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	

REPLY MEMORANDUM OF LAW IN SUPPORT OF THE BANK OF AMERICA DEFENDANTS' MOTION TO DISMISS THE CONSOLIDATED AMENDED CLASS ACTION COMPLAINT

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TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Cases **Page**

Statutes

Other Authorities

PRELIMINARY STATEMENT

The Bank Defendants respectfully submit this reply in support of their motion to dismiss. As set forth in the Bank Defendants' opening Memorandum ("Mem."), Plaintiffs' amended complaint is legally defective.[1] The Bank made no misrepresentation whatsoever with respect to Merrill's right to pay bonuses or Merrill's interim or forecasted fourth quarter performance and fully complied with all applicable disclosure requirements related to the merger. Plaintiffs' Opposition ("Opp.") misstates the applicable law and offers no cogent response to the Bank Defendants' showing that the Complaint fails to state claim.

Plaintiffs' Opposition principally focuses on their purported Section 14(a) claims, but fails to come to grips with a dispositive threshold flaw in those claims: Plaintiffs — who did not buy, sell or exchange their Bank shares in the merger — do not have standing to assert a direct Section 14(a) claim. Both the Supreme Court and the Second Circuit have made clear that whether a federal securities law claim may be brought directly or derivatively is determined by ***state*** law. The Bank is a Delaware corporation; Delaware law controls. And the Delaware Supreme Court has squarely held that where, as here, an acquiring company's shareholders are allegedly misled into approving a dilutive transaction, there is no direct cause of action. Accordingly, Plaintiffs' Section 14(a) claims must be dismissed in their entirety. *See* Point I, *infra*.

Furthermore, Plaintiffs' claims of purported misrepresentations and omissions are fatally defective. Plaintiffs' revised theory is that the Proxy supposedly advised shareholders that the Merger Agreement imposed a contractual proscription on Merrill's ability to pay employee bonuses as it always had in the ordinary course, unless consented to by the Bank. This contention is insupportable from the face of the Proxy and materials incorporated therein. First, the Proxy expressly disclosed that the Merger Agreement ***required*** Merrill to "conduct its business in the ordinary course" and "use reasonable efforts to . . . retain the service of its key officers and key employees," and ***required*** the Bank to provide "compensation opportunities" to Merrill employees

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[1] Capitalized terms have the same meaning as in the Bank Defendant's Memorandum. Exhibits ("Ex.") are attached to the Declaration of Jonathan E. Goldin filed on November 24, 2009, and the Supplemental Declaration of Jonathan E. Goldin filed herewith.

"substantially comparable, in the aggregate, to those made available to those employees immediately prior to completion of the merger." In addition, the Proxy expressly incorporated by reference SEC filings explaining that, in order to retain key personnel, it was Merrill's "ordinary course" practice to pay its employees billions in bonuses (even in years when it incurred substantial losses). Second, the SEC filings incorporated into the Proxy made apparent that — even after entering into the Merger Agreement and despite ongoing losses — Merrill was accruing compensation expenses in roughly the same amounts as it had over the first three quarters of the prior year, indicating an intent to pay bonuses in the billions of dollars. As a matter of GAAP, Merrill could not have so accrued if it was contractually prohibited from paying bonuses. Third, ***no one read the Proxy and the materials it incorporated to say what Plaintiffs claim it could be read as saying***. To the contrary, numerous contemporaneous media accounts uniformly, and correctly, reported that Merrill intended to pay multibillion-dollar bonuses for 2008. Plaintiffs' Opposition, like their Complaint, does not point to a single contemporaneous report indicating that anyone misread the Proxy to somehow say otherwise. Finally, Plaintiffs' attempt to fall back on allegations of nondisclosure of a contractual "cap" on bonus payments, which amount was never intended to be paid and never came close to being paid — and the disclosure of which had the potential to be affirmatively misleading as to Merrill's intent and to create unwarranted expectations in its employees — is equally without merit. *See* Point II, *infra*.

Plaintiffs' claims regarding fourth quarter losses fare no better. There was no misrepresentation or actionable nondisclosure concerning the financial condition of Merrill or the Bank either prior to the shareholder vote (*see* Point III, *infra*) or thereafter (*see* Point IV, *infra*). In the five fiscal quarters prior to the vote, Merrill had reported billions of dollars of losses — including some $15 billion in pre-tax losses on an adjusted basis for the third quarter of 2008 alone (*see* Mem. 41 & n.32). Both Merrill's and the Bank's third quarter 10-Qs, which were issued in November, disclosed that "volatility and disruption" in the financial markets had "reached unprecedented levels" in "***recent weeks***" (*i.e.*, in the fourth quarter), and that "[t]urbulent market conditions in the ***short- and medium-term***" (*i.e.*, in the fourth quarter and beyond) would "continue to have an adverse impact on Merrill's core businesses." These (and other) disclosures satisfied the companies' obligation under the proxy rules to "describe" any "material changes in affairs" since their last quarterly reports and to "describe" the "known trends" that were expected to have a material impact on future performance. No more was required under the periodic disclosure regime created by the securities laws. There was no "fundamental change"; there was no duty to "correct" anything in the Proxy as nothing was said that had been rendered misleading. The continuous *ad hoc* reporting regime Plaintiffs advocate simply does not exist, and there was no duty to update the Proxy with interim results for October or November as and when they became known. *See* Point III, *infra*.

Plaintiffs' post-vote disclosure claims are similarly deficient. "Bright-line" SEC rules mandate disclosure only of the entry into, or termination of, material definitive agreements, not mere contemplation or negotiation thereof. Given the fragile state of the financial system, premature, voluntary notice that the Bank was considering invoking the Material Adverse Effect clause (which Plaintiffs call the "MAC clause") of the Merger Agreement would have been imprudent, particularly given that the Merger Agreement was ***never*** terminated. And no government funding was agreed to or provided until mid-January 2009, at which time it was promptly disclosed. No earlier disclosure was required. *See* Point IV, *infra.*

ARGUMENT

I. THE BANK'S SHAREHOLDERS — WHO DID NOT BUY, SELL OR EXCHANGE THEIR SHARES — DO NOT HAVE ANY DIRECT SECTION 14(A) CLAIM.

As a threshold matter, Plaintiffs' Section 14(a) proxy claims cannot be sustained as direct claims and must be dismissed for that reason alone. Defendants' Memorandum demonstrated:

- Both the Supreme Court and the Second Circuit have held that a federal court must look to the law of the state of incorporation to determine whether a shareholder may proceed directly on a federal securities law claim premised on harm to the corporation. *See* Mem. 70-71.
- The Delaware Supreme Court has repeatedly held that, where an acquiring company's shareholders are allegedly misled into approving a transaction that diluted their equity equally, there is no direct cause of action, because such harm is not independent of the acquiring company, which allegedly overpaid in the transaction. *See* Mem. 71-74.
- In order to sue directly, a shareholder plaintiff must show that he or she has suffered individual harm "independent of any alleged injury to the corporation." *See* Mem. 71-74.

Plaintiffs concede that *Kamen* v. *Kemper Financial Services, Inc.*, 500 U.S. 90 (1991), and *Strougo* v. *Bassini*, 282 F.3d 162 (2d Cir. 2002), hold that, "where a federal statute is silent on an issue, it is appropriate to look at state law," and appear to concede tacitly that this principle applies to whether a direct action may be maintained. Opp. 67 n.50. This principle was recently reiterated by the Second Circuit in *Halebian* v. *Berv*, 2009 WL 5101758 (2d Cir. 2009), an action for allegedly misleading statements under the proxy provisions of the Investment Company Act. Citing *Kamen* and *Strougo*, the Second Circuit ruled that "whether the action is properly classified" as direct "is ordinarily determined by state law." *Id.* at *6.

Plaintiffs argue that actions under Section 14(a) are an exception to this rule, contending that federal law governs whether they have a direct action here because supposedly "Section 14(a) is not silent" on the issue. Opp. 67 n.50. Yet Plaintiffs do not point to any language in Section 14(a) that speaks to the issue. That is because there is none: like the statutes addressed in *Kamen*, *Strougo* and *Halebian*, Section 14(a) is indeed silent on the issue.

Plaintiffs also argue that *J.I. Case Co.* v. *Borak*, 377 U.S. 426 (1964), "squarely rejected the argument that the question of rights and remedies under Section 14(a) was dictated by state law." Opp. 65. But this contention is also wrong — even putting aside that *Borak* was decided 27 years before *Kamen*, and that in the event of any conflict *Kamen* would control. In the passage Plaintiffs quote to the effect that "federal law . . . controls," the Court discussed "appropriateness of redress" (specifically, whether remedies under Section 14(a) are limited to prospective relief). 377 U.S. at 434. The quoted passage did ***not*** address the issue here — which law controls whether a Section 14(a) claim for damages is properly brought as a direct claim. While the availability of prospective relief under Section 14(a) is appropriately an issue of federal law, *Kamen* holds that the relationship between shareholders and a corporation — the critical relationship in determining whether shareholders own and control a claim — is a state law question. *Kamen*, 500 U.S. at 90.

Plaintiffs' assertion that application of state law would frustrate specific objectives of Section 14(a) (Opp. 67 n.50) is also wrong. Plaintiffs do not spell out how applying state law to determine whether they have a direct claim would frustrate any objective of Section 14(a). *Cf.* *Kamen*, 500 U.S. at 107-08 (applying state law does not frustrate objectives of Investment Company Act). And Plaintiffs' claim that *Borak* held that the objectives of Section 14(a) would be frustrated if state law controlled whether shareholders could assert a direct claim (Opp. 67 n.50) is simply untrue. *Borak* held that if the federal cause of action under Section 14(a) were limited to prospective relief or did not extend to derivative actions, then the statute's purpose would be defeated. 377 U.S. at 434-35. It did not hold that applying state law to determine if claims could be asserted by shareholders directly would undermine the statute.

Plaintiffs' claim that "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" is demonstrably wrong. Opp. 66 & n.49. In addition to *Borak*, *Kamen* and *Strougo* (two Supreme Court cases and a Second Circuit decision), Defendants cite district court decisions that have squarely addressed this question in the Section 14(a) context. *See Vogel* v. *Jobs*, 2007 WL 3461163, at *2 (N.D. Cal. 2007) ("The proper characterization of a [§ 14(a)] claim as direct or derivative is governed by the law of the state of incorporation."); *Kelley* v. *Rambus, Inc.*, 2008 WL 5170598, at *3 n.5 (N.D. Cal. 2008) (same). *See also* Mem. 71, 73.[2]

Plaintiffs' attempt to distinguish the clear holding of *In re J.P. Morgan Chase & Co. Shareholder Litigation*, 906 A.2d 766, 772-73 (Del. 2006) — that, in order to sue directly, a shareholder must have suffered harm independent of any alleged injury to the corporation — is unavailing. Plaintiffs rely upon a decision on a motion to dismiss the *federal* action in the *JPMorgan* litigation. Opp. 67 (citing *In re JPMorgan Chase & Co. Sec. Litig.*, 2007 WL 4531794 (N.D. Ill. 2007)). There, however, defendants' motion to dismiss did not raise the direct standing issue, and thus the Illinois district court's silence on the point does not support Plaintiffs' position here. In any event, that decision cannot be read to trump the clear Supreme Court and Second Circuit authority holding that state law controls, and the Delaware Supreme Court decisions (including the *J.P. Morgan* Delaware case) holding that claims of the type raised here are ***not*** direct.

Plaintiffs assert that "[i]n *J.I. Case & Co. v. Borak*, the Supreme Court held that Section 14(a) claims can be direct, derivative ***or*** both," and thus "under federal law, plaintiffs may

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[2] Plaintiffs claim that "Courts frequently permit Section 14(a) claims in the merger context to proceed directly, without any inquiry into what state law would allow." Opp. 65 n.46. But the cases cited all involve stockholders who, unlike Plaintiffs, ***exchanged their shares*** in a merger allegedly as a result of a defective proxy, and thus clearly had direct claims. *See Mills* v. *Elec. Auto-Lite Co.*, 396 U.S. 375, 377 (1970); *Mendell* v. *Greenberg*, 927 F.2d 667, 670 (2d Cir. 1990); *In re AOL Time Warner, Inc. Sec. & "ERISA" Litig.*, 381 F. Supp. 2d 192, 231-32 (S.D.N.Y. 2004); *Tracinda Corp.* v. *DaimlerChrysler AG*, 197 F. Supp. 2d 42, 49-50 (D. Del. 2002); *In re Cendant Corp. Litig.*, 60 F. Supp. 2d 354, 378 (D.N.J. 1999).

choose to plead their claims directly under Section 14(a), and courts award such relief as they believe appropriate." Opp. 65 (emphasis in original). *Borak* held no such thing. Although the Court recognized that Section 14(a) encompasses both claims that are direct and claims that are derivative, it did not hold that the very same claim can be either direct or derivative at a plaintiff's predilection. Indeed, *Borak*'s reasoning leads to the exact opposite conclusion. *Borak* implied a potential derivative right of action in certain circumstances under Section 14(a) because it recognized that the "injury which a stockholder suffers from corporate action . . . ordinarily flows from the damage done the corporation, rather than from the damage inflicted directly upon the stockholder," 377 U.S. at 432, and thus that in the absence of a derivative cause of action, there would in most instances be no cause of action at all. If it were a matter of indifference as to whether actions under Section 14(a) are brought derivatively or not, as Plaintiffs suggest, this reasoning would make no sense.

