fin. Corp.*, 967 F.2d 335, 338 (9th Cir. 1992); *Cowin v. Bresler*, 741 F.2d 410, 425 (D.C. Cir. 1984).

[48] The *McKesson* court ultimately dismissed the Section 14(a) claims on technical pleading grounds, but stated that, "it should be a relatively simple matter to restate the Section 14(a) allegations in the proper form." *Id.* at 1268 n.10.

[49] Defendants also rely on District Judge Fogel's opinions in two option-backdating cases, *Kelley v. Rambus*, *Inc.*, No. C07-1238 JF (HRL), 2008 WL 5170598 (N.D. Cal. Dec. 9, 2008) and *Vogel v. Jobs*, No. C06-5208 JF, 2007 WL 3461163 (N.D. Cal. Nov. 14, 2007) to support their argument that Section 14(a) is governed by Delaware law. Both cases simply assume that state law controls the issue, without providing any analysis of whether Section 14(a) is governed by federal law.

2006), wherein the Delaware Supreme Court dismissed direct state law claims brought by shareholders of an acquiring corporation based on misleading statements in the proxy. Defendants fail to point out, however, that in the ***federal*** action a year later, the court sustained direct Section 14(a) claims based on the same merger. *See In re JPMorgan Chase & Co. Secs. Litig.*, No. 06 C 4674, MDL No. 1783, 2007 WL 4531794, at *11-12 (N.D. Ill. Dec. 18, 2007). In so doing, the court deferred to the Delaware case when examining claims alleging ***state*** breaches of fiduciary duty, ***but did not*** defer to Delaware law when determining the scope of the federal Section 14(a) cause of action.[50]

Finally, even if resort to state law were appropriate, Plaintiffs have properly stated a direct claim under Section 14(a). Delaware law asks: "(1) who suffered the alleged harm (the corporation or the suing stockholders, individually); and (2) who would receive the benefit of any recovery or other remedy (the corporation or the stockholders, individually)?" *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1033 (Del. 2004).[51] Proxy disclosure violations harm individual shareholders directly by denying shareholders (and not the corporation) the right to a fully informed vote. *See In re Tyson Foods, Inc. Consol. S'holder Litig.*, 919 A.2d 563, 601-02 (Del. Ch. 2007). Plaintiffs seek damages related to the decline of BoA's stock price and other relief for their personal injuries suffered directly as a result of a vote obtained by the material misstatements made in the Defendants' proxy solicitations, not

[50] *Kamen v. Kemper Fin. Servs.*, 500 U.S. 90 (1991) and *Strougo v. Bassini*, 282 F.3d 162 (2d Cir. 2002) (*cited at* BoA Mem. at 71), are inapposite. *Kamen* and *Strougo* hold that where a federal statute is ***silent*** on an issue, it is appropriate to look to state law. *See Kamen*, 500 U.S. at 97-98; *Strougo*, 282 F.3d at 167-68. As *Borak* and its progeny have made clear, Section 14(a) is not silent. *See, e.g.*, *Yamamoto*, 564 F.2d at 1326. Moreover, both *Kamen* and *Strougo* recognize that federal courts ***should not*** apply state law where "application of the particular state law in question would frustrate specific objectives of the federal programs," *Strougo*, 282 F.3d at 168 (quoting *Kamen*, 500 U.S. at 98) – which is precisely what *Borak* held would occur if state law governed this question. *See Borak*, 377 U.S. at 434-35.

[51] Delaware law allows certain claims to be brought both directly and derivatively. *See Gentile v. Rossette*, 906 A.2d 91, 99-100 (Del. 2006).

restitution of an "overpayment" for Merrill stock, nor are they seeking recovery of the "pro rata" economic value of corporate assets. *Feldman v. Cutaia,* 951 A.2d 727, 733 (Del. 2008). The proximate harm to BoA shareholders flowing from the merger vote was the decline in the price of their common shares when the true facts concerning the merger were ultimately revealed. ¶¶261-272, 334, 349, 359. Therefore, because Plaintiffs are not seeking "derivative" damages in the form of their "pro rata" share of corporate assets (*Feldman,* 951 A.2d 727, 733), they would "receive the benefit of any recovery" and their claims are properly characterized as direct. *Tooley*, 845 A.2d at 1033.

III. PLAINTIFFS HAVE STATED CLAIMS UNDER SECTION 10(b)

A. Pleading Standards And Elements Of The Claim

To state a claim under Section 10(b) and Rule 10b-5, a plaintiff must allege: "(1) a material misstatement or omission, (2) scienter, (3) a connection with the purchase or sale of a security, (4) reliance . . . (5) economic loss, and (6) loss causation." *In re Salomon Analyst Metromedia Litig.*, 544 F.3d 474, 478 n.1 (2d Cir. 2008) (quotations omitted). Federal Rule of Civil Procedure 9(b) requires that the Complaint "(1) specify the statements that the plaintiff contends were fraudulent, (2) identify the speaker, (3) state where and when the statements were made, and (4) explain why the statements were fraudulent." *Novak*, 216 F.3d at 306 (citation and quotations omitted). Similarly, Section 78u-4(b)(1) of the PSLRA requires a complaint to "specify each statement alleged to have been misleading [and] the reason or reasons why the statement is misleading." It is well-established that a violation of another statute's disclosure requirements or SEC disclosure regulations will satisfy the falsity element of a Section 10(b) claim. *See Scholastic*, 252 F.3d at 70-71; *accord Lockspeiser v. Western Maryland Co.*, 768 F.2d 558, 561-62 (4th Cir. 1985) (material omission in proxy triggers liability under both Section

14(a) and Section 10(b)).[52] Therefore, Defendants' misrepresentations and failures to disclose material facts pursuant to Section 14(a) and Rule 14a-9 also rendered their statements materially false and misleading for Section 10(b) purposes.

B. The Complaint Adequately Alleges That Defendants Made False And Misleading Statements And Failed To Disclose Material Information During The Period Of September 15, 2008 Through December 5, 2008

As described above in Section II, Plaintiffs have alleged actionable misstatements and omissions by, among others, the BoA Defendants, Merrill and Thain, during the period of September 15, 2008 through the date of the shareholder vote, on December 5, in support of their Section 14(a) claims. These statements and omissions also give rise to claims under Section 10(b) because, in addition to being pled with the requisite particularity as being materially false or misleading at the time they were made, Plaintiffs have alleged facts giving rise to a strong inference that these Defendants made these statements and/or omitted material information with scienter. *See infra*, III.D.[53]

C. The Complaint Adequately Alleges That Defendants' Failure To Disclose The Events Post-Dating The Vote Violated Section 10(b)

Within days of the shareholder vote on December 5, 2008, numerous highly material developments occurred that fundamentally altered the nature and terms of the merger. Specifically:

- Merrill's losses were so massive that, no later than December 14, the BoA Defendants definitively concluded that a materially adverse change had occurred in Merrill's condition;

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[52] *See also Atlas v. Accredited Home Lenders Holding Co.*, 556 F. Supp. 2d 1142, 1158 n.6 (S.D. Cal. 2008) (for purposes of determining whether materially false statements or misleading omissions exist, "[p]laintiff's Section 14(a) claim is effectively indistinguishable from the Section 10(b) claim").

[53] No Defendant has challenged Plaintiffs' allegations regarding economic loss and loss causation, thereby conceding these elements have been adequately pled.

- BoA's management, including Lewis, decided to terminate the merger because Merrill's losses were so large that BoA could not complete the transaction without substantial government assistance;

- The BoA Defendants agreed to consummate the merger only after Secretary Paulson told Lewis that he and the rest of the BoA Board would be fired if they backed out of the deal; and

- In order to complete the merger and prevent BoA's collapse, BoA negotiated and secured a $138 billion taxpayer.

None of these events were disclosed to investors prior to the close of the merger, and the failure to do so violated Section 10(b).[54]

1. The Defendants Violated Their Duty To Update And Correct Their Prior Statements Including Their Representation That No MAC Had Occurred As Of January 1, 2009

As set forth above in Section II.D.3, Defendants had a continuing duty to update their statements when intervening events rendered those statements misleading. The Proxy and Merger Agreement warranted that no materially adverse change had occurred in Merrill's financial condition "as of the Effective Time [*i.e.*, January 1, 2009]." Goldin Dec., Ex. 1 at 98, 163, 190. This was a materially false statement because, before that date, BoA had determined that a MAC had in fact occurred in Merrill's financial condition. Indeed, Plaintiffs have alleged that the BoA Defendants determined that a MAC existed almost immediately after the shareholder vote, if not before. ¶115. The BoA Defendants were so firm in their conviction that they went so far as to inform Secretary Paulson that they were going to invoke the MAC – and then only proceeded with the merger because Secretary Paulson threatened to fire them, and offered them a $138 billion taxpayer bailout. ¶¶114-15, 124-27, 135. In sum, having

[54] When testifying before Congress, Lewis admitted the materiality of these post-vote developments, describing Merrill's losses, BoA's determination to invoke the MAC and the $138 billion bailout as matters of "enormous magnitude and consequence to the company and the shareholders." ¶243.

represented that Merrill had not suffered a MAC through January 1, 2009, Defendants were required to disclose to investors when that representation was no longer true.[55]

In the same vein, the BoA Defendants had a continuing a duty to update the numerous statements they made during the Class Period touting the improved risk profile of Merrill and the stability and strength of BoA and Merrill. In addition to the false and misleading statements and omissions set forth above in Section II, directly after the December 5 shareholder vote, the BoA Defendants issued a press release stating, "When this transaction closes, Bank of America will have the premier financial services franchise." ¶226.[56] These "representation[s] remain[ed] 'alive' in the minds of investors as [] continuing representations," *IBM*, 163 F.3d at 110, because they were explicitly offered as solicitations or justifications of the merger. Shareholders and investors therefore reasonably believed that they would remain accurate at least through the merger's consummation, triggering Defendants' duty to disclose the facts that rendered them misleading.

This Court's decision in *City of Sterling Heights Police & Fire Retirement System v. Abbey National PLC*, 423 F. Supp. 2d 348, 348 (S.D.N.Y. 2006) (Chin, J.), is directly on point. There, the defendant began insisting in late 2001 that it had appropriately provisioned for losses and that there was no "huge cause for concern" regarding its investments in Enron, WorldCom and Tyco. *Id.* at 361. In early 2002, the company learned that its investments in these companies were in severe jeopardy, but "failed to disclose the substantial risk it faced." *Id.* at 353, 354. Based on these facts, this Court held that defendants' prior representations were

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[55] At a minimum, these statements were "continuing" and "remained alive" in investors' minds until at least January 1, when the merger was to be consummated. *IBM*, 163 F.3d at 110. As a result, Defendants were required to update these statements under Section 10(b) when intervening events rendered them materially false and misleading. *Id.*

[56] Defendants have not even challenged Plaintiffs' allegations with respect to the December 5th press release in their briefing as setting forth a claim under Section 10(b).

"particularly misleading" because they failed to disclose the new information especially where, as here, the defendants continued to issue reassuring statements. *Id.* at 360-61.

This case presents facts that are even more compelling than those at issue in *Sterling Heights*. By the time the BoA Defendants began debating whether to invoke the MAC, they ***knew*** that Merrill had not dramatically reduced its risk profile that BoA had suffered $800 million in losses and was projecting its own loss of $1.4 billion, that the merger would not result in a combined entity with a "strong capital position, funding capabilities and liquidity," and that BoA's "very thin" capitalization was the precise opposite of the picture that they had painted for shareholders and investors. The BoA Defendants thus were required to disclose the truth. ¶103. *See In re Bayer AG Sec. Litig.*, No. 03 Civ. 1546 WHP, 2004 WL 2190357, at *12 (S.D.N.Y. Sept. 30, 2004) (because, by a certain date, "defendants believed the brand was at risk," they had a "duty to update" prior statements that their product "would 'produce a sustained increase in [Bayer's] operating margin' and provide 'strong potential for future growth.'"). At least by the time they determined a MAC had occurred, if not earlier, the BoA Defendants "crossed the Rubicon" and had a duty to correct the misleading impressions left by their earlier representations. *Bayer*, 2004 WL 2190357, at *10.[57]

2. The BoA Defendants' Duty To Disclose "Sharp Break" From Prior Positions

Weeks before the merger closed, Lewis told the BoA Board that the merger might be terminated, and days later, told Secretary Paulson that the Bank intended to cancel the deal because it lacked the capital to absorb Merrill's losses (a position he altered only after he and the Board were threatened with termination). ¶¶114-15, 126. This 180-degree turnaround from the

[57] Moreover, contrary to the BoA Defendants' claim that the Complaint fails to allege "when the Bank's own fourth quarter results became available," BoA Mem. 48-49, Plaintiffs have alleged that as of December 19, even BoA executives had acknowledged BoA's own losses. ¶103. These facts are more than sufficient to demonstrate that the BoA Defendants' statements, even if true earlier, had become misleading, triggering the duty to update.

BoA Defendants' statements touting the merger and expressing "a strong interest in consummating a merger" as recently as December 5th, ¶226, represented exactly the sort of "change of heart," that triggers a duty to disclose. *Time Warner*, 9 F.3d at 267 (*citing Gulf Oil/Cities*, 725 F. Supp. at 745-49).

Moreover, the BoA Defendants were required to disclose their determination that BoA could complete the merger only if the terms were fundamentally changed, namely, if the merger were supported by a $138 billion taxpayer bailout. ¶¶145-46. This "change of heart" caused BoA to enter into a transaction that was fundamentally different than the one that had been described in the Proxy and promoted to investors. *See Time Warner*, 9 F.3d at 268 (disclosure required when a corporation pursues a different "approach[] to reaching the goal" previously announced to shareholders).

In response, the BoA Defendants claim that because they did not actually terminate the merger, SEC regulations and Form 8-K did not require them to disclose either their determination that a MAC had occurred or the taxpayer bailout. BoA Mem. 51. The BoA Defendants apparently believe that Secretary Paulson's threat to fire them obviates the need to comply with their disclosure requirements. But SEC regulations only state that "[n]o disclosure is required ***solely*** by reason" of Form 8-K when discussions are in a preliminary phase. Form 8-K, at Instruction 1 to Item 1.02(a) (emphasis added). Here, the BoA Defendants had a duty to disclose because they had specifically represented that they would indeed complete the merger on the terms set forth in the Proxy, and that a MAC had not occurred. *Time Warner*, 9 F.3d at 268. The duty to disclose thus arose under Rule 10b-5(b)'s prohibition on "omit[ting] to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading." 17 C.F.R. § 240.10b-5(b).