Plaintiffs' reliance on *Yamamoto* v. *Omiya*, 564 F.2d 1319, 1325-26 (9th Cir. 1977), is also misplaced. *Yamamoto*, which was decided 14 years before *Kamen*, is irrelevant: in vacating a district court order that denied class certification on a Section 14(a) claim, the Ninth Circuit referred generally to the principle that both direct and derivative claims are possible under Section 14(a), but did not address whether state or federal law determined if the claim before it could be brought directly. And *Vogel* and *Kelley* — two squarely on point post-*Kamen* cases also from the Ninth Circuit — make clear that after *Kamen*, state law controls.[3]

Finally, Plaintiffs contend that, "even if resort to state law were appropriate, Plaintiffs have properly stated a direct claim under Section 14(a)." Opp. 67. Plaintiffs argue that they satisfy the Delaware requirements for direct standing because they are seeking to recover "the decline in the price of their common shares when the true facts concerning the merger were ultimately revealed,"

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[3] Several cases cited by Plaintiffs did not involve challenges to a shareholder's ability to assert Section 14(a) claims directly, and are thus irrelevant. *See, e.g.*, *City of St. Clair Shores Gen. Employees Ret. Sys.* v. *Inland W. Retail Real Estate Trust*, 635 F. Supp. 2d 783 (N.D. Ill. 2009); *Washtenaw County Employees Ret. Sys.* v. *Wells Real Estate Inv. Trust*, 2008 WL 2302679 (N.D. Ga. 2008); *In re McKesson HBOC, Inc. Sec. Litig.*, 126 F. Supp. 2d 1248 (N.D. Cal. 2000). Other cases cited by Plaintiffs address whether shareholder reliance is necessary to prove a Section 14(a) claim, rather than the issue of standing to assert a direct claim. *See Stahl* v. *Gibraltar Fin. Corp.*, 967 F.2d 335, 338 (9th Cir. 1992); *Cowin* v. *Bresler*, 741 F.2d 410, 428 (D.C. Cir. 1984); *Bender* v. *Jordan*, 439 F. Supp. 2d 139, 164-65 (D.D.C. 2006).

and that "because [they] 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." Opp. 68. But this is not Delaware law. Indeed, Plaintiffs' citation to *Feldman* v. *Cutaia*, 951 A.2d 727 (Del. 2008), is ironic because *Feldman* makes clear that "[t]he mere fact that the alleged harm is ultimately suffered by, or the recovery would ultimately inure to the benefit of, the stockholders does not make a claim direct under *Tooley*. In order to state a direct claim, the plaintiff must have suffered some individualized harm not suffered by all of the stockholders at large." *Id.* at 733. Put another way, in order to establish direct standing under Delaware law, Plaintiffs must allege harm "independent of any alleged injury to the corporation." *In re Syncor Int'l Corp. S'holders Litig.*, 857 A.2d 994, 997 (Del. Ch. 2004).

The provisions of the Complaint that Plaintiffs cite in support of their claim of individual harm (*see* Opp. 68 (citing AC ¶¶ 261-272, 334, 349, 359)) allege only that the value of their shares declined when the "true facts concerning the merger were ultimately revealed." But that alleged harm impacted "all of the stockholders at large" and was not "independent of [the alleged] harm to the [Bank]" in allegedly overpaying for Merrill. There can be no direct remedy for such harm under Delaware law. *See* Mem. 72-74.

II. PLAINTIFFS' ALLEGATIONS REGARDING COMPENSATION TO BE PAID TO MERRILL PERSONNEL DO NOT STATE A CLAIM.

Plaintiffs assert that the Proxy ***affirmatively misrepresented*** that the Merger Agreement prohibited Merrill from paying employee bonuses — as it always had in the ordinary course — without the Bank's prior consent. This contention is wholly insupportable: the Proxy made clear that Merrill would continue — and indeed, was required to continue — to conduct its business in the ordinary course and use reasonable best efforts to retain key personnel, which would necessarily entail payment of bonuses. Merrill's publicly disclosed compensation accrual in its third quarter 10-Q reflected the cost Merrill would incur to do that: had the Merger Agreement actually contained a proscription against paying bonuses, GAAP would have required Merrill to reduce its third quarter accrual to reflect that — and potentially to reverse previous accruals as well. It was apparent to all from the Proxy and Merrill's third quarter 10-Q that — despite the merger and the difficult economic environment — Merrill would pay its employees billions of dollars in bonuses. Indeed, numerous and widespread media accounts uniformly confirmed this understanding of the Proxy and the Merger Agreement. Plaintiffs do not cite a single media account to the contrary; nor do they identify anyone who misread the Proxy to represent that no bonuses would be paid. ***No one was misled***. *See, e.g.*, *White* v. *H&R Block, Inc.*, 2004 WL 1698628, at *12 (S.D.N.Y. 2004) (dismissing complaint where the "truth was all over the market"). As shown below, nothing more was required to be said with respect to bonuses or the bonus cap.

A. There was no misrepresentation regarding bonuses.

As previously shown, the Complaint's allegations that the Proxy and the Merger Agreement affirmatively misrepresented that Merrill would not pay bonuses before the merger closed (AC ¶¶ 108, 196, 215, 217) are demonstrably false. Both documents plainly disclosed that the negative covenant contained in § 5.2(c) of the Merger Agreement was subject to three specific exceptions. *See* Mem. 12-14. Plaintiffs now concede the Proxy disclosed these exceptions (Opp. 9 (quoting § 5.2(c))), but have revised their misrepresentation theory: Plaintiffs now argue that the Merger Agreement and Proxy falsely represented that Merrill "shall not" pay bonuses prior to the merger without the Bank's consent, without disclosing that the Bank "had already agreed" to allow Merrill to pay such bonuses. Opp. 25; *see also id.* at 2, 9, 26. Plaintiffs' new theory is meritless.

As previously noted (Mem. 13), § 5.1 of the Merger Agreement contained an affirmative covenant requiring Merrill, between signing and closing, to "conduct its business in the ordinary course in all material respects" and "use reasonable best efforts to maintain and preserve intact its business organization and advantageous business relationships and retain the services of its key officers and key employees." Proxy at A-31 (Ex. 1). Documents incorporated by reference in the Proxy, including Merrill's March 2008 Proxy, made clear that "in the ordinary course" Merrill paid billions of dollars in bonuses because it was "essential that the Company pay many key employees at market levels in order to retain them and avoid long-term damage to the franchise." Merrill March 2008 Proxy at 28 (Ex. 7). And the compensation accruals disclosed in Merrill's November 5, 2008 10-Q specifically revealed the levels of compensation of "ordinary course" operations. Merrill 3Q08 10Q, at 5 (Ex. 34). Indeed, in § 6.5(a) of the Merger Agreement, the Bank itself agreed to maintain Merrill's "employee benefit plans and compensation opportunities" until ***December 31, 2009*** on terms "substantially comparable" to those provided prior to the consummation of the merger, thereby obligating the Bank to cause such bonuses to be paid if the merger closed before Merrill did so. Proxy at A-35 (Ex. 1).

Section 5.1 thus both authorized and contractually obligated Merrill to maintain its "ordinary course" compensation and bonus payments until the merger closed as part of its "reasonable best efforts" to "preserve intact its business organization" and "retain the services of its key" personnel. Proxy at A-31 (Ex. 1). Section 5.1 also manifested the Bank's fully disclosed "prior consent" to the payment of such "ordinary course" bonuses. Plaintiffs' new argument that the Bank failed to disclose that it had *already* consented to Merrill's payment of bonuses is an improper attempt to read § 5.1 out of the Merger Agreement and the description of § 5.1 out of the Proxy.

Plaintiffs attempt to brush § 5.1 aside as "meaningless" because it does not mention bonuses by name. *See* Opp. 30. This argument is frivolous: the above-quoted statements in the March 2008 Proxy made clear that the payment of billions of dollars in bonuses was an "ordinary course" business practice at Merrill — even in years like 2007 when, despite billions in losses, Merrill disclosed that it believed it necessary to pay billions in bonuses "in order to retain" "key employees" and "avoid long-term damage to the franchise." Merrill March 2008 Proxy at 28-29 (Ex. 7) ("compensation framework emphasizes variable pay," and "base salary normally represents a small percentage of total compensation"). Plaintiffs' argument is also belied by the $11.17 billion in compensation accruals that Merrill reported in its 2008 third quarter 10-Q (incorporated by reference into the Proxy), which were roughly on par with its 2007 accruals. *See* Merrill 3Q08 10Q, at 5 (Ex. 34); Proxy at 123-24 (Ex. 1). Under GAAP, Merrill could not have so accrued if it was prohibited from paying bonuses. And those accruals, which were fully disclosed to shareholders, reflected Merrill's contractual obligations under § 5.1 to use "reasonable best efforts" to retain key employees and keep its business organization intact.

Plaintiffs' new "prior consent" argument also requires the Court to ignore the fact that one of the three specific exceptions to the negative covenant in § 5.2(c) — again, fully disclosed in the Proxy — is "except as expressly contemplated or permitted by this Agreement." Proxy at A-31

(Ex. 1). The Bank's shareholders were thus told that the § 5.2(c) restrictions were subject not only to whatever the Company Disclosure Schedule provided, but also to Merrill's affirmative obligation to operate in the ordinary course and use reasonable best efforts to retain key personnel.

Reading §§ 5.1 and 5.2 together, as one must, Merrill was permitted (and required) under the Merger Agreement to pay bonuses "in the ordinary course."[4] The Company Disclosure Schedule simply made clear that payments ***in excess of the bonus cap***, even if otherwise justified by Merrill's ordinary course of business, would require the Bank's ***further consent***. One would not need to know the numerical cap in the disclosure schedule — a number that far ***exceeded*** what was paid — to know that Merrill had the contractual right (and obligation) to pay bonuses "in the ordinary course" and that the ordinary magnitude of such bonuses was in the billions of dollars.

Plaintiffs argue that the bonus cap in the Company Disclosure Schedule "effectively contradicted the stated terms of the Merger Agreement and . . . Proxy," and that disclosure of the cap was "necessary to render these statements not misleading." Opp. 26. But the bonus cap did not "contradict" — "effectively" or otherwise — the terms of the Merger Agreement and Proxy, which said nothing about whether or under what circumstances consent could or would be granted. And both documents stated that Merrill was obligated under § 5.1 to "conduct its business in the ordinary course in all material respects" and to use "reasonable best efforts" to "retain the services of its key officers and . . . employees" — an obligation Merrill could not satisfy without following its traditional practice of paying bonuses. Indeed, post-closing, the Bank was required to make ordinary course bonus payments. *Id.* at § 6.5. And the Proxy incorporated Merrill's compensation accruals

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[4] There is a "generally acknowledged distinction in merger agreements between affirmative and negative covenants: affirmative covenants require that a bound party take action while negative covenants forbid action." *Alliance Data Sys. Corp.* v. *Blackstone Capital Partners*, 963 A.2d 746, 766 (Del. Ch.), *aff'd*, 976 A.2d 170 (Del. 2009). To read a merger agreement's negative covenants without giving meaning to the affirmative covenants would "not only distort its plain meaning, it would override the carefully negotiated provision of the Merger Agreement dealing with the parties' duties to take certain affirmative actions. . . ." *Id. Cf. Postlewaite* v. *McGraw-Hill, Inc.*, 411 F.3d 63, 67 (2d Cir. 2005) ("It is . . . important to read the document as a whole to ensure that excessive emphasis is not placed upon particular words or phrases."); *Galli* v. *Metz*, 973 F.2d 145, 149 (2d Cir. 1992) ("[W]hen interpreting [a] contract we must consider the entire contract and choose the interpretation . . . which best accords with the sense of the remainder of the contract."). The Proxy's descriptions of §§ 5.1 and 5.2 must also be read together. *See Olkey* v. *Hyperion 1999 Term Trust*, 98 F.3d 2, 5 (2d Cir. 1996) ("It is undisputed that the prospectus must be read as a whole.").

that likewise indicated Merrill's intention to pay billions of dollars in bonuses. Further, both documents made clear that the limitations of § 5.2(c) were subject to multiple exceptions, including exceptions contained in the Company Disclosure Schedule.[5]