Additionally, contrary to what they contend, the BoA Defendants did have a regulatory duty under Form 8-K to immediately disclose their arrangement with the Government to receive the $138 billion taxpayer bailout. Form 8-K requires that "material definitive agreements" be disclosed within four business days. *See* Form 8-K, at Instruction B; Form 8-K at Item 1.01(a). Plaintiffs allege that by December 22, the taxpayer bailout was firmly in place. ¶132. In a meeting with the BoA Board on that date, Lewis repeatedly assured the Board members that he had the "commitment" of federal regulators, including the incoming regulators of the Obama Administration, to provide the bailout funds by January 20. ¶¶132-133. Lewis also told the Board that the only reason he would not obtain the commitment in writing was that he sought to do an end-run around the securities laws, ¶¶134, 136, explaining that "there was no way the Federal Reserve and the Treasury could send us a letter of any substance without public disclosure ***which, of course, we do not want***." ¶134.[58] These allegations make it crystal clear that the taxpayer bailout was in place prior to the consummation of the merger, and that BoA Defendants violated Rule 10b-5(b) by failing to disclose that fact in accordance with the requirements of Form 8-K.

In the face of these detailed allegations, the BoA Defendants argue that Form 8-K did not require announcing the taxpayer bailout earlier because Plaintiffs have only alleged the existence of "informal assurances" by a government agency and not a definitive agreement. BoA Mem. 54. This argument is particularly disingenuous given that Defendants ***intentionally avoided committing the terms of the deal to a formal contract solely to avoid public disclosure***. ¶¶134, 136. But the securities laws are not so easily evaded. The allegations in the Complaint detail

[58] At a second Board meeting on December 30, Lewis reiterated that BoA had told federal regulators that completion of the merger was "condition[ed]" on the receipt of the taxpayer bailout, that he had "detailed oral assurances from the federal regulators with regard to their commitment," and that he had "documented those assurances with e-mails and detailed notes of management's conversations with the federal regulators." ¶¶134-35.

with extraordinary clarity that federal regulators from two different administrations had "committed" to a deal, and that Defendants "conditioned" their completion of the merger on that commitment. ¶¶132-35. Moreover, the BoA Defendants admitted that they could not have completed the merger on January 1 had they not received government assistance, demonstrating that they knew that the deal was sufficiently definite to undertake a major corporate transaction – ***one that would have jeopardized BoA's solvency without the bailout*** – in reliance on its terms. ¶147. The BoA Defendants' intentional attempt to avoid their disclosure obligations by exploiting what they perceived to be a technicality in the rules should not be countenanced.[59]

3. The Misleading January 1st Press Release

Finally, Defendants' January 1 press release announcing the completion of the merger was also materially false and misleading. Rather than disclose the fact that BoA "conditioned" completion of the merger on receipt of substantial government assistance and utterly failing to mention the $21 billion in pre-tax losses Merrill had suffered in the fourth quarter, the release announced that the merger "creat[ed] a premier financial services franchise," ¶139, going so far as to hail an expected "$7 billion in pre-tax expense savings," *id.* These statements were materially false and misleading because by then, it was obvious to the BoA Defendants, Merrill and Thain that Merrill's dire financial situation would not be alleviated by "$7 billion in pre-tax expense savings," and because these Defendants were fully aware that the "purchase" of Merrill mentioned in the press release was fundamentally different than the transaction described in the Joint Proxy given the taxpayer bailout. ¶¶145-47. Investors, with no way of knowing these

[59] Nor can Defendants find support for their position in their cited summary judgment and post bench trial opinions. *1st Home Liquidating Trust v. United States*, 581 F.3d 1350 (Fed. Cir. 2009) (*cited at* BoA Br. 54 n.41) is an opinion on summary judgment and, in any event, the Complaint adequately alleges the elements of mutuality of intent, consideration, and lack of ambiguity. *Teachers Ins. & Annuity Ass'n of Am. v. Tribune Co.*, 670 F. Supp. 491 (S.D.N.Y. 1987) (*cited at* BoA Mem. 54 n.41) was decided after a bench trial and, further, the court held that the critical question is whether the parties exhibited an intent to be bound. *See id.* at 499-500. At a minimum, the existence of a contract under these circumstances cannot be determined as a matter of law at this stage of the proceedings.

facts, took the press release as an affirmation that the purchase had been completed as described in the Joint Proxy, and were therefore misled.

By touting the benefits of the merger in terms nearly identical to those issued months earlier, *e.g.*, ¶¶112, 192, Defendants implied that no material changes in the deal or their outlook had occurred, when in fact the opposite was true. For that reason, the press release misled investors and furthered Defendants' fraud. *See Caiola*, 295 F.3d at 331 (upon choosing to speak, defendant must "be both accurate and complete"); *Sterling Heights*, 423 F. Supp. 2d at 360.

D. The Complaint's Allegations Give Rise To A Strong Inference Of Scienter

1. Legal Standards For Pleading Scienter

A complaint alleging securities fraud must give rise to a "strong inference" of scienter. *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 314 (2007). To determine whether a strong inference of scienter exists, a court must "accept all factual allegations in the complaint as true" and determine "whether *all* of the facts alleged, taken collectively, give rise to a strong inference of scienter, not whether any individual allegation, scrutinized in isolation, meets that standard." *Id.* at 322-23 (emphasis in original).

The inference of "scienter need not be irrefutable, *i.e.*, of the smoking-gun genre, or even the most plausible of competing inferences." *Id.* at 324 (internal quotation makes omitted). Instead, an inference of scienter is "strong" when it is ***at least as likely as*** any other inference. *Id.*; *Akerman v. Arotech Corp.* 608 F. Supp. 2d 372, 382 (E.D.N.Y. 2009) ("When the competing inferences rest in equipoise, the tie goes to the plaintiff'") (internal quotations omitted). Thus, under *Tellabs*, it is Defendants' burden to show that the Complaint's allegations give rise to an inference of innocent behavior that is ***stronger*** than the inference of recklessness.

A complaint establishes a strong inference of scienter by pleading facts that ***either*** constitute strong circumstantial evidence of conscious misbehavior or recklessness, ***or*** show that

defendants had both motive and opportunity to commit fraud. *Sterling Heights*, 423 F. Supp. 2d at 356 (S.D.N.Y. 2006) (*citing Rothman v. Gregor*, 220 F.3d 81, 90 (2d Cir. 2000)). A strong inference of recklessness is adequately pled where the complaint alleges that defendants knew or had access to non-public information suggesting that their public statements were not accurate. *See, e.g., Scholastic*, 252 F.3d at 76; *Sterling Heights*, 423 F. Supp. 2d at 356.

2. Defendants' Scienter With Respect To The Secret Bonus Agreement

There are overwhelming facts that give rise to a strong inference that Defendants Lewis, Price, Cotty and Thain acted with scienter in failing to disclose the bonus agreement. Indeed, Lewis and Thain ***negotiated*** the agreement, and Thain has acknowledged that the timing and amount of the massive bonuses were one of the three "main things" negotiated in connection with the merger (the other two being the price and the MAC clause). ¶¶67-69, 71. Such facts establishing their knowledge of the undisclosed bonus agreement are easily sufficient to establish their scienter. *See, e.g., Scholastic*, 252 F.3d at 72-73, 76-77; *Sterling Heights*, 423 F. Supp. 2d at 362.

Further, despite their knowledge of this bonus agreement, the BoA Defendants, Merrill and Thain represented in the Proxy and Merger Agreement that Merrill could not pay discretionary bonuses prior to the close of the merger without BoA's prior written consent. ¶¶196, 215-216. Courts uniformly hold that where defendants are aware of facts or have access to information that directly contradicts their public statements, a strong inference of scienter can be inferred. *See, e.g., In re Atlas Air Worldwide Holdings, Inc. Sec. Litig.*, 324 F. Supp. 2d 474, 489 (S.D.N.Y. 2004) (scienter adequately pled where available facts contradict a high-level officers' public statements); *NTL*, 347 F. Supp. 2d at 28 (allegations of defendant's knowledge of

facts or access to contradictory information are sufficient to state a claim based on recklessness).[60]

In response, Defendants raise a series of arguments which can be swiftly rejected. Defendants contend that Plaintiffs fail to allege scienter because the bonus agreement was effectively disclosed (*see* BoA Mem. 29) and that, in any event, Defendants followed "customary disclosure practice" in not providing a copy of the bonus schedule to investors (*see* BoA Mem. 29, n.19). These arguments are identical to those raised by the 14(a) Defendants with respect to the bonus agreement and should be rejected for the same reasons set forth in Section II.B.3, *supra.* Second, Defendants' argument that Plaintiffs have supposedly engaged in "impermissible 'group' pleading," and that "the only individual allegations [establishing scienter as to the bonus agreement] are directed against" Defendants Lewis and Thain is nonsense. Defendants' recharacterization entirely ignores the detailed allegations demonstrating that Price (BoA's CFO) and Cotty (BoA's Chief Accounting Officer and, during the Class Period, Merrill's acting CFO) were intimately involved in the merger negotiations and signed the Joint Proxy Registration Statement containing the Merger Agreement and Joint Proxy. ¶¶36-37, 178-179. Given their extensive involvement in the merger, the notion that these two senior officers were somehow unaware of the bonus agreement is neither plausible nor credible. *See, e.g.*, *Scholastic*, 252 F.3d at 72-73, 76-77; *Atlas*, 324 F. Supp. 2d at 491 ("The individual defendants were not entitled to

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[60] The Delaware Chancery Court has concluded that virtually identical allegations pled scienter, rejecting Defendants' argument that the complaint in the Delaware Derivative Action failed to "show that Defendants withheld [disclosure of the bonus agreement] in bad faith," and holding that the size of the bonus agreement, and the fact that the merger agreement was known to BoA's executives and Board at the time they agreed to the Merger but was not disclosed, supported the ruling. *See* Hr'g Tr. at 29:21-34:14, *Del. Derivative Action* Tr., Nirmul Decl. Ex. C. Significantly, just like a finding of scienter, a finding of "bad faith" under Delaware law is made "where the fiduciary ***intentionally*** acts with a purpose other than that of advancing the best interests of the corporation" or "demonstrate[es] a ***conscious*** disregard for his duties." *In re The Walt Disney Co. Derivative Litig*., 907 A.2d 693, 755 (Del. Ch. 2005), *aff'd*, 906 A.2d 27 (Del. Supr. 2006).

make statements . . . and ignore reasonably available data that would have indicated that those statements were materially false or misleading.").

3. Defendants' Scienter With Respect to Merrill's Financial Condition

Similarly, there is no question that the Complaint alleges that the BoA Defendants, Merrill and Thain each possessed detailed facts regarding Merrill's financial condition throughout the Class Period. Immediately after announcing the merger, BoA installed 200 employees at Merrill to monitor Merrill's financial condition, including a substantial financial team. ¶93. Additionally, BoA appointed Cotty as Merrill's interim CFO so that Cotty could provide BoA's senior officers, including Lewis and Price, with reports on Merrill's financial condition. ¶¶93, 97. As Merrill's acting CFO, Cotty attended weekly meetings with Thain to discuss Merrill's losses. ¶94. Likewise, Thain stated that Merrill was "completely transparent" about its losses with BoA's senior officers, providing them with "daily" profit and loss statements and access to Merrill's trading positions and accounting marks, such that BoA's senior officers knew of Merrill's losses "***step by step***" throughout the fourth quarter. ¶¶93, 95.

Lewis himself was forced to admit in sworn testimony to Congress and the NYAG that he received "***detailed financial reports***" regarding Merrill "every week" and that Merrill's losses were "***clear***" before the shareholder vote. ¶¶97-98. Lewis also led weekly conference calls with the BoA Board and Defendant Price during which they discussed Merrill's losses. ¶99. Given these facts, BoA itself has acknowledged that "***we were kept informed about the financial condition of [Merrill]***." ¶96. These facts alone establish scienter for the BoA Defendants, Merrill and Thain. *See, e.g.*, *In re Globalstar Sec. Litig.*, No. 01 Civ. 1748 (SHS), 2003 WL 22953163, at *7 (S.D.N.Y. Dec. 15, 2003) (scienter adequately pled where defendants "were updated on a weekly basis" as to adverse information).

The BoA Defendants' scienter is further established by the fact that, as a direct result of Merrill's losses, they repeatedly debated invoking the MAC ***before*** the shareholder vote (¶¶100-102), yet consciously decided not to disclose this information even though it was admittedly "of ***enormous magnitude and consequence to the company and the shareholders***." ¶243.[61] *See, e.g.*, *Lormand*, 565 F.3d at 252-54 (scienter adequately pled where defendants "privately admitted" and internally "protested" adverse, undisclosed facts that contradicted their public statements).[62]

In addition, the fact that Lewis attempted to cover-up his knowledge of and responsibility for the material misrepresentations and non-disclosure after the vote is strong evidence of his scienter. In this regard, Lewis requested a letter from Chairman Bernanke stating that the Government "ordered him to proceed" with the merger to "use as a defense" to shareholder actions – a fact that is extraordinary evidence of his scienter. ¶¶129-31. It should be noted that Chairman Bernanke did not honor Lewis's request to immunize himself — and this Court should not either.

Likewise, Lewis told both the Federal Reserve and Congress that Merrill's losses supposedly surprised him because they suddenly materialized ***after*** the shareholder vote. ¶245. Upon reviewing Merrill's loss data, however, senior Federal Reserve officials concluded that Lewis's claim that the losses only dramatically increased after the vote was "***not credible***"; an

[61] Vice Chancellor Strine has already rejected Defendants' argument that Lewis was uninvolved in the decision not to disclose Merrill's losses before the vote (*see* BoA Mem. 46, n.36) finding it an absurd argument that Lewis was not involved in the decision making but that rather this was delegated to "a bunch of underlings … walking around with high-priced outside counsel talking about MACs," as Defendants suggested, given the size of the transaction and the involvement of senior banking regulators. Hr'g Tr. at 11:5-6, *Del. Derivative Action*, Nirmul Decl., Ex. C.