As previously shown, Plaintiffs' misrepresentation claim is also belied by the express warnings from both the Bank and Merrill that the terms of the Merger Agreement were "qualified by confidential disclosures," were "not [intended] to provide any . . . factual information regarding Merrill," and had to be read "in conjunction with" the Merrill SEC filings incorporated into the Proxy. Mem. 14-15 (quoting Merrill 9/18/09 8K, at Item 1.01; Proxy at 125); *see also* Mem. 52-53. Citing the Ninth Circuit's decision in *Glazer Capital Management* v. *Magistri*, 549 F.3d 736 (9th Cir. 2008), Plaintiffs argue these warnings are of no moment. But *Glazer* is easily distinguished. As Plaintiffs concede (Opp. 31 n.17), *Glazer* involved an affirmative misrepresentation of fact — namely, that the company to be acquired was "in compliance in all material respects with all laws" — and not a contractual covenant. 549 F.3d at 742. This difference is not "[s]emantics," as Plaintiffs would have it. Opp. 31 n.17. A negative covenant is an agreement not to take specified action, not a factual representation that a particular fact is true.[6] In addition, the Proxy here contained other disclosures making clear Merrill had the right (and obligation) to pay employee bonuses and fully intended to do so — the affirmative covenant in § 5.1 and the $11.17 billion compensation accrual in Merrill's third quarter 10-Q. In *Glazer*, no equivalent disclosure qualified the merger agreement representation that the company was "in compliance in all material respects

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[5] By contrast, in the cases Plaintiffs cite (*see* Opp. 26), the defendants made statements to investors that were unqualified by other statements in the disclosure document at issue or other documents incorporated by reference therein. *See Mendell* v. *Greenberg*, 927 F.2d 667, 678, 687 (2d Cir. 1990) (unqualified statement in proxy that officer would not "acquire an equity interest" in the company following cash merger when the company "had in fact planned prior to the issuance of the proxy statements to give [the officer] stock"); *In re Bristol-Myers Squibb Co. Sec. Litig.*, 586 F. Supp. 2d 148, 160-61 (S.D.N.Y. 2008) (company unqualifiedly represented it would "vigorously pursue" its patent rights against a competitor when, secretly, it had already "bargained away" its right to an injunction and statutory damages in settlement negotiations).

[6] *See* JAMES C. FREUND, ANATOMY OF A MERGER: STRATEGIES AND TECHNIQUES FOR NEGOTIATING CORPORATE ACQUISITIONS 153-56, 286 (1975) (contrasting covenants and representations); JOSEPH W. BARTLETT, EQUITY FINANCE: VENTURE CAPITAL, RESTRUCTURINGS AND REORGANIZATIONS § 10.8 (2008) ("The company 'represents' facts, that is existing statuses. When it 'covenants' something, the obligation is promissory; the company is promising to do (or not do) an act in the future."). Plaintiffs argue that this would be lost on the reasonable investor, but the Proxy explained it. *See* Proxy at 82-85 (Ex. 1).

with all laws." Finally, here, the Proxy and SEC filings it incorporated by reference warned investors that, because the negative covenants in the Merger Agreement were "qualified by confidential disclosures," they were not intended to provide "factual information" about Merrill. Merrill 9/18/08 8K, at Item 1.01 (Ex. 18); BofA 9/18/08 8K, at Item 1.01 (Ex. 17); Proxy at 123-25 (Ex. 1). While the *Glazer* proxy stated its representations were qualified by a disclosure schedule, it did not contain equivalent cautionary language.

For the same reasons, Plaintiffs' reliance on the SEC's Titan Report, Exch. Act Rel. No. 51,283, 2005 WL 1074830 (Mar. 1, 2005) (cited at Opp. 31-32, 35), is to no avail. Like *Glazer*, and unlike the case at bar, Titan involved an unqualified representation by a company in a merger agreement that it was in full compliance with the Foreign Corrupt Practices Act. Moreover, the SEC expressed the view in Titan that descriptions of a contractual representation in a merger agreement could be actionable where "a reasonable investor could conclude that the statements made in the representation describe the actual state of affairs." 2005 WL 1074830, at *2. Here, by contrast, the Proxy cautioned investors that the descriptions of contractual provisions were ***not*** intended to describe the actual state of affairs. In fact, those contractual provisions were not statements of fact at all, but were instead promises about future conduct by Merrill, making them different in kind from the factual representations that were the subjects of both *Glazer* and the Titan Report. In any event, the Titan Report is not an adjudicated decision, but a report under Section 21(a) of the Exchange Act, and is thus not entitled to any precedential weight. *See* Titan, at *1 n.1 ("This Report . . . does not constitute factual findings or an adjudication of any issue addressed herein."); *SEC* v. *Adler*, 137 F.3d 1325, 1339 (11th Cir. 1998) ("declin[ing] to accord much deference" to a comparable SEC investigative report).[7]

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[7] Contrary to Plaintiffs' assertion (Opp. 35), practitioners do not interpret *Glazer* and Titan as Plaintiffs do. *See* Mem. 32 & n.23. Indeed, 97% of 100 recent merger agreements summarized in an unrebutted expert report in *SEC* v. *Bank of America Corp.*, No. 09-Civ. 6829 (S.D.N.Y.) (filed Dec. 10, 2009) (Docket No. 69), were qualified by disclosure schedules, and ***none*** appended those schedules.

B. Merrill's expected compensation expense levels and intention to pay bonuses were public, and there was no actionable omission as a matter of law.

Having failed to show any affirmative misrepresentation in the Proxy, Plaintiffs contend that the Bank had a duty to disclose omitted information concerning the bonus cap. *See* Opp. 27-30. Plaintiffs' argument rests on the assertion that the federal proxy laws imposed a duty to disclose "all the objective material facts relating to the transaction" in the Proxy. Opp. 5, 27 (citing *Mendell*, 927 F.2d at 674). But that is not the correct legal standard. And, in any event, the existence of the bonus cap on top of the existing accruals was immaterial as a matter of law.

1. Plaintiffs misstate the applicable legal standard.

An omission is actionable under Section 14(a) and Rule 14a-9 only if "SEC regulations specifically require disclosure of the omitted fact in a proxy statement, or the omission makes other statements in the proxy statement materially false or misleading." *Resnik* v. *Swartz*, 303 F.3d 147, 151, 153 (2d Cir. 2002) (no duty to disclose value of option grants where SEC regulations did not specifically require it and "no statement is made materially misleading by the failure to" provide values). Unless an SEC rule requires a fact to be disclosed, Section 14(a) and Rule 14a-9 are not violated by its omission unless the fact was both material and either "necessary in order to make the statements [in the proxy] not false or misleading" or "necessary to correct any statement in any earlier communication . . . which has become false or misleading." 17 C.F.R. § 240.14a-9.

The Second Circuit's prior decision in *Mendell* is not to the contrary. There, a proxy in a cash-out merger did not disclose that the family that controlled the company urgently needed to sell to pay taxes. While the opinion includes the "all material facts" language Plaintiffs quote, it twice made clear what Section 14(a) and Rule 14a-9 actually require. *See* 927 F.2d at 670 ("When a corporation issues a proxy statement it must not contain any false or misleading statements respecting any material fact, or omit stating material facts necessary to make the statements in it not false or misleading."); *id.* at 673 ("Liability under Rule 14a-9 requires the omission of a material fact which renders the proxy statement false or misleading.") (emphasis omitted).

More recent Second Circuit authority is to the same effect as *Resnik*. *See United Paperworkers Int'l Union* v. *Int'l Paper Co.*, 985 F.2d 1190, 1198 (2d Cir. 1993) (Rule 14a-9 "prohibits the inclusion in a proxy statement of 'any statement . . . which omits to state any material fact necessary in order to make the statements therein not false or misleading.'") (emphasis omitted).[8] Plaintiffs cite no case in this Circuit that has read *Mendell* (as they do) to require a merger proxy disclose "all material facts" relating to a merger to satisfy Section 14(a) and Rule 14a-9.[9]

2. <u>There was no duty to disclose the bonus cap.</u>

Applying *Resnik*, there was no duty to disclose the bonus cap. As previously shown (Mem. 22-23), there is no line-item requirement under the proxy rules requiring disclosure of the cap. Plaintiffs do not dispute this. *See* Opp. 25-36. And Plaintiffs do not (nor could they) point to a single statement in the Proxy that was rendered false or misleading by the nondisclosure of the cap. The Proxy accurately disclosed that Merrill was obligated to "conduct its business in the ordinary course" and to use "reasonable best efforts" to "retain the services of its key" people. Proxy at A-31 (Ex. 1). The Proxy incorporated SEC filings warning investors that the negative covenants in the Merger Agreement were "qualified by confidential disclosures" and that, because that was the case, the covenants should not be relied upon as representations of fact. Merrill 9/18/08 8K, at Item 1.01 (Ex. 18); BofA 9/18/08 8K, at Item 1.01 (Ex. 17); Proxy at 123-25 (Ex. 1). And the Proxy told shareholders to rely instead on the companies' SEC filings, including Merrill's third quarter 10-Q, which contained the accruals detailing the billions in compensation, including bonuses, Merrill expected to pay. *Id.* at 123-24. The bonuses ultimately paid ($3.6 billion) were consistent with these accruals — and over ***two billion dollars less*** than the undisclosed cap. *See* Mem. 16-19.

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8 *See also Vladimir* v. *Bioenvision Inc.*, 606 F. Supp. 2d 473, 485 (S.D.N.Y. 2009) (duty to disclose arises only: (1) "when the SEC's rules require disclosure;" (2) "when an insider trades on the basis of non-public information;" and (3) when "necessary to make prior statements not misleading"); *In re Canandaigua Sec. Litig.*, 944 F. Supp. 1202, 1208 (S.D.N.Y. 1996) ("Mere non-disclosure of information will not necessarily give rise to [securities fraud] liability even if the information was material; a plaintiff must also establish that the defendant had a duty to disclose.").

9 Plaintiffs' attempt to distinguish *Resnik* (Opp. 29 n.16) because the case did not involve a merger is unavailing. Rule 14a-9 applies to all proxy solicitations, whether or not a merger is at issue. There is no reason why *Resnik*'s interpretation of Rule 14a-9 would not apply to a merger. *See* Mem. 22-23. As noted above, although the *Mendell* case did involve a merger, it actually supports *Resnik*'s reading of the rule. But even if *Mendell* could be read as Plaintiffs urge, *Resnik* and *United Paperworkers* are more recent controlling authorities and should be followed on this point.

3. <u>The bonus cap was not material as a matter of law.</u>

In any event, as previously shown (Mem. 21-23), even if Plaintiffs were able to show that the Bank had a duty to disclose the bonus cap, the existence of the bonus cap was immaterial as a matter of law. *See also* Mem. 16-20. Plaintiffs advance three arguments as to why the bonus cap was supposedly material. None has merit.

First, Plaintiffs argue that the bonus cap was material to Bank shareholders because the parties allegedly spent significant time negotiating it. Opp. 7, 27 (quoting AC ¶ 67). But materiality is not determined by reference to the amount of time spent negotiating a term: a fact is material if there is a "substantial likelihood that a reasonable shareholder would consider [the omitted fact] important in deciding how to vote" because it would have "significantly altered the total mix of information made available." *TSC Indus.* v. *Northway, Inc*., 426 U.S. 438, 449 (1976). Here, where the disclosures that were made showed that Merrill intended to pay bonuses in the multibillions — and the undisclosed "cap" bore no relation to what ***was*** paid — the bonus cap would not have "significantly altered the total mix" of available information. And the cap did not in any way impact the accruals; it was the intent to pay bonuses — not the cap thereon — that mattered.

Second, Plaintiffs assert that the bonus cap was material because the cap amount represented 12% of the merger consideration. Opp. 27. This argument again ignores that the cap represented only an upper limit on the aggregate amount of bonuses that Merrill could award without further approval by the Bank. The Complaint is devoid of any allegation that Merrill had any actual intent to pay out bonuses at the "cap" levels. Plaintiffs do not (and cannot) deny that the accrued compensation and benefit expense reflected in Merrill's financials necessarily included any amount Merrill expected to pay out in bonuses. And although Plaintiffs argue that the ***precise amount*** of the anticipated bonus payments could not be discerned from the accruals (*see* Opp. 33-34), the accruals were a more accurate gauge since the "cap" overstated the amounts actually paid by over two billion dollars. Nor can Plaintiffs dispute that the SEC's rules impose no requirement to differentiate between base salary and incentive compensation — in the merger context or otherwise — when reporting accrued compensation and benefit expense. *See* Mem. 17-18. From the standpoint of a reasonable Bank shareholder, the aggregate compensation that Merrill actually expected to pay employees — and not the bonus cap — was the potentially relevant information; it was that accrued amount, and not the ceiling established by the bonus cap, that represented Merrill's best estimate as of the time of the shareholder vote of its bottom-line, all-in compensation expense.