[62] Merrill and Thain contend that they did not know that Merrill's losses were material to BoA shareholders because they were unaware that BoA's senior executives were discussing invoking the MAC, and they did not know that BoA was unable to absorb Merrill's losses. Merrill Mem. 10; Thain Mem. 7. However, it strains reason to think that Merrill had "no clue" that its $15 billion of accelerating, pre-vote losses – which were large enough to ***bankrupt*** Merrill – would also materially impact BoA.

independent expert commissioned by Congress concluded that any acceleration in Merrill's losses was clear by "November 14," ¶246; and the NYAG investigation also established that Merrill's $2 billion goodwill impairment "was known of by November," but was lumped in with the "purportedly 'surprising' losses" arising after the shareholder vote (¶233). According to Thain, Lewis's version of the acceleration in losses was the opposite of "what actually happened" given the $7 billion in losses Merrill recognized in October alone (¶245).[63]

Additionally, in a sworn deposition before the NYAG, Lewis testified that Secretary Paulson "instructed" him not to disclose Merrill's losses or the bailout. ¶249. When testifying before Congress just two months later, Lewis revised his story, claiming that he "never heard from [Secretary Paulson] on the issue of us not disclosing something" – which caused Congress to caution Lewis that he was "under oath."[64] *Id.* Lewis's repeated false explanations and inconsistent statements are further evidence of his scienter. *See Novak*, 216 F.3d at 311-12; *SEC v. Lucent Techs., Inc.,* 363 F. Supp. 2d 708, 717 (D.N.J. 2005); *Rocker Management, L.L.C. v. Lernout & Hauspie Speech Prods.*, No. Civ. A 00-5965 (JCL), 2005 WL 136465, at *13 (D.N.J. June 7, 2005).

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[63] Merrill attempts to negate its scienter by asserting that the Complaint does not allege that its executives ever discussed the timing of its $2 billion goodwill impairment with Federal regulators. *See* Merrill Mem. 11, n.13. This is irrelevant: as noted above, Merrill obviously knew that it had suffered this impairment as of November, which alone establishes its scienter.

[64] These allegations belie Defendants' argument set forth in footnote 36 of the BoA Defendants' brief; as demonstrated above, Lewis has reversed or contradicted his own testimony on numerous occasions. Defendants also argue that the evidence contradicting Lewis's statements about Merrill's losses comes from "others who may have differing recollections or motives, or whose understanding of the underlying events is at best second-hand." *Id.* At best, the "motives" and "recollections" of the country's most senior banking regulators, Congress, the New York Attorney General, or Thain, are questions for discovery. Finally, Defendants' reliance on *In re BearingPoint, Inc. Sec. Litig.*, 525 F. Supp. 2d 759, 777 (E.D. Va. 2007), for the proposition that the existence of a Government investigation does not establish a strong inference of scienter, is flawed. In that case, unlike here, the Government investigations "***ha[d] nothing to do with the alleged fraud***," and the complaint merely "refer[red] to an alleged DOJ investigation," without describing any facts emerging from it or quoting internal company documents or defendants' own sworn admissions. *Id.*

In response to these compelling facts, the BoA Defendants, Merrill and Thain offer a series of meritless arguments. First, Defendants argue that the Complaint fails to plead with particularity "which Defendants were apprised of Merrill's losses" before the vote and "precisely what they knew." This argument simply ignores the Complaint's allegations and should be rejected. *See, e.g.,* ¶¶88-101; Hr'g Tr. at 115:9-22, *Del. Derivative Action* (rejecting the same argument because Defendants simply ignored the "very specific allegations about what was known before the stockholder vote" by "Defendant Lewis, the entire board, and the transition team"), Nirmul Decl. Ex. C.[65]

Second, Defendants contend that Plaintiffs have "mischaracterized" the reference to Merrill's losses in the NYAG's September 8, 2009 letter because these were "forecasted" losses, rather than incurred losses. *See* BoA Mem. 44, n.34. However, regardless of whether Merrill's losses were projected, the letter establishes that these Defendants knew that Merrill's losses were "so great" that they repeatedly discussed invoking the MAC on November 20, December 1 and December 3, 2008. ¶101. Moreover, contrary to what Defendants contend, by the date of the vote, Defendants knew Merrill's results for October and November, and numerous facts establish that Merrill had ***actually suffered*** more than $15 billion of losses before the vote. *See* ¶¶88-90.

Third, Defendants argue that the Complaint fails to "support an inference that any of the Defendants ***knew or believed*** that disclosure of Merrill's losses was required." BoA Mem. 46. For the reasons set forth above in Section III.B, this argument defies belief – the losses were large enough to threaten BoA's financial stability, and caused the most senior officers at BoA to decide to invoke the MAC and ultimately obtain a $138 billion taxpayer bailout to close the

[65] For these reasons, Defendants' citation to *CALPERS v. Chubb Corp.* 394 F.3d 126 (3d Cir. 2004), is inapposite. *See* BoA Mem. 44-45. In *Chubb*, plaintiffs had failed to allege that their low-level confidential sources were in a position to possess information about the defendants' knowledge. *Id.* at 152. Here, the Complaint relies on Defendants' own admissions and well-documented facts to demonstrate their knowledge.

transaction but they were not material enough to disclose to BoA investors.[66] *See Lormand*, 565 F.3d at 253-54. Moreover, ignorance of the law is no defense to liability under Rule 10b-5. *See, e.g.*, *O'Hagan*, 139 F.3d at 647 (1998). Indeed, if this were not the case, then any defendant could escape liability simply by claiming that he did not believe that he was required to disclose obviously material facts.[67]

Fourth, the BoA Defendants argue that there can be no inference of scienter against them because they "conferred with legal counsel as to whether disclosure of Merrill's [losses] was required." BoA Mem. 46. This argument also fails. A blanket assertion of reliance on counsel is a highly fact-intensive affirmative defense which cannot negate scienter at the pleading stage. *Siemers v. Wells Fargo & Co.*, 2006 WL 2355411, at *9 (N.D. Cal. 2006) ("If defendants wish to rely on advice of counsel defense, that would be a matter for an affirmative defense" subject to discovery); *SEC v. Martino*, 255 F. Supp. 2d 268, 285 (S.D.N.Y. 2003) (listing facts that must be established for defense to be invoked).[68]

Finally, the BoA Defendants contend that the inference of their scienter is negated by their purported warning prior to the public that "turbulent market conditions" "may" have an "anticipated" effect on Merrill's financial results. BoA Mem. 47. As set forth in Section II.D,

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[66] Moreover, contrary to Defendants' argument that scienter requires a showing of subjective "belief," it is black-letter law that Rule 10(b)(5) does not require "deliberate illegal behavior." *See, e.g.*, *Novak*, 216 F.3d at 308 (scienter requires only "recklessness").

[67] Merrill's reliance on *Kalnit* is misplaced. Merrill Mem. 8. In *Kalnit*, the plaintiffs failed to allege scienter where the duty to disclose a waiver of a three-year old standstill agreement was not "clear" in light of that information's immateriality. *See Kalnit v. Eichler*, 264 F.3d 131, 144 (2d Cir. 2001). Here, as set forth above, Defendants' duty to disclose Merrill's highly material losses was clear. Moreover, because Plaintiffs allege that Merrill made affirmative misstatements rather than omissions, *Kalnit* does not apply.

[68] Moreover, Judge Rakoff has already rejected this argument in the SEC Action. In that case, BoA asserted that none of its individual officers were responsible for the Proxy's misstatements or omissions because the Proxy's disclosures were "all negotiated and worked on by lawyers." Hr'g. Tr. at 24:13-25:13, *SEC v. Bank of America Corp.*, 09-CV-06829 (JSR) (S.D.N.Y Aug. 10, 2009), Nirmul Decl., Ex. B. Judge Rakoff commented that Defendants' argument was "at war with common sense." *S.E.C. v. Bank of America Corp.*, No. 09 Civ. 6829(JSR), 2009 WL 2842940, at *2 (S.D.N.Y. Aug. 25, 2009).

above, this is the proverbial Grand Canyon lurking around the corner, when Defendants warned about the "turbulent market conditions" and "anticipated" effects while withholding the concrete, highly material facts that Merrill had already suffered $7 billion in losses in October alone and more than $15 billion in losses before the vote. *See, e.g., Prudential*, 930 F. Supp. at 72.