Plaintiffs' third and last materiality argument is that the timing of the bonus payments — the fact that bonus payments would be made to employees in December rather than January — was material because it allowed Merrill to pay bonuses despite "poor financial performance during 2008." Opp. 27-28. This argument is baseless. The amount of any portion of the accrual representing bonus payments would be the same whether bonuses were expensed on December 31 or January 2. And, as noted, it was publicly known that Merrill suffered "poor financial performance" in 2007 and had paid billions of dollars in bonuses. Moreover, in light of § 6.5, which committed the Bank to maintain the same compensation opportunities available to Merrill employees through 2009, it made no difference whether the monies were paid by Merrill *before* closing — for they would have been paid by the Bank afterwards in any event.

Plaintiffs' materiality arguments must also be rejected because, as previously shown, in the weeks leading up to the shareholder vote, the news media widely and uniformly reported that Merrill intended to pay billions of dollars in bonuses. *See* Mem. 19-20. These numerous articles and reports in television, print and online media, including *NBC News*, *The Today Show*, *CNN*, *Bloomberg*, *The New York Times*, *The Financial Times*, *Business Week* and *Fox News Network*, demonstrate the broad-based awareness in the marketplace that Merrill would be paying billions of dollars in bonuses to its employees. Plaintiffs' characterization of these articles as "speculative, incomplete and vague" (Opp. 34) is belied by the articles themselves, which (i) reported on the size of Merrill's publicly disclosed compensation accruals, (ii) quoted a Merrill spokeswoman who confirmed that the company's bonuses would not be down as much as those at Goldman Sachs and Morgan Stanley and (iii) on December 3 — just two days before the vote — reported that Merrill would pay bonuses exceeding $3 billion. *See* Mem. 19-20 (citing Ex. 29-32, 40-41).

Plaintiffs argue that the Court should ignore these reports because "Section 14(a) requires that a proxy disclose — within its four corners — all material facts regarding the proposed transaction." Opp. 33. Putting aside that "all material facts" is not the standard, *see* pp. 13-14, *supra*, this argument cannot be squared with the "total mix" doctrine as it has been repeatedly applied by courts in this Circuit since *Northway*. The cases cited by Plaintiffs (Opp. 33) are easily distinguishable. *United Paperworkers Int'l Union* v. *Int'l Paper Co.*, 985 F.2d 1190, 1199 (2d Cir. 1993), was decided in the pre-Internet era, and the Second Circuit noted the articles at issue were sporadic and not widely distributed. *Kronfeld* v. *Trans World Airlines*, *Inc.*, 832 F.2d 726, 736 (2d Cir. 1987), parrots similarly dated and inapposite law.[10] In contrast, cases holding that the "total mix" of available information includes widespread media reports are legion. *See, e.g.*, Mem. 40 n.31; *see also Garber* v. *Legg Mason, Inc.*, 2009 WL 3109914, at *2-3 (2d Cir. 2009). The widespread and uniform reporting by analysts and the media that Merrill would pay billions in 2008 bonuses show that the Proxy could not plausibly be — and indeed, was not — read as alleged in the Complaint. *Ashcroft* v. *Iqbal*, 129 S. Ct. 1937, 1949 (2009).

It is no answer that the Proxy stated that shareholders "should rely only on the information contained or incorporated by reference" in the Proxy since others are not "authorized . . . to give any information or make any representation about the merger or our companies that is different from, or in addition to, that contained in [the Proxy] or in any of the materials that have been incorporated in [the Proxy]." Proxy at 124-25 (Ex. 1). As a threshold matter, the uniform and widespread media reports stating that Merrill intended to pay bonuses in the multibillion-dollar magnitude were ***entirely consistent*** with the accruals and disclosures in the Proxy. Indeed, the contemporaneous media reports — a number of which were based on the information set forth in the Proxy and SEC filings incorporated therein — were not "different" from such disclosures. In any event, the SEC's "plain English" handbook interprets a comparable disclaimer to mean that investors should not view material outside the Proxy as having been authorized by the Bank — not to preclude

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[10] *Kronfeld* relied on two cases — *Fisher* v. *Plessey Co. Ltd.*, 559 F. Supp. 442, 446-47 (S.D.N.Y. 1983) and *Spielman* v. *General Host Corp.*, 538 F.2d 39, 40-41 (2d Cir. 1976). In *Fisher*, the defendants relied on international news sources that might not be "readily obtainable," 559 F. Supp. at 447-48, and in *Spielman*, the court afforded less weight to information omitted from a prospectus but provided in "self-serving" communications from the company's board. 538 F.2d at 41. Here, the bonus provisions were described in the Proxy, and numerous media reports from the most popular and widely available sources confirmed the market's understanding of the Proxy disclosures. *See* Mem. 12-14, 19-20.

consideration of widely reported publicly available information under the "total mix" doctrine. *See* SEC, *Plain English Handbook* 18 (1998), *available at* http://www.sec.gov/pdf/handbook.pdf.[11]

Plaintiffs' Opposition, like their Complaint, does not point to a single media or analyst report or commentary stating that Merrill could not (or would not) pay bonuses. Under these circumstances, the bonus cap was immaterial as a matter of law.

C. The Complaint fails to adequately allege negligence, much less scienter, with respect to the subject of bonuses.

Plaintiffs' bonus claims, which purport to arise under both Sections 10(b) and 14(a) (*see* Opp. 69), do not adequately plead that the Bank Defendants acted negligently, much less satisfy the heightened pleading requirements for claims, like these, that "sound in fraud." *See* Mem. 25-33.

Plaintiffs assert that their Section 14(a) and Securities Act claims do not sound in fraud and thus need only satisfy the "plausibility" requirements of Rule 8(a). Opp. 22-23, 92; *see also Iqbal*, 129 S. Ct. at 1949. But Plaintiffs do not dispute that their Section 14(a) bonus claims (that Defendants "affirmatively misrepresented," "falsely represented" and "falsely portrayed" Merrill's intention to pay bonuses) and their Securities Act allegations (that the Offering Documents were "misleading" in failing to disclose the same) essentially parallel their scienter-based Section 10(b) claims. *See* Opp. 22-23, 92; Mem. 30-31 & nn.21-22 (citing allegations). *Contrast In re Refco, Inc. Sec. Litig.*, 503 F. Supp. 2d 611, 632 (S.D.N.Y. 2007) (complaint "carefully structured so as to draw a clear distinction between negligence and fraud claims" with separate factual allegations in support of each set of claims, and a ten-paragraph section called "Defendants' Negligence").[12]

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[11] It is respectfully submitted that Judge Rakoff's January 4, 2010 ruling to the contrary is erroneous. In *Kapps* v. *Torch Offshore*, the Fifth Circuit considered news reports in evaluating the "total mix" of information available to investors, notwithstanding presence of a disclaimer warning investors to "rely only on the information contained in [the] prospectus." 379 F.3d 207, 216 (5th Cir. 2004); Torch Offshore Inc. Form 424B (Prospectus), at 3 (June 7, 2001) (Ex. 68); *see also Caiola* v. *Citibank, N.A.*, 295 F.3d 312, 328-29 (2d Cir. 2002) (finding comparable disclaimers only "relevant to the analytically distinct element of reliance"). In any event, Judge Rakoff's ruling did not exclude the reports themselves, and he subsequently ordered the SEC to respond to requests for admissions seeking to establish that the articles were authentic.

[12] Plaintiffs argue that they have pled "negligence and fraud in the alternative" and "disclaim[ed] any allegations of fraud." Opp. 23. But even the cases they rely on recognize that one "cannot evade the Rule 9(b) strictures by summarily disclaiming any reliance on a theory of fraud." *Refco*, 503 F. Supp. 2d at 633; *see also* Mem. 30-31 & n.20 (citing cases). Further, unlike in *Refco*, the Complaint here lacks a separate section detailing alleged negligence, pleading instead in only a few conclusory paragraphs that the defendants named in the Section 14(a) and Securities Act counts acted "negligently." *See* AC ¶¶ 333(g), 347, 377.

Under the leading Second Circuit authority of *Rombach* v. *Chang,* 355 F.3d 164, 172 (2d Cir. 2004), Plaintiffs' use of "wording and imputations . . . classically associated with fraud" require that they satisfy Rule 9(b) as to all of their claims. *See* Mem. 30-31.[13]

For multiple reasons addressed below, Plaintiffs fail to plead scienter. But even if the standard here were negligence, Plaintiffs' bonus claims fail.

1. Negligence is not adequately pled.

In light of the disclosures made, Plaintiffs have not (and cannot) establish that any Bank Defendant acted negligently with respect to bonus disclosures. The Proxy appropriately described §§ 5.1, 5.2 and 6.5 of the Merger Agreement (*see* Proxy 83-85, 87 (Ex. 1)), and it was clear from both the Proxy and the SEC filings incorporated therein that these contractual terms were not factual representations. The factual representation made as to compensation was Merrill's compensation accrual, which indicated that Merrill intended to pay billions in bonuses, even after the Merger Agreement was signed. These accurate disclosures cannot be deemed negligent, particularly where there is no allegation that anyone misread them. *Tuosto* v. *Philip Morris USA Inc.*, 2009 WL 4016160, at *14 (S.D.N.Y. 2009) (complaint "bereft of content and contain[ing] only legal conclusions unsupported by factual allegations" insufficient to state a claim for negligence).

No credible assertion of negligence is (or can be) made with respect to the omission of the bonus cap. As shown (*see* p. 14, *supra*; Mem. 22-23), no line-item requirement mandates disclosure of incentive compensation separate from aggregate compensation expense accruals — much less an independent requirement to disclose a "cap" on incentive compensation. Plaintiffs do not challenge this assertion; nor do they dispute the accuracy of the accruals that were disclosed or that Merrill followed industry practice by disclosing its aggregate compensation expense accrual. *See* Mem. 18 & n.6. Nor do Plaintiffs explain why a reasonable shareholder would consider the bonus cap significant when he knew the total compensation amount Merrill expected to pay.

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[13] That Plaintiffs have not asserted Section 10(b) claims against every defendant who faces a Section 14(a) claim (Opp. 23) is beside the point. In determining whether a securities claim "sounds in fraud" under *Rombach*, the "appropriate focus is on [the] underlying conduct," not on the identity of the parties named. *See Ladmen Partners, Inc.* v. *Globalstar, Inc.,* 2008 WL 4449280, at *13 (S.D.N.Y. 2008) (complaint solely asserting Securities Act claims "sounded in fraud").

Plaintiffs' negligence allegations against the Bank Defendants are wholly conclusory. *See* AC ¶¶ 333(g), 347, 376-77. The Section 14(a) and Securities Act counts of the Complaint state no factual basis to support these conclusions. Nor could they. There is no allegation that the Bank Defendants deviated from accepted practice by: accurately describing the Merger Agreement terms in the Proxy (noting exceptions existed as to certain matters); warning investors that those terms were not intended to convey factual information in part because they were qualified by a non-public schedule; incorporating into the Proxy SEC filings that included factual information on accrued compensation expense; and including in a non-public schedule of the Merger Agreement — the existence of which was identified in the public disclosures — information about a contractual cap on bonuses that reflected neither the level intended to be paid nor actually paid. *See* Mem. 12-19, 32.

Accordingly, Plaintiffs' conclusory allegations of negligence are not even "plausible on [their] face." *Iqbal*, 129 S. Ct. at 1949. And here, the PSLRA requires an even higher standard — a "strong inference" that each Bank Defendant acted negligently. *See* Mem. 31-33. Plaintiffs dispute that a "strong inference" is required, citing the Seventh Circuit's decision in *Beck* v. *Dobrowski*, 559 F.3d 680, 681-82 (7th Cir. 2009). *See* Opp. 24-25. But *Beck* is not the law in the Second Circuit and is contrary to the weight of authority.[14] In any event, whether viewed through the lens of Rule 8(a) or Rule 9(b), the Complaint fails to adequately plead negligence.

2. <u>Plaintiffs' scienter allegations are inadequate.</u>

A fortiori, having failed to demonstrate negligence, Plaintiffs' allegations cannot conceivably establish scienter. Plaintiffs' scienter allegations with respect to their bonus claim — consisting of only four paragraphs (AC ¶¶ 236, 250, 256-57) — are thin indeed. *See* Mem. 25-29. And Plaintiffs' defense of those allegations (Opp. 77-79) is equally unpersuasive.

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[14] District courts in this Circuit have held the PSLRA to require Section 14(a) plaintiffs to plead facts giving rise to a "strong inference" of negligence. Mem. 32 (citing *In re JP Morgan Chase Sec. Litig.*, 363 F. Supp. 2d 595, 636 (S.D.N.Y. 2005); *Bond Opportunity Fund* v. *Unilab Corp.*, 2003 WL 21058251, at *4 (S.D.N.Y. 2003), *aff'd*, 87 F. App'x 772 (2d Cir. 2004); *In re Elan Corp. Sec. Litig.*, 2004 WL 1305845, at *16 (S.D.N.Y. 2004)). Several appellate courts outside this Circuit are in accord. *See, e.g.*, *Little Gem Life Sciences LLC* v. *Orphan Med. Inc.,* 537 F.3d 913, 917 (8th Cir. 2008); *Knollenberg* v. *Harmonic, Inc.*, 152 F. App'x 674, 682-83 (9th Cir. 2005); *CALPERS* v. *Chubb Corp.*, 394 F.3d 126, 144-45 (3d Cir. 2004); *Hayes* v. *Crown Cent. Petroleum Corp.*, 78 F. App'x 857, 861 (4th Cir. 2003).

Plaintiffs have pleaded no facts showing that any Bank Defendant had a "motive" with respect to the bonus claim. There are no allegations demonstrating that any of them stood to receive the requisite "concrete and personal benefit" from not disclosing the bonus cap. *ECA* v. *JP Morgan Chase Co.,* 553 F.3d 187, 198 (2d Cir. 2009). In the four-page section of the Opposition devoted to discussion of "motive and opportunity," Plaintiffs fail to identify a single "motive" on the part of the Bank Defendants — none of whom, of course, was a potential recipient of a bonus from Merrill — to withhold disclosure of the bonus cap. *See* Opp. 87-90. Moreover, as shareholders holding over $1 billion in Bank stock (Mem. 28 & n.18, 46-47), the Bank Defendants would have had no incentive to deceive fellow shareholders by recommending a deal they supposedly believed would permit Merrill to take advantage of the Bank and pay unwarranted bonuses.

As to the "conscious misbehavior or recklessness" element of the scienter pleading standard, *ECA*, 553 F.3d at 198, Plaintiffs do not argue that the Complaint contains particularized allegations of scienter against any of the Bank's outside directors relating to the bonus issue. *See* Opp. 76-78. As to Bank executives Price and Cotty, Plaintiffs assert that the Complaint satisfies the PSLRA because it alleges that these two executives had "knowledge of [the] bonus agreement" and were "intimately involved in the merger negotiations and signed the Joint Proxy Registration Statement." *Id.* (citing AC ¶¶ 36-37, 178-79). But none of these cited paragraphs in the Complaint (none of which even mentions the bonus cap) nor any of the other paragraphs that describe the negotiation of the bonus cap (AC ¶¶ 67-78) allege that either Price or Cotty had any role whatsoever in negotiating the bonus cap or were even aware of its terms. Plaintiffs' scienter allegations against Price and Cotty are inadequate. *See* Mem. 26.

That leaves only Lewis and Thain. Plaintiffs reiterate the flawed argument that their allegations that Lewis and Thain "negotiated the bonus agreement" (and Thain later characterized the bonus cap as one of the "main things" the parties negotiated) suffice to establish their scienter. Opp. 77. Plaintiffs cite cases involving allegations that corporate executives were aware of facts that directly contradicted their companies' public statements on a particular subject. *See* Opp. 77-78. Here, by contrast, there is no such conflict. No reasonable investor could have read § 5.2(c) of the Merger Agreement or the Proxy as setting forth an unqualified representation that Merrill would not pay bonuses prior to closing (*see* Mem. 11-15), and Lewis's knowledge of a "cap" on the amount Merrill could pay does not contradict any public statement that the Bank or Merrill made on the subject.[15] And Defendants have not alleged with particularity any facts to suggest that Defendants consciously disregarded a clear duty to disclose the bonus cap.[16]

Even if some cogent inference of scienter with respect to the bonus cap claim could be teased out of Plaintiffs' Complaint, the "plausible nonculpable explanations" for the Bank Defendants' conduct — which *Tellabs* requires the Court to consider on this motion — are far more compelling. *See* Mem. 28 & n.18, 46-47. As noted, during the relevant time period the individual Bank Defendants owned over ***$1 billion*** in Bank stock — holdings that aligned their interests with those of the Bank's shareholders — and there is no allegation that any of them sold any shares. *See* Mem. 28 & n.18. Although Plaintiffs claim the absence of any stock sales is "of no moment" (Opp. 88), it is obvious that, given their huge personal holdings of Bank stock, the individual Bank Defendants had no financial incentive to dupe shareholders into voting in favor of a merger that they believed was contrary to their best interests. *See ECA*, 553 F.3d at 200. Plaintiffs simply offer no response to the Bank Defendants' showing that if, prior to the vote, the Bank Defendants believed the bonus cap called into question the wisdom of the merger, they had no conceivable motive to deliberately withhold that information. *See* Mem. 29.[17]

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15 Plaintiffs appear to have abandoned the argument that their allegations regarding "inconsistencies" in Lewis's public statements (*see* AC ¶ 250) give rise to an inference of scienter in view of the showing to the contrary. *See* Mem. 27. In a footnote, Plaintiffs argue that the Delaware Court of Chancery concluded that "virtually identical allegations" made in the Delaware Derivative Action adequately pleaded "bad faith." Opp. 78 n.60. But that decision did not squarely address allegations regarding bonuses (*see* Transcript, *In re Bank of America Corp. S'holder Litig.*, No. 4307-VCS, at 112-28 (Del. Ch. Oct. 12, 2009)); state law derivative claims are not subject to the federal law (PSLRA) "strong inference" standard; and, in any event, "bad faith" simply does not equate to scienter. *See Elliott Assocs.* v. *Hayes*, 141 F. Supp. 2d 344, 358 (S.D.N.Y. 2000), *aff'd*, 26 F. App'x 83 (2d Cir. 2002). Additional reasons scienter has not adequately been pled as to Thain are addressed in his separate memoranda of law.

16 The failure to disclose a known fact does not create an inference of scienter absent an obvious duty to disclose. *See ECA*, 553 F.3d at 202 (failure to disclose transaction did not support finding of scienter absent allegation that defendants knew failure to disclose was "inaccurate"); *Kalnit* v. *Eichler*, 264 F.3d 131, 142-43 (2d Cir. 2001) (board's nondisclosure of letter releasing significant shareholder from standstill agreement did not create inference of scienter because alleged duty to disclose "not so clear"); *see also In re Geopharma Sec. Litig.*, 411 F. Supp. 2d 434, 446 (S.D.N.Y. 2006) ("[F]ailure to disclose particular information, by itself, can only constitute recklessness if there was an obvious duty to disclose that information.").

17 The cases Plaintiffs cite (*see* Opp. 88) address only the inferences that can be drawn from a lack of stock sales and in no way dispel the powerful motives created by such extensive personal holdings.

Plaintiffs likewise have no answer to the showing (Mem. 29) that the disclosures that were made with respect to Merrill's intentions to pay bonuses for 2008 — including the Proxy's description of § 5.1 of the Merger, the Proxy's incorporation by reference of the $11.17 billion of compensation accruals and the Merrill spokeswoman's confirmation to *The New York Times* on October 27, 2008 that Merrill would be paying bonuses — strongly negate any inference of scienter. Clearly, "nonculpable explanations" of the Bank Defendants' conduct — *e.g.,* that they did not believe disclosure of the bonus cap was required under the federal securities laws — are far more compelling than any inference that the Bank Defendants intended to defraud anyone.[18]

III. PLAINTIFFS' ALLEGATIONS REGARDING THE FINANCIAL CONDITION OF MERRILL AND THE BANK PRIOR TO THE SHAREHOLDER VOTE DO NOT STATE A CLAIM.

Plaintiffs' claims that Defendants were required to disclose interim results for October and November and forecasts for the fourth quarter prior to the December 5 vote plainly fail as a matter of law. Plaintiffs seek to replace the orderly, bright-line, periodic disclosure regime embodied in the federal securities laws with a hodgepodge of continuous, partial, interim bulletins. There is no warrant for doing so. As previously shown:

- Merrill's November 2008 10-Q (incorporated into the Proxy) set forth that Merrill's third-quarter results had been abysmal: Merrill reported pre-tax losses of over ***$15 billion*** for that period on an adjusted basis. *See* Mem. 41 & n.32.
- Merrill's atrocious third-quarter results followed on the heels of a year of consistent multibillion-dollar losses quarter after quarter. Together, Merrill's adjusted pre-tax losses for the five quarters from the third quarter of 2007 through the third quarter of 2008 totaled nearly ***$50 billion*** — *i.e.*, average pre-tax losses of nearly ***$10 billion per quarter***. Mem. 41.

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[18] Plaintiffs also raise the spurious argument that Lewis was motivated by a desire to amass "prestige" by "mak[ing] BoA the largest bank in the country." Opp. 88. Putting aside that this allegation is without foundation in the source material (AC ¶ 59), this is precisely the sort of "generalized desire" common among corporate executives that the Second Circuit has held not to constitute scienter. *See ECA*, 553 F.3d at 200-01 (interest in obtaining "lucrative acquisition proposal" too generalized to constitute scienter); *Teamsters Local 445 Freight Div. Pension Fund* v. *Dynex Capital Inc.*, 531 F.3d 190, 196-97 (2d Cir. 2008) (desire to maintain appearance of profitability shared by virtually all corporate insiders not evidence of scienter).

- Both the Bank's and Merrill's November 2008 10-Qs sharply warned of "unprecedented" "disruption" in "recent weeks" and that "adverse" conditions were continuing to "materially impact" Merrill in the "short- and medium-term." *See* Mem. 42-43.

Given these consistently dismal results and stern warnings of deterioration in conditions continuing to plague Merrill, no reasonable investor would have been under a misimpression that Merrill's fourth-quarter results were suddenly expected to improve. In any event, the disclosures made plainly were sufficient under the federal securities laws and Plaintiffs' claims should be dismissed.[19]

A. <u>The Bank had no duty to disclose interim results or forecasts.</u>

As shown, the Bank was not required to disclose Merrill's or the Bank's interim fourth quarter results or forecasts. *See* Mem. 33-39. The federal courts have repeatedly recognized that the securities laws "create a system of periodic rather than continual disclosures," *Higginbotham* v. *Baxter Int'l Inc.*, 495 F.3d 753, 760 (7th Cir. 2007), and there is accordingly no duty to disclose intra-quarter results or forecasts. *See* Mem. 34-36.

Plaintiffs argue the cases so holding are "mere projections" cases. Opp. 40. Not so: numerous cases squarely hold that under the periodic reporting system imposed by the federal securities laws, there is no duty to disclose interim financial results. *See* Mem. 35-36 & n.25 (citing, *e.g.*, *Higginbotham*, 495 F.3d at 760 (no duty to disclose accounting fraud until next quarterly report due); *In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1432 (3d Cir. 1997) (Alito, J.) (rejecting claim of "continuous duty to update the public with either forecasts or hard information that would in anyway change a reasonable investor's perception"); *In re N. Telecom Ltd. Sec. Litig.*, 116 F. Supp. 2d 446, 459 (S.D.N.Y. 2000) ("The rule that there is no obligation to pre-announce results has long been embraced by courts.")).[20]

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[19] Although Plaintiffs' Opposition is focused primarily on Merrill's interim results, Plaintiffs also assert that the Bank improperly failed to disclose its own interim fourth quarter results and forecasts. *See, e.g.*, Opp. 36-37, 47; AC ¶ 12. This claim suffers from essentially the same defects as Plaintiffs' Merrill-based claims: the Bank had no duty to disclose its own interim results or forecasts and Plaintiffs have not pled facts demonstrating that this information was material or that its disclosure was necessary to make the statements contained in the Proxy not false or misleading.

[20] Plaintiffs cite *Blum* v. *Semiconductor Packaging Materials Co.*, 1998 WL 254035, at *2 (E.D. Pa. 1998) for the proposition that, while a company may not have the obligation to provide an intra-quarter update to shareholders under normal circumstances, there is an "exception" when a "fundamental change" has

Nor do Plaintiffs' other duty-to-disclose arguments have any merit. ***First***, as with their bonus cap claim, Plaintiffs' assertion that Section 14(a) and Rule 14a-9 required the Bank Defendants to disclose "all material objective facts relating to the transaction" (Opp. 37) misstates the law. *See* pp. 13-14, *supra*.[21]

Second, Plaintiffs argue the SEC proxy rules required disclosure of Merrill's interim losses. *See* Opp. 41-42. But, as shown, the regulation applicable to the information provided in a proxy related to a stock-for-stock merger, Form S-4, does not impose any obligation to disclose interim results or forecasts. *See* Mem. 38-39.[22] Item 10 of Form S-4, 17 C.F.R. § 239.25, requires the "registrant" in a stock-for-stock merger to "[d]escribe any and all material changes in the registrant's affairs that have occurred since the end of the latest fiscal year . . . and that have not been described in a report on Form 10-Q . . . or Form 8-K." Item 11 of Form S-4 permits the

occurred. Opp. 40. The quoted portion of *Blum* cites the Third Circuit's decision in *Burlington* in which the Court ***rejected*** the argument that a company had a duty to update a public earnings projection once it obtained hard information that was materially different, 114 F.3d at 1432-33, and clarified that it was "not saying that once a fundamental change is announced the company faces a duty continuously to update the public with all material information relating to that change." *Id.* at 1434 n.20.