4. Defendants' Scienter Regarding BoA's Inadequate Due Diligence, Merrill's True Risk Profile, And The Pressure By Federal Regulators

On September 15, 2008, Defendants BoA, Lewis, Price, and Thain issued a series of statements assuring investors that BoA had conducted "comprehensive" due diligence (¶¶179-81); Merrill's risk profile was "dramatically" improved (*id.*); there had been no pressure from Federal regulators to agree to the merger (¶187); and the merger would create "the leading financial institution in the world" (¶192). These Defendants either knew contradictory facts at the time they made these statements, or knew that subsequent material events rendered these statements misleading, and failed to update these statements. *See Scholastic*, 252 F.3d at 76; *Sterling Heights*, 423 F. Supp. 2d at 356.

Regarding Lewis's and Price's statements about BoA's due diligence, and Merrill's risk profile and liquidity, Lewis ***admitted*** to senior Federal Reserve officials in December 2008 that he "***knows they [BoA] did not do a good job of due diligence***" and thus was "worried about stockholder lawsuits" and "his own job." ¶122. This admission alone establishes his scienter for these statements. *See Cendant*, 60 F. Supp. 2d at 371 (defendants' admission that due diligence of acquired company was inadequate established inference of scienter). Moreover, Plaintiffs allege that Lewis and Price knew of or recklessly disregarded Merrill's true risk profile. Indeed, after reviewing BoA's due diligence, senior Federal Reserve officials concluded that Merrill's

risk exposures "were clearly shown" in the reports that BoA received. ¶182;[69] *see Freedman*, 958 F. Supp. at 757 (scienter alleged where defendant later admitted that due diligence it publicly described as "full" had "shortcomings" and deficiencies in due diligence were "sufficiently profound").[70]

Defendants Lewis and Thain also knew facts which contradicted Lewis's statement that Federal regulators exerted "absolutely no pressure" to finalize the merger. As *PBS Frontline* reported, Secretary Paulson had "adamant[ly]" demanded that the senior executives of BoA and Merrill finalize the merger within 36 hours. ¶65. Further, Thain has ***admitted*** that Secretary Paulson personally ordered him to "make sure this happens" in "very strong" terms. *Id.* Thain's inaction (standing by silently at the joint press conference without offering any correction) in the face of this knowledge establishes his recklessness with regard to this misstatement. *See Barrie v. Intervoice-Brite, Inc.*, 397 F.3d 249, 262 (5th Cir. 2005) ("[A] high ranking company official cannot sit quietly at a conference with analysts, knowing that another official is making false statements and hope to escape liability for those statements. If nothing else, the former official is at fault for a material omission in failing to correct such statements in that context."). Moreover, contrary to Lewis's argument, it defies reason to think either that Lewis was unaware of

[69] Thus, Lewis's argument (BoA Mem. 66) that his scienter for these statements rests solely on Thain's admission that Lehman's bankruptcy filing would have caused Merrill to become effectively insolvent "beginning Monday morning," September 15, is factually and legally inaccurate.

[70] In response, Defendants BoA, Lewis, Price, and Cotty attempt to assert what they characterize as a non-culpable competing inference: if they "believed" as of September 15 that their due diligence had been inadequate or the Merger would not be beneficial, they would have never agreed with the merger. BoA Mem. 69. First and foremost, this ignores allegations of the Complaint that Lewis admitted he was "drooling" at the idea of acquiring Merrill (¶59) and that he wanted to "win" against Wall Street (¶¶15, 229). Thus, the more plausible inference from the allegations of the Complaint is that Defendants' statements about BoA's due diligence and the benefits of the merger were deliberately reckless, precisely because BoA failed to conduct adequate due diligence as they were pressing forward with this merger irrespective of their ability to properly conduct due diligence. Second, Defendants' subjective belief in their statements at the time is not relevant in situations in which Plaintiffs assert that they were reckless. Finally, all that is required to establish a strong inference of scienter is that Defendants "knew facts or had access to information suggesting that their public statements were not accurate," which is amply alleged. *Novak*, 216 F.3d at 311; *Sterling Heights*, 423 F. Supp. 2d at 356 (same).

Paulson's order, or that Paulson did not exert pressure on Lewis as well given the fact that BoA finalized the most significant transaction in its history over the course of a single weekend – just as Secretary Paulson desired.

5. The BoA Defendants' Scienter Regarding BoA's Losses

Defendants Lewis, Price, and Cotty also knew, in stark contrast to their statements in the Joint Proxy and November 26 Proxy Supplement, that BoA possessed a "strong capital position," that in reality, BoA's capitalization and financial condition was extremely weak at that point in time. In fact, Lewis ***admitted*** in sworn testimony that he and BoA's senior executives personally received daily profit and loss statements for BoA (¶98), and that BoA's own unprecedented losses were "clear" before the shareholder vote (¶97). *See,* e.g., *Scholastic*, 252 F.3d at 72-73, 76-77 (scienter alleged by specifying internal reports containing undisclosed information). According to the Federal Reserve Merger Analysis – which was based on a review of BoA's internal loss data that Lewis, Price and Cotty admittedly received – by the time of the shareholder vote, BoA had suffered $800 million in losses and was projecting a fourth quarter loss of $1.4 billion – the first quarterly loss in its history. ¶103. Moreover, BoA's officers ***admitted*** during a meeting with federal regulators, that, "even on a stand-alone basis, the firm is very thinly capitalized." ¶235.[71]

The BoA Defendants also argue that their purported generic disclosure of "turbulent market conditions" days before the shareholder vote negates the inference of recklessness. BoA Mem. 47. However, as set forth above in Section II.D, courts universally hold that such vague

[71] Federal regulators, reviewing BoA's financial condition, also concluded that BoA's fourth quarter earnings guidance to the market contradicted the information that BoA had told them and wrote in an internal memo: "The earnings guidance provided by the firm to the investor community does not infer that 4Q performance at either organization will be as negative as we have been told. Further, a survey of equity analysts suggests that the investor community have significantly more positive expectations regarding fourth quarter performance." ¶140. This also supports scienter as the BoA Defendants were clearly managing earnings information in this respect.

statements do not insulate a defendant from liability for failing to disclose or misrepresenting known, material facts. *See Prudential*, 930 F. Supp. at 72.

6. Motive And Opportunity Strengthens The Inference of Scienter

Although the Complaint need not plead any motive to establish scienter (*see Ganino*, 228 F.3d at 170), the Complaint contains compelling allegations regarding the BoA Defendants' motive to conceal the facts described above. First, Secretary Paulson personally threatened to fire Defendants Lewis, Price, Cotty and the entire BoA Board if they attempted to terminate the merger. ¶126. As set forth in the Complaint, Lewis admitted in sworn testimony to the ***NYAG that*** "***Secretary Paulson's threat changed his mind*** about invoking the MAC clause and terminating the deal." ¶127. *See, e.g.*, *Aldridge v. A.T. Cross Corp.*, 284 F.3d 72, 84 (1st Cir. 2002) (motive adequately pled where defendants' "jobs were in jeopardy if the goals were not met"). Despite Defendants' protests, it is hard to imagine a more "concrete and personal" benefit than avoiding a very public and humiliating termination at the hands of government regulators. *See, e.g.* Hr'g Tr. at 123:1-5, *Del. Derivative Action* (it is "impossible to ignore" this concrete motive), Nirmul Decl. Ex. C.

Second, Lewis, Price, and Cotty were motivated to conceal material facts from shareholders because – as Chairman Bernanke explicitly told Lewis and Price – if they revealed the truth about Merrill's financial condition and the merger's impact on BoA, it would: (i) call into question the statements they had made regarding the benefits of the merger and BoA's due diligence and company analysis; (ii) call into question their judgment and competence in agreeing to pay a large premium for Merrill; and (iii) "expose the weaknesses in [BoA's] capital and asset quality," causing the "market [to] conclude that [BoA] was too weak to address the problems at Merrill." ¶242; *see also* ¶125.

Third, these arguments ignore the allegation that Lewis coveted Merrill as the "final piece" of his plan to make BoA the largest bank in the country and deliver him significant prestige and respect for which he had "long clamored." ¶59. *See, e.g.*, *JPMorgan Chase & Co.,* 2007 WL 4531794, at *8 (desire to "reclaim the mantle of Wall Street superstar" and "increase [] prestige and reputation" constitute motive for fraud).

Fourth, with respect to Thain's motive, it is patently obvious that he needed this deal to go through no matter what the consequences because, as he has admitted, without the consummation of the merger, Merrill would have been bankrupt. ¶62. *See, e.g.*, *In re Cabletron Sys.*, 311 F.3d 11, 39 (1st Cir. 2002) (desire to save company constituted motive). In addition, at the time of the merger negotiations, Thain had secured a $40 million bonus for himself. ¶68.

That Defendants did not sell any of their personal holdings in BoA is of no moment. *See In re Netbank, Inc. Sec. Litig.*, No. 1:07-cv-2298-BBM, 2009 WL 2432359, at *12-13 (N.D. Ga. Jan. 29, 2009) (scienter adequately pled even though defendants held 100,000 shares and actually acquired additional stock during class period); *In re Nuko Inf. Sys., Inc. Sec. Litig.*, 199 F.R.D. 338, 344-45 (N.D. Cal. 2000). Even assuming that Defendants were permitted to sell their stock following the announcement of the merger, they could not have done so as a practical matter as any large stock sales would have raised serious questions in the minds of investors as to why, if the merger was going to be so successful, Defendants would be unloading material amounts of their shares in advance of the merger.

Defendants BoA, Lewis, Price, and Cotty attempt to counter Plaintiffs' strong inference of scienter by contending that if they had truly believed that Merrill's pre-vote losses "called into question the Bank's rationale for the merger," they could have simply disclosed the losses before the vote, BoA Mem. 47, or the BoA Board could have withdrawn its recommendation in favor of

the merger. BoA Mem. 53. However, neither of these hypothetical options would have eliminated their prior false and misleading statements regarding the proposed benefits of the merger and the adequacy of the due diligence that BoA had purportedly performed. Indeed, Chairman Bernanke said as much when he testified that he told Lewis that after "months of review, preparation and public remarks . . . about the benefits of the acquisition," disclosing these facts "would cast doubt in the minds of financial market participants . . . about [BoA's] due diligence and analysis, its capacity to consummate significant acquisitions, its overall risk management processes and the judgment of its management." ¶125.[72]

Defendants similarly ask what they could have hoped to gain from nondisclosure in December 2008, when they all knew that disclosure would have to occur in mid-January 2009. BoA Mem. 50. By this time, their omissions and false statements had already harmed BoA's shareholders as the vote had already taken place. As the Complaint amply alleges, Secretary Paulson had bluntly threatened to fire them if BoA did not consummate the Merrill merger, and Defendants certainly understood that disclosure of Merrill's massive losses or the need for the $138 billion taxpayer bailout would have threatened consummation of the merger and placed their jobs in peril.[73]

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[72] While Chairman Bernanke's comments were made in connection with a discussion about what would have happened if BoA had invoked a MAC, they apply with equal force to Defendants' pre-vote conduct. Indeed, the very fact that Defendants repeatedly debated invoking the MAC in the weeks leading up to the shareholder vote demonstrates creates a strong inference of scienter in allowing the vote to take place without disclosure of Merrill's losses or withdrawing the recommendation.

[73] In a footnote, Defendants argue that Secretary Paulson's threat could not have motivated them to withhold material facts because Secretary Paulson threatened to fire them if they "terminated the transaction," not if they disclosed any "particular facts." BoA Mem. 45, n.35. Of course, had Defendants terminated the transaction, presumably the market would have learned the reasons for that termination. Defendants also argue that, because Paulson's threat post-dated the shareholder vote, it could not have motivated them before the vote. *Id.* However, Plaintiffs have not alleged that the threat of the loss of their jobs motivated Defendants' concealment of the material information "pre-vote." Instead, Plaintiffs allege that Secretary Paulson's termination threat motivated Defendants to "close" the transaction, which is exactly what happened. ¶241.

Finally, Defendants argue that a "compelling non-fraudulent" explanation for their failure to disclose the taxpayer bailout before January 16, 2009 is their belief that disclosure of the bailout "before a binding agreement with the government was reached" would have harmed both companies and the economy as a whole. BoA Mem. 56. This argument ignores the fact that a binding agreement had been reached as early as December 22, and certainly no later than December 30; otherwise, Defendants could not have closed the merger in direct reliance on that agreement. Moreover, despite repeated protestations on the part of federal regulators that terminating the merger would harm both companies and the broader economy (*see* ¶¶116, 124-25), Lewis and Price flatly ignored these systemic concerns and continued to insist on terminating the transaction right up until December 21 – the day that Secretary Paulson threatened to fire them. ¶¶126-28. It was only then that Lewis and Price became enamored with saving the U.S. economy.[74]

IV. PLAINTIFFS HAVE ADEQUATELY ALLEGED CLAIMS UNDER SECTIONS 11, 12 AND 15 OF THE SECURITIES ACT

Counts VII, VIII and IX of the Complaint assert violations of the Securities Act in connection with the $9.9 billion offering of BoA common stock on or about October 7, 2008 (the "Offering").[75] *See generally* ¶¶362-395. Specifically, Plaintiffs allege that the registration statement and prospectus issued in connection with the Offering (the "Offering Documents") incorporated by reference certain materially false and misleading statements: (i) from the

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[74] In any event, altruism is no defense to a charge of intentionally misleading shareholders. *See, e.g., Basic, Inc. v. Levinson*, 485 U.S. 224, 235 (1988) (companies not permitted to mislead shareholders to "maximize" their wealth); *U.S. v. Simon*, 425 F.2d 796, 809 (2d Cir. 1969) (government burden in criminal securities fraud prosecution is not to show that defendants "were wicked men with designs on anyone's purse . . . but rather that they had certified a statement knowing it to be false.").

[75] The Complaint alleges violations of Section 11 of the Securities Act against the BoA Defendants and the BoA Board for signing or approving the materially false and misleading Registration Statement issued in connection with the Offering. Section 11 claims are also brought against BAS and MLPFS for their role as underwriters of the Offering. The Complaint also alleges violations of Section 12(a)(2) of the Securities Act against BoA and the Underwriter Defendants for false and misleading statements in the registration statement, and control person liability under Section 15 against Defendants Lewis, Price and the BoA Board.

September 18, 2008 Form 8-K which failed to disclose BoA's pre-existing agreement allowing Merrill to pay up to $5.8 billion in discretionary bonuses before the merger closed, and (ii) from the September 15, 2008 Form 8-K concerning the benefits and impact of the merger on BoA. ¶364.