Although Plaintiffs have not done so, the SEC has alleged that the Bank was required to disclose Merrill's October and November losses as a "fundamental change" from prior results under Item 512(a)(1)(ii) of Regulation S-K. That claim lacks merit. Under Item 512, the Bank gave an undertaking to the SEC to update the *prospectus sent to Merrill shareholders* in the event of a "fundamental change" in the *Bank's* business. 17 C.F.R. § 229.512(a). The rule thus has no bearing on disclosures made in the *Proxy sent to Bank shareholders* related to changes in *Merrill's* business. *Id.* In any event, a "fundamental change" within the meaning of Item 512 is one that relates to "major changes in the issuer's operations, such as significant acquisitions or dispositions," and not to "variations in matters such as operating results, properties, business, product development, backlog, management and litigation." Sec. Act Rel. No. 6383, Exch. Act Rel. No. 18,524, 1982 WL 90370, at *29 (Mar. 3, 1982).

[21] Plaintiffs cite an SEC release that supposedly "mandates disclosure of any material information that becomes known *after* the issuance of a proxy." Opp. 37 (emphasis in original). The release says no such thing: it addresses the amount of time that revised preliminary proxy materials must be on file before definitive proxy materials can be issued and does not purport to create an independent disclosure obligation. *See* Sec. Act Rel. No. 6676, Exch. Act Rel. No. 23,789, 1986 WL 722059, at *5 (Nov. 10, 1986). Plaintiffs' reliance on *In re Bank of America Sec. Litig*., 78 F. Supp. 2d 976 (E.D. Mo. 1999), is also misplaced, as that case noted its ruling was contrary to the controlling law of the Second Circuit. *Id.* at 993.

[22] Plaintiffs assert that "Defendants had a regulatory duty to comply with Schedule 14A." Opp. 41. Form S-4, rather than Schedule 14A, is the regulation applicable to solicitations made in connection with stock-for-stock mergers. *See* 17 C.F.R. § 239.25, General Instructions A, E.1; 17 C.F.R. § 230.145, Note 2(a)(2); 11 LORNE & BRYAN, ACQUISITIONS & MERGERS § 3:39 (2009) ("To the extent that an acquisition transaction is covered by both the proxy rules and Form S-4, the provisions of Form S-4 will prevail, so that only the information requirements of the form need be satisfied."). And, in any event, by complying with the Form S-4 requirements, the Bank satisfied Schedule 14A as well.

registrant to incorporate by reference into the prospectus its latest annual and quarterly reports, which are required to include "management's discussion and analysis" (referred to as "MD&A") disclosures as set forth in Item 303 of Regulation S-K. *See* 17 C.F.R. §§ 239.25, Item 11(a)(1), (2); *see also* 17 C.F.R. § 229.303. The MD&A rules require annual and quarterly reports to "describe any known trends" affecting the registrant's liquidity and capital resources or are reasonably expected to "have a material favorable or unfavorable impact on [its] net sales or revenues or income from continuing operations." 17 C.F.R. § 229.303(a)(1), (a)(2)(ii), (a)(3)(ii). The information required by Items 10 and 11 must be provided for both the registrant (here, the Bank) and the company to be acquired (here, Merrill). *See* 17 C.F.R. § 239.25, Item 15.

Neither Item 10 of Form S-4 nor Item 303 of Regulation S-K requires disclosure of intra-quarter financial results. These rules require only narrative descriptions of "material changes in the registrant's affairs" since its last quarterly report and "known trends" affecting liquidity, capital, revenue and sales. *See* Sec. Act Rel. No. 6835, Exch. Act Rel. No. 26,931, 1989 WL 1092885, at *3 (May 18, 1989) (MD&A requires a "narrative explanation of the financial statements") (quoting Sec. Act Rel. No. 6711, Exch. Act Rel. No. 24,356, 1987 WL 847497, at *3 (April 17, 1987)); *cf. In re Lyondell Petrochem. Co. Sec. Litig.*, 984 F.2d 1050, 1053 (9th Cir. 1993) (Item 303 imposes no requirement to disclose forecasts). Tellingly, Plaintiffs fail to cite any authority interpreting these rules to require disclosure of intra-quarter losses in a merger proxy. *See* Opp. 41-42.

The Proxy fully satisfied Item 10 and the MD&A rules in Item 303 by (1) including a "Recent Developments" section that contained explanations of both companies' third quarter performance (Proxy at 35-37 (Ex. 1)) and (2) incorporating by reference the third quarter Forms 10-Q filed by Merrill and the Bank on November 5 and 6, 2008, respectively. These documents contained extensive discussion of both the "material changes" in the affairs of both Merrill and the Bank during the third quarter and the "known trends and uncertainties" having an unfavorable impact on both companies' fourth quarter performance. Thus:

- The Proxy disclosed that "market conditions ha[d] been ***extremely volatile***" during "***the past few weeks***," that Merrill's third quarter results were impacted by "severe market dislocations in September," that the Bank's third quarter earnings were "impacted . . . as credit costs continued to rise," and that a "challenging and uncertain" market environment was "***expected to persist***." Proxy at 35-38, 52 (Ex. 1) (emphasis added).

- Merrill's November 5 third quarter 10-Q disclosed that the "adverse market environment ***intensified towards the end of the [third] quarter, particularly in September***, and was characterized by increased illiquidity in the credit markets, wider credit spreads, lower business and consumer confidence, and concerns about corporate earnings and the solvency of many financial institutions" and predicted that "[t]urbulent market conditions in the short- and medium-term ***will continue to have an adverse impact*** on [its] core businesses." Merrill 3Q08 10Q, at 82-83 (Ex. 34) (emphasis added).

- The Bank's November 6 third quarter 10-Q noted ongoing "market turmoil and tightening of credit" and cautioned that "***[i]n recent weeks [i.e., during the fourth quarter], the volatility and disruption [had] reached unprecedented levels***." It warned that these difficult conditions could "continue or worsen" and "could lead to losses or defaults." Specifically as to Merrill, the Bank predicted that the valuation of Merrill's various exposures to the credit markets "***will continue to be impacted*** by external market factors," and that Merrill's "future results may ***continue to be materially impacted*** by valuation adjustments." BofA 3Q 10Q, at 175-77 (Ex. 35) (emphasis added).

And elsewhere in the documents incorporated by reference into the Proxy, Merrill provided further detail regarding the adverse impact of market conditions on its various business segments:

- "FICC (Fixed Income, Currency and Commodities) recorded ***significant losses*** as a result of ***severe market dislocations in September***, including credit spread volatility and the default of a major U.S. broker-dealer." Merrill 3Q08 10Q, at 78 (Ex. 67) (emphasis added).

- "***[C]hallenging market conditions, particularly in September***, resulted in net losses in FICC and lower revenues in Investment Banking." *Id.* at 95 (emphasis added).

- "During the third quarter of 2008, and ***particularly in September***, the credit and equity markets continued to experience ***significant deterioration***, as spreads across the financial services sector widened dramatically and equity valuations fell, significantly increasing the cost and decreasing the availability of both funding and capital." *Id.* at 109 (emphasis added).

Plaintiffs argue that these disclosures did not inform investors of Merrill's October and November 2008 losses. Opp. 42. But neither Item 10 nor Item 303 required the Bank to do so. And neither rule creates an affirmative obligation to issue updated descriptions of "material changes" or "known trends" every day that a proxy is outstanding. If Plaintiffs' reading of these provisions were correct, every public company's quarterly and annual reports would be required to disclose the results for the weeks since the last fiscal quarter ended (rather than the "known trends" themselves), and issuing a proxy would entail continuous bulletins of developments as they occur. For good reason, that is not the law. *See Gallagher* v. *Abbott Labs.*, 269 F.3d 806, 809 (7th Cir. 2001) ("Regulation S-K does not replace periodic with continuous disclosure.").[23]

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[23] Plaintiffs argue that Item 303 was not satisfied because "incorporation by reference is sufficient only if the information accurately discloses the trends *as they exist at the time of the Proxy*," and the disclosures in the Form 10-Q regarding market conditions "were current only through September 2008, not as of the time of the vote." Opp. 42 (emphasis in original). That is false. As is apparent from the above-quoted excerpts, the

B. Defendants' optimistic statements about the merger did not trigger any duty to disclose fourth quarter interim results or forecasts.

Unable to find any duty to disclose interim results or forecasts in the applicable line-item requirements, Plaintiffs argue that the Bank Defendants made "numerous positive statements" about the merger at the time it was announced and were therefore obligated to update them prior to the shareholder vote under Rule 14a-9 by disclosing fourth quarter interim losses or forecasts. *See* Opp. 42-47. Plaintiffs are wrong.

Rule 14a-9 is explicit as to the scope of a company's obligations to disclose post-proxy, pre-meeting developments. It requires such disclosures to the extent "necessary to correct any statement in any earlier communication . . . which has become false or misleading." 17 C.F.R. § 240.14a-9. Here, disclosure of the interim fourth quarter results or forecasts was not necessary to "correct" any prior statement that had become false or misleading: the Proxy contained no disclosures of interim or forecasted fourth quarter results for either Merrill or the Bank. To the contrary, as noted, the Proxy and its incorporated filings warned of market disruption and expected losses in the "short- and medium-term." *See* pp. 26-27, *supra*; Mem. 42-43.

Plaintiffs nevertheless argue that a series of optimistic statements when the merger was first announced in September triggered a duty to update. *See* Opp. 45-46. But none of these September statements addressed fourth-quarter performance; they instead constituted generalized statements of optimism regarding anticipated merger benefits once the companies were combined — benefits which in fact have been realized (Mem. 2). As the Second Circuit has held, "there is no duty to update [such] vague statements of optimism or expressions of opinion." *In re IBM Corp. Sec. Litig.*, 163 F.3d 102, 105, 110 (2d Cir. 1998) (no duty to update statement that company had "no plans" to cut dividend and "fully expect[ed] [its] cash flow . . . [to be] sufficient to cover the dividend," when six weeks later it decided that dividend was "likely to be cut," because initial statement was "not sufficiently concrete"). And a decision to release results on the SEC's reporting

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third quarter 10-Qs filed by Merrill and the Bank contained disclosures regarding "known trends" — the extremely volatile market conditions that had continued into the fourth quarter — and disclosed that those conditions were having an adverse effect on their fourth quarter performance. That said, the Bank had no duty to continuously update its trend disclosures until the vote occurred.

timetable does not contravene any alleged duty to update, even where prior positive statements exist in the marketplace. *See In re Verity Sec. Litig.*, 2000 WL 1175580, at *4-7 (N.D. Cal. 2000).[24]

In any event, Plaintiffs ignore the statements contained in the Proxy and the incorporated 10-Qs that graphically disclosed the disarray in the credit markets and its anticipated adverse impact on the financial condition of both companies. If (contrary to law) the generalized September 15 statements had given rise to any duty to update, these later disclosures satisfied it.

C. The Proxy's description of the MAC clause did not trigger any duty to disclose interim fourth quarter results or forecasts.

Plaintiffs also argue the Proxy's description of the MAC clause somehow constituted a representation to the Bank's shareholders that Merrill had not suffered a MAC prior to the shareholder vote, such that the Bank Defendants had a duty to update the Proxy by disclosing Merrill's interim fourth quarter results or forecasts. Opp. 46, 54. This claim is frivolous.

Neither the Merger Agreement nor the Proxy represented to investors the absence of a MAC at Merrill. As noted, the Proxy accurately disclosed the Merger Agreement terms and cautioned investors that the parties' contractual representations and warranties were "subject to important qualifications and limitations agreed to between the parties" and were "included in the agreement for the purpose of allocating risk between the parties rather than to establish matters as facts." Proxy at 83, 125 (Ex. 1).[25] No reasonable investor would have read the Proxy's description of the MAC clause as a factual representation as to the financial condition of either company. *See* Mem. 52-53; pp. 11-12, *supra*.

But even if the Proxy's description of the MAC clause were misread in this fashion, the clause cannot be read in a vacuum. Both the "Recent Developments" section of the Proxy and the companies' November 10-Qs made clear Merrill's recent history of multibillion-dollar losses and

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[24] Plaintiffs predicate their Section 14(a) and Section 10(b) claims on many of the same alleged misstatements or omissions. *See* Opp. 42, 45, 46, 55-61, 69. But while Rule 14a-9 requires a speaker "to correct any statement . . . which has become false or misleading," Rule 10b-5 does not. *See* pp. 36-37, *infra*.

[25] Indeed, the MAC clause specifically excepted adverse effects stemming from market conditions (unless the impact on Merrill was substantially disproportionate relative to its competitors). *See* Proxy at 82, A-13, A-14 (Ex. 1).

the prospect of additional losses in the future. *See* pp. 26-27, *supra*. Thus, even if the purported "representation" in the Proxy that Merrill had not suffered a MAC gave rise to a duty to update, the Bank Defendants fully discharged that duty.[26]

D. Merrill's interim results and forecasts were not material as a matter of law.

Disclosure of Merrill's interim results or forecasts prior to the vote would not have "significantly altered the 'total mix' of information." *TSC Indus.*, 426 U.S. at 449. As noted, the market was advised of Merrill's history of multibillion-dollar losses and cautioned that the ongoing financial crisis would adversely impact its results in the short- and medium-term. These disclosures warned investors that Merrill could well suffer major fourth quarter losses. *See* Mem. 40-43.

Plaintiffs argue that Merrill's history of multibillion-dollar losses leading up to the vote is "irrelevant" because the Bank supposedly 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." Opp. 38-39 & n.22. But the Bank said just the opposite. *See* pp. 23-27, *supra*. Moreover, at an investor conference on November 11, Thain, likening the economic climate "to the 1929 period," warned that Merrill was "not going to get better quickly" as "asset prices [were] falling," and that Merrill was "going to be in a difficult credit environment in the near term." 11/11/08 Conf. Tr., at 2-3 (Ex. 36). And, at the December 5 meeting, Lewis told shareholders that the Bank faced "extraordinarily bad times" and the "worst economic slump since the Great Depression." Transcript of Shareholder Meeting, December 5, 2008, at 14-15 (Ex. 64).

In other words, far from making rosy fourth quarter predictions, the Bank's and Merrill's disclosures leading up to the shareholder vote accurately and quite pointedly presented that

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[26] Plaintiffs assert that the Bank's "highest ranking executives repeatedly debated terminating the transaction in the weeks leading up to the vote." Opp. 38, 46. This assertion — like the corresponding Complaint allegations (AC ¶¶ 7, 232, 247) — rests upon a misreading of the source on which it relies. *See* Mem. 53 n.40. In any event, there is no allegation that anyone at the Bank reached the decision at that time that a MAC had taken place. Plaintiffs' related attempt to draw support from a comment by Vice Chancellor Strine in the Delaware derivative action that "if [Lewis] is seriously pondering the declaration of a MAC" prior to the vote "many people would want to know" (Opp. 38) is of no aid, as the Complaint here does not allege Lewis was seriously pondering that issue, that he ever raised it with the board, or that the Bank ever altered its intent to close the merger before the vote. Indeed, any such allegation would be implausible: before the vote, the board could have scuttled the merger by withdrawing its recommendation and allowing shareholders to vote it down — there would have been no need to litigate a MAC. *See* Mem. 53.

bleak picture. *See* Mem. 40-43. And contrary to Plaintiffs' assertion (Opp. 39), there was nothing "vague" or "generic" about these disclosures: the harsh impact of widening credit spreads and falling asset prices on the valuation of Merrill's positions was specifically highlighted.[27]

E. Plaintiffs' state of mind allegations with respect to the nondisclosure of interim results or forecasts are inadequate.

The Bank Defendants' accurate (and indeed quite prescient) disclosures regarding the impact of market conditions on Merrill's fourth quarter performance cannot remotely be deemed negligent. And the omission of interim results for October or November that were neither required to be disclosed by any line item of the proxy rules nor needed to "correct" another statement made does not demonstrate any failure of due care. *See also* pp. 23-29, *supra*. Plaintiffs' conclusory allegations of negligence are not "plausible on [their] face." *Iqbal*, 129 S. Ct. at 1949.

Furthermore, particularized allegations of ***scienter*** are required because the claims sound in fraud. *See* pp. 18-19, *supra*. Plaintiffs fail to plead facts giving rise to a "strong inference" of scienter. *See* Mem. 43-47. The Opposition fails to identify any "concrete and personal benefit" any defendant received by not disclosing this information. *See ECA*, 553 F.3d at 198; Mem. 45.[28]

In addition, Plaintiffs' attempt to show "strong circumstantial evidence of conscious behavior or recklessness" falls far short. Plaintiffs assert that Defendants received regular updates concerning Merrill's financial condition. But such generalized allegations of "access to information" do not suffice. *See, e.g.*, *Konkol* v. *Diebold, Inc.*, 2009 WL 4909110, at *3-4 (6th Cir. 2009) (allegations of "access to information" through periodic reports, absent "detailed facts regarding the . . . reports, how they were used, and their connection to Defendants" do not give rise to a "strong inference" of scienter); *accord Dynex*, 531 F.3d at 196 ("[W]here plaintiffs contend

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[27] Plaintiffs assert that "debating whether Merrill's losses constituted a material[] adverse change . . . prior to the vote establishes" the materiality of Merrill's interim losses. *See* Opp. 38, 39-40 n.23. But putting aside the absence of support for any such "debate," had the Bank's management actually viewed the interim results as "material," they could have simply withdrawn their recommendation. *See* n.26, *supra*.

[28] Plaintiffs argue that Lewis, Price and Cotty were motivated to conceal facts from the Bank's shareholders because revealing the truth about Merrill's financial condition would result in shareholders questioning their judgment in acquiring Merrill. This is not the type of tangible personal benefit required to show motive. *See Kalnit*, 264 F.3d at 139-40 (motives to have "the corporation to appear profitable" and to "avoid[] . . . personal liability" are insufficient).

defendants had access to contrary facts, they must specifically identify the reports or statements containing this information.").[29] The Complaint fails to allege what interim results were known to the Bank and when, and it does not allege that, even if known, the results were reliable. *See* Mem. 43-45; *see also* Form 10-Q, Instruction A(1), 17 C.F.R. § 249.308a (requiring 10-Q filings "40 days after the end of the fiscal quarter"). In particular, the Complaint does not allege when Bank Defendants learned of either Merrill's $7 billion October loss or its November loss relative to when the Proxy was sent to the Bank's shareholders; nor does it allege any basis for concluding that those losses were inconsistent with the "known trends" that were disclosed to investors in the companies' third quarter 10-Qs of November 5 and 6. Instead, the Complaint improperly conflates actual and projected losses. *See* Mem. 33 n.24, 44 n.34.[30] Moreover, Plaintiffs have not pled facts demonstrating that Defendants consciously disregarded a duty to disclose. *See* pp. 20-23, *supra*. Accordingly, Plaintiffs' generalized allegations that the Bank Defendants were kept apprised of Merrill's condition in the fourth quarter do not give rise to the requisite strong inference of scienter. Furthermore, as previously shown, the various alleged "inconsistencies" in Lewis's statements (Opp. 80-81) are unpersuasive and fall short. *See* Mem. 46 n.36.

Plaintiffs have also failed to dispel the compelling inferences of nonfraudulent intent that *Tellabs* requires the Court to consider. Plaintiffs do not dispute that Defendants' $1 billion in Bank stock aligned their interests with the Bank's shareholders. *See* Mem. 28 & n.18, 46-47. Nor do they explain why — much less with the cogency *Tellabs* demands — the Bank Defendants would intentionally or recklessly injure their own economic interests. Plaintiffs also have no answer to the point that, if the Bank Defendants had actually come to the conclusion, prior to the December 5 vote, that Merrill's fourth quarter losses were such that it was contrary to the Bank's interest to proceed

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[29] *In re GlobalStar Sec. Litig.*, 2003 WL 22953163, at *7 (S.D.N.Y. 2003) is inapposite. There, defendants possessed "***specific information*** which called into doubt their ***stated projections***." *Id.* (emphasis added). Here, Plaintiffs have failed to identify any statement ***contradicted*** by Merrill's interim results or forecasts, as no statement concerning Merrill's fourth quarter interim results or forecasts was ever made.

[30] Plaintiffs' assertion that, in any event, "Defendants knew Merrill's results for October and November" and that "numerous facts establish that Merrill had actually suffered more than $15 billion of losses before the vote" (Opp. 82 (citing AC ¶¶ 88-90)) is unsupported by their Complaint. *See* Mem. 33.

with the merger, they had every incentive to ***disclose*** that conclusion so that the Bank's shareholders could vote down the merger. *See* Mem. 47; *Faulkner* v. *Verizon Commc'ns, Inc.*, 156 F. Supp. 2d 384, 394 (S.D.N.Y. 2001) (rejecting scienter allegation where acquiror would "obviously have benefited by announcing its withdrawal from the merger immediately after learning of [target's] revised third-quarter [earnings results];" it was "simply illogical to conclude" that acquiror "would have deliberately concealed that decision" because it "had nothing to gain" by doing so).

IV. PLAINTIFFS' ALLEGATIONS REGARDING POST-VOTE CONSIDERATION OF INVOKING THE MAC CLAUSE, DISCUSSIONS WITH REGULATORS, AND INTERIM RESULTS OR FORECASTS FAIL TO STATE A CLAIM.

After the December 5, 2008 shareholder vote, Plaintiffs concede that their only claims arise under Section 10(b). *See* Opp. 69-70. These claims are fatally flawed. *See* Mem. 48-56.

A. There was no actionable misrepresentation or omission regarding consideration of invoking the MAC clause and, in any event, no "strong inference" of scienter is pled.

As previously shown, there was no duty to disclose the Bank's consideration of the possibility of invoking the MAC clause after the shareholder vote. The applicable SEC regulation provides that a company is not required to disclose its discussions or negotiations regarding the potential termination of a definitive material agreement "unless and until the agreement has been terminated." Mem. 51-53. Plaintiffs' attempt to argue (Opp. 44-45, 72-73) for a "duty to update" based on *In re Time Warner Sec. Litig.*, 9 F.3d 259 (2d Cir. 1993), and *In re Gulf Oil/Cities Service Tender Offer Litig*., 725 F. Supp. 712 (S.D.N.Y. 1989), is unfounded.

Time Warner is inapposite. In 1989, Time Warner, saddled with excessive debt, announced it was seeking international "strategic partners" in an effort to infuse billions of dollars of capital into the company. Between November 1990 and June 1991, the company issued a series of statements confirming ongoing discussions with potential partners, but failed to acknowledge that the negotiations were not going well. On or about May 1, 1991, the company began actively considering an alternative means of raising capital — a stock offering dilutive to shareholders — but it continued that month to make public statements about its ongoing discussions with potential strategic partners and did not disclose its active consideration of the stock offering. The company ultimately announced a stock offering on June 6. 9 F.3d at 262, 266, 269. The Second Circuit stated that "when 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." *Id.* at 268.

As the Second Circuit has recognized, "*Time Warner* went nearly to the outer limit of the line that separates disclosable plans from plans that need not be disclosed." *San Leandro Emergency Med. Group Profit Sharing Plan* v. *Philip Morris Cos.*, 75 F.3d 801, 810 (2d Cir. 1996). And, as in *San Leandro*, this case plainly falls "on the safe side of the line." *Id.*

Plaintiffs try to analogize the Bank's consideration of invoking the MAC clause to the consideration of the stock offering in *Time Warner*, but they overlook at least two critical distinctions. ***First***, here, unlike *Time Warner*, the initial "intended approach" was never abandoned and the "other approach" was never adopted. The merger closed as originally planned on January 1, and no MAC was ever declared. The Bank, unlike Time Warner, is a regulated entity and did not believe it appropriate to act unilaterally. Plaintiffs' own allegations show that the Bank's management consulted with its regulators about the possibility of invoking the MAC clause, and determined not to do so when the regulators expressed strong objection. *See, e.g.*, AC ¶¶ 114-16. By contrast, Time Warner unilaterally changed its strategy for raising capital. 9 F.3d at 267-68.

The same is true in *Gulf Oil*. Gulf commenced a tender offer for Cities Service, but soured on the deal over a month before unilaterally terminating the offer. Judge Mukasey stated that "[w]hen 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." 725 F. Supp. at 748. Here, by contrast, there was no "sharp break" requiring disclosure: Plaintiffs do not allege the Bank ever ceased working toward the merger, the MAC clause was never invoked, and the merger was never abandoned.

Second, as the Complaint here acknowledges, any "active and serious consideration" of the possibility of declaring a MAC occurred within a *five-day* window — between Wednesday, December 17, the first meeting with regulators, and Sunday, December 21, when Lewis informed regulators the Bank would proceed with the merger. AC ¶¶ 114-28.[31] By contrast, the period of active consideration in *Time Warner* was over five weeks and in *Gulf Oil* more than six weeks. The speed with which the Bank ceased exploring the possibility of attempting to terminate the contract is highly significant in that it shows that here, unlike in *Gulf Oil*, there was no "sharp break" with the Bank's previously disclosed intention to go forward with the deal. As one court recently observed in distinguishing *Gulf Oil:*

> *Gulf Oil* does not . . . provide that every change in attitude must be disclosed. Instead, it provides for disclosure of "significant change[s] that constitute a sharp break from prior public positions." The emphasis is on a change in intention significant enough that a prior public statement, upon which investors might rely, is no longer accurate. . . .