Under Section 11, an issuer such as BoA faces strict liability for any material misrepresentation or omission in a registration statement. 15 U.S.C. §77k(b)(3)(A). Hence, "[i]f a plaintiff purchased a security issued pursuant to a registration statement, he need only show a material misstatement or omission to establish his *prima facie* case. Liability against the issuer of a security is virtually absolute, even for innocent misstatements." *Herman & MacLean v. Huddleston*, 459 U.S. 375, 382 (1983). Thus, a plaintiff need not allege or prove even negligence, let alone fraud, to prevail under Section 11 against BoA.[76]

Similarly, Section 12(a)(2) of the Securities Act imposes liability upon "[a]ny person who . . . offers or sells a security . . . by the use of any means or instruments . . . which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements . . . not misleading." 15 U.S.C. §77l(a)(2); *see also Milman,* 72 F. Supp. 2d at 228 (S.D.N.Y. 1999). Like Section 11, Section 12 does not require a plaintiff to plead scienter or reliance.[77]

Finally, to plead a claim under Section 15 of the Securities Act, a complaint must allege 1) a primary violation of the Securities Act, and 2) direct or indirect control of the violator by the defendant. *See Garber,* 537 F. Supp. 2d at, 618; *In re Adelphia Commc'ns Corp. Sec. and*

[76] Although the issuer is strictly liable under Section 11, directors and underwriters may attempt to prove an affirmative defense of due diligence. *In re Worldcom Sec. Litig.*, 346 F. Supp. 2d 628, 662 (S.D.N.Y. 2004). As explained below, however, the burden is on non-issuer defendants to prove their good faith or due diligence, which simply cannot be done at the pleading stage.

[77] Also similar to Section 11, Section 12 provides for an affirmative defense of "reasonable care" for non-issuers. 15 U.S.C. §77l(a)(2).

Derivative Litig., Nos. 03 Civ. 7301 (LMM), 2007 WL 2615928, at *10 (S.D.N.Y. Sept. 10, 2007).[78]

A. Securities Act Claims Are Subject To The Rule 8 Pleading Standard

For Securities Act claims, a complaint need only "say enough to give the defendant 'fair notice of what the plaintiff's claim is and the grounds upon which it rests,'" in compliance with Rule 8(a) of the Federal Rules of Civil Procedure. *Tellabs,* 551 U.S. at 319 (*quoting Dura Pharms., Inc. v. Broudo*, 544 U.S. 336, 346-47 (2005); *see also In re WorldCom, Inc. Sec. Litig.,* 294 F. Supp. 2d 392, 406 (S.D.N.Y. 2003).[79] "[T]he PSLRA pleading requirements have no application to claims that arise under Section 11 or other provisions of the Securities Act (e.g., Section 15)." *In re Initial Public Offering Sec. Litig.*, 241 F. Supp. 2d 281, 338 (S.D.N.Y. 2003).

Defendants argue that Plaintiffs' Securities Act claims "sound in fraud," and thus must be pled with particularity under Rule 9(b). For the reasons described above in Section II in connection with Plaintiffs' Section 14(a) claims, this is not so.

As discussed below, Plaintiffs have more than satisfied the applicable pleading standard of Rule 8, and indeed, even if this Court were to find it necessary, have alleged sufficient facts to satisfy Rule 9(b).

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[78] Defendants' only argument against Plaintiffs' Section 15 claims is that Plaintiffs have inadequately alleged a primary violation of the Securities Act. As described below, Plaintiffs have more than adequately alleged violations of Sections 11 and 12, therefore, the alleged control persons are liable under Section 15.

[79] As many courts have recognized, *Bell Atl., Inc. v. Twombly*, 550 U.S. 544 (2007) did not change the notice pleading requirements under Rule 8(a). *See Erickson v. Pardus*, 551 U.S. 89, 93 (2007) (per curiam) (post-*Twombly* opinion confirming that a complaint "need only 'give the defendant fair notice of what the claim is and the grounds upon which it rests'"); *Rivell v. Private Health Care Sys., Inc.*, 520 F.3d 1308, 1309 (11th Cir. 2008); *BMC-The Benchmark Mgmt. Co. v. Ceebraid-Signal Corp.*, 508 F. Supp. 2d 1287, 1290 (N.D. Ga. 2007); *see also Aktieselskabet AF 21. Nov. 2001 v. Fame Jeans Inc.*, 525 F.3d 8, 15 (D.C. Cir. 2008) ("*Twombly* leaves the long-standing fundamentals of notice pleading intact."). Here, Defendants are on notice of the statements which are at issue and why such statements are allegedly false.

B. Materially False And Misleading Statements In The Offering Documents

As set forth above at Sections II.C.1-4 and II.C.6, the Complaint contains ample allegations that statements in BoA's Offering Documents concerning the existing agreement on Merrill bonuses (¶¶365-68) and the benefits and impact on BoA of the merger (¶¶369-71) were materially false and misleading when made. The Offering Documents incorporated the Merger Agreement and the September 15 press release by reference. ¶¶365, 369. Plaintiffs respectfully refer the Court to Section II.C of the brief for this purpose.

C. Defendants' Due Diligence Defense Is Unavailing

Defendants argue that the Section 11 and 12 claims should be dismissed for failure to adequately plead Defendants' negligence. BoA Br. 31-32. However, negligence is not an element of a claim under Sections 11 or 12. Rather, "[u]nder both sections, the burden is on ***defendants*** (other than issuers under Section 11) to 'exculpate' themselves by proving either good faith or due diligence. Plaintiffs, therefore, need not affirmatively plead negligence." *In re Initial Public Offering*, 241 F. Supp. at 396 (emphasis in original); *see also In re Fuwei Films Sec. Litig.*, 634 F. Supp. 2d 419, 435 (S.D.N.Y. 2009). Given that BoA was acting in a dual capacity as an issuer and an underwriter with respect to the offering, and that Merrill could not possibly complain of its inability to discover its own financial condition or its own right to accelerate and pay billions in bonuses, it is highly unlikely that these Defendants will ever establish such a defense at any time in this case, much less at the outset of the litigation in a 12(b)(6) dismissal motion.

With respect to the remaining Defendants, although not required to plead negligence, Plaintiffs have sufficiently alleged their lack of good faith or due diligence in issuing the allegedly false and misleading statements by alleging that these Defendants had access to facts

that stood in stark contrast to the disclosures in the Registration Statement, such as the omitted Disclosure Schedule. *See* Section II hereof.

Further, with respect to the September 15, 2008 representation that the merger would be highly beneficial to BoA, Plaintiffs allege that these Defendants failed to conduct a ***reasonable*** due diligence effort to support their claims. ¶371. *See In re Atlas Air*, 324 F. Supp. 2d at 503 (finding negligence adequately pled where defendants "failed to conduct a reasonable investigation and lacked 'reasonable grounds for the belief that the statements contained in the Registration Statement and [] Prospectus Supplement . . . were not misleading'").

Thus, as set forth above, the Complaint alleges a sufficient factual basis for the respective Defendants' liability under Sections 11, 12 and 15, and Defendants' motion to dismiss these claims should be denied.

CONCLUSION

For the reasons set forth above, Lead Plaintiffs respectfully submit that Defendants' Motions to Dismiss the Consolidated Amended Complaint should be denied in their entirety.

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