DeCicco v. *United Rentals, Inc.*, 602 F. Supp. 2d 325, 345 (D. Conn. 2009). Here, as in *DeCicco,* the Complaint does not allege a "significant change constituting a sharp break from [the Bank's] prior public positions." *See also Evanowski* v. *BankWorcester Corp.,* 788 F. Supp. 611, 614 (D. Mass. 1991) (rejecting argument that bank that was party to merger agreement had duty to disclose renegotiation discussions; "The mere existence of renegotiation discussions does not mean that BankWorcester had stopped working towards completing the merger on its original terms.").[32]

Thus, *Time Warner* and *Gulf Oil* in no way support Plaintiffs' argument that the Bank had a duty to disclose its brief consideration of attempting to terminate the Merger Agreement.

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[31] Here, Plaintiffs' allegations of "active and serious consideration" relate to the period beginning December 17. *See* AC ¶¶ 114-26. Plaintiffs allege that Bank executives "discussed" the MAC clause on three occasions prior to the vote (*e.g.*, AC ¶ 101) but, as noted (*see* p. 30 & n.26, *supra*), that allegation is unsupported by Plaintiffs' "source." Moreover, Plaintiffs do not allege that the Bank made any decision, held any vote or contacted anyone at Merrill or its regulators as a result of those purported pre-vote discussions. The Complaint also refers to a conference call that Lewis supposedly had with the Bank's Board "no later than December 14" in which he said the Bank "might abandon the acquisition that was supposed to close in two weeks" (AC ¶ 113), but the "source" referred to in the Complaint — a February 5, 2009 *Wall Street Journal* article (Ex. 48) — does not support that allegation. Thus, the Complaint lacks any particularized facts that any contrary plan was under "active and serious consideration" prior to December 17.

[32] Plaintiffs' additional claims lack merit. The assertion that the merger was completed on different terms from those originally agreed to because it came to include federal assistance (*see* Opp. 73) does not save this flawed theory. Not only was no agreement with the government entered into until over two weeks after the merger closed, *see* BofA 1/16/09 8K, at Ex. 99.1 (Ex. 44), but no statement made during the period of discussions with regulators is alleged to have been rendered false or misleading by the omission of disclosures regarding such discussions. Plaintiffs' further argument that the description in the Proxy of the MAC clause somehow constituted a factual representation that was rendered false and misleading (Opp. 42, 46, 70-72) is also flawed. Both the Proxy and incorporated SEC filings were explicit that the terms of the Merger Agreement were not factual representations. *See* pp. 11-12, 29, *supra*; Mem. 14-15, 52-53.

Plaintiffs urge the Court to adopt a rule that would require parties to merger agreements to disclose their preliminary consideration of the possibility of seeking termination before any determination to do so has been made — a rule that would likely harm companies and their investors by requiring premature disclosure of strategic deliberations before any final determination is made. The SEC expressly rejected any such rule when, in 2004, it adopted a bright-line standard for contract-termination disclosures. Item 1.02(a) of Form 8-K (which took effect August 23, 2004) provides that an issuer must disclose when "a material definitive agreement . . . is ***terminated***, . . . and such termination . . . is material." *See* 17 C.F.R. § 249.308; Sec. Act Rel. No. 8400, Exch. Act Rel. No. 49,424, 2004 WL 536851, at *7-8 (Mar. 16, 2004). Instruction 1 to Item 1.02 makes clear that this rule means what it says: "***[n]o disclosure is required solely by reason of this Item 1.02 during negotiations or discussions*** regarding termination of a material definitive agreement ***unless and until the agreement has been terminated***." *See* Mem. 51-53 (quoting Form 8-K) (emphasis added).

Although *Time Warner* and *Gulf Oil* are not on point, it should also be noted that the law has changed considerably since these cases were decided. *Time Warner* and *Gulf Oil* pre-date not only the SEC's adoption of Item 1.02 of Form 8-K, but also Congress's enactment of the PSLRA, which altered the law as it relates to a "duty to update" forward-looking statements.[33] Under the PSLRA, forward-looking statements are statutorily protected, *see* 15 U.S.C. § 78u-5(c)(1), and no duty to update such statements exists. *See* 15 U.S.C. § 78u-5(d) ("Nothing in this section shall impose upon any person a duty to update a forward-looking statement.").[34] The PSLRA's elimination of the "duty to update" is in keeping with the text of Rule 10b-5 itself, which makes it

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[33] Statements concerning strategic objectives are routinely held to be forward-looking in nature. *See, e.g.*, *Grossman* v. *Novell, Inc.*, 120 F.3d 1112, 1121-22 (10th Cir. 1997) (statements relating to merger objectives and progress forward-looking); *see also San Leandro*, 75 F.3d at 809-10 (change in marketing strategy not actionable).

[34] *See also Eisenstadt* v. *Centel Corp.*, 113 F.3d 738, 746 (7th Cir. 1997) (Posner, J.) ("Even if it had made a public prediction of such a result, it would have had no legal duty, in this circuit anyway and perhaps in no circuit after [the PSLRA] to make a public revision of the prediction when it became clear that no such bonanza was in the offing."); *In re FoxHollow Techs. Sec. Litig.*, 2008 WL 2220600, at *17-18 (N.D. Cal. 2008) (post-PSLRA there is "no duty to update vague statements of optimism or expressions of opinion," "[n]or . . . any duty to update forward-looking statements"), *aff'd*, 2009 WL 4913215 (9th Cir. 2009); *In re CIGNA Corp. Sec. Litig.*, 2005 WL 3536212, at *4 (E.D. Pa. 2005) (post-PSLRA "law does not impose a duty to update forward-looking statements such as earnings estimates with all relevant material information and/or upon changes in business strategy").

unlawful "to make any untrue statement of a material fact or to omit 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) (emphasis added). Rule 10b-5 does not, on its face, require updating of statements that, though true when made, have become misleading. In any event, even the decisions stating that a duty to update "may exist" under Rule 10b-5, *see, e.g.*, *IBM*, 163 F.3d at 110, have held that "there is no duty to update vague statements of optimism or expressions of opinion." *Id.*[35] Here, the statements that the Bank is alleged to have made on September 15, and on December 5, regarding the anticipated benefits of the merger, are precisely the sort of vague statements of optimism that require no updating. *See* pp. 28-29, *supra*; Mem. 56-67. Moreover, the Bank's and Merrill's public filings with respect to the merger expressly disclaimed any duty to update. *See, e.g.*, BofA 9/15/08 8K, at Item 1.01 (Ex. 65); BofA 9/18/08 8K, at Item 1.01 (Ex. 66); Proxy at 22 (Ex. 1); BofA 3Q08 10Q, at 59 (Ex. 35); Merrill 3Q08 10Q, at 74 (Ex. 67).[36]

There are also no particularized allegations of scienter with respect to this claim. Plaintiffs' allegation that Secretary Paulson threatened to remove certain Defendants from their positions at the Bank if they sought to terminate the merger (*see* Opp. 87) does not give rise to a "strong inference" of scienter.[37] The alleged "threat" related only to what could happen if the Bank Defendants invoked the MAC clause — not if they disclosed that they were considering doing so. *See* Mem. 45 n.35. And Plaintiffs do not even attempt to grapple with the compelling inferences of nonfraudulent intent — to wit, that the Bank Defendants did not believe they were obligated to disclose their consideration of invoking the MAC clause or their preliminary discussions with the

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35 Although *IBM* was decided after the PSLRA went into effect, the case was decided under pre-PSLRA law, as it was filed in the district court years before the statute's date of enactment, December 22, 1995. The Second Circuit thus did not address the PSLRA's impact on the duty to update.

36 *Time Warner* and *Gulf Oil* were also decided before the Supreme Court's decisions in *Twombly*, *Iqbal* and *Tellabs*. *Time Warner* applied the now-overruled "no set of facts" pleading standard set forth in *Conley* v. *Gibson*, 355 U.S. 41, 45-46 (1957), and noted that its decision was "a close question" even under that lenient standard and the outer-limit facts at issue there. 9 F.3d at 263, 269.

37 In any event, "motives of compensation and job security — which are generally possessed by most corporate directors and officers — have been held not to be sufficient to give rise to an inference of fraudulent intent." *In re Centerline Holdings Co. Sec. Litig.*, 613 F. Supp. 2d 394, 401 (S.D.N.Y. 2009).

regulators, and that premature disclosure before a definitive understanding was reached would cause major harm to the Bank's shareholders and the financial system. *See* Mem. 55-56.

Furthermore, the Complaint alleges no particularized facts to support the contention that Defendants were deliberately disregarding a known obligation to disclose. *See* p. 22 & n.16, *supra*. To the contrary, the inference is compelling that matters had not reached a point where there was any "sharp break" from the plan to consummate the merger that could potentially (even on Plaintiffs' theory) call for disclosure. And still further undercutting any inference of scienter is the existence of an applicable SEC regulation (Item 1.02 of Form 8-K) with which Defendants clearly complied. *See Centerline*, 613 F. Supp. 2d at 403-04 ("existence of SEC regulations relating to the disclosure of the[] transaction[] and defendants' compliance with them" militates against scienter).

B. There was no actionable misrepresentation or omission regarding discussions with regulators and, in any event, no "strong inference" of scienter is pled.

"Bright-line" SEC rules, including 1.01 of Form 8-K and Instruction 2(b) thereto, requiring issuers to disclose "material definitive agreement[s]" only if there is an "agreement that provides for ***obligations that are material to and enforceable against*** . . . ***and enforceable by*** the registrant," also preclude Plaintiffs' argument that the Bank was required to disclose its discussions concerning an agreement with the Government to receive additional funding. *See* Mem. 53-54.

Plaintiffs argue the "bailout was firmly in place" on December 22, 2008. Opp. 74. But the Complaint alleges only a "verbal commitment" "to have a transaction . . . in existence no later than January 20, 2009." *See, e.g.*, AC ¶ 133. The Complaint does not allege an enforceable agreement was reached as of December 22, 2008. *See* Opp. 15; AC ¶ 135-36 (alleging non-specific "commitment" to provide "adequate and appropriate assets"). There is no allegation that any "material definitive agreement" was reached before January 16, 2009. *See* Mem. 54 & n.41.[38]

[38] *See also Adjustrite Sys.* v. *GAB Bus. Servs.*, 145 F.3d 543, 548, 550-51 (2d Cir. 1998) (no enforceable agreement where parties agreed to many terms but did not execute final agreement); *Ciaramella* v. *Reader's Digest Ass'n*, 131 F.3d 320, 326 (2d Cir. 1997) (preliminary agreement is not binding contract where magnitude and complexity of agreement reinforced stated intent of parties not to be bound until written contracts were signed); *Shann* v. *Dunk*, 84 F.3d 73, 77 (2d Cir. 1996) ("Ordinarily, preliminary manifestations of assent that require further negotiation and further contracts do not create binding obligations.").

Plaintiffs instead contend that "Defendants intentionally avoided committing . . . to a formal contract solely to avoid public disclosure." Opp. 74 (emphasis omitted). Plaintiffs cite no legal support for their claim that ***avoidance*** of a formal contract could somehow trigger a disclosure obligation that turns upon the ***existence*** of a "material definitive agreement." The standard advocated by Plaintiffs would be completely at odds with the "bright-line" rule the SEC has adopted.

The SEC considered adopting a rule requiring disclosure of "letters of intent and other non-binding agreements," but rejected it after "many commentators" expressed concern that such a rule "could cause significant competitive harm to the company and create excessive speculation in the market." *See* Exch. Act Rel. No. 49,424, 2004 WL 536851, at *7-8 (Mar. 16, 2004). Holding that a non-binding agreement triggers a disclosure obligation would thwart the intent of the SEC rule. *See Centerline*, 613 F. Supp. 2d at 402-03 (no duty to disclose impending sale of bond portfolio until definitive agreement executed).

And again, Plaintiffs fail to plead scienter with particularity. The suggestion that Bank executives deliberately forbore from entering into a formal contract with the Government to avoid public disclosure makes no sense given that a formal contract could have provided assurances that the Complaint indicates the Bank Defendants sought, and, in any event, disclosure would be required once a definitive agreement was reached. AC ¶¶ 134-36. A far more compelling inference is that no disclosure was made because it was not possible to reach agreement on all definitive terms over the holidays — much less to document them in an enforceable manner. As Plaintiffs admit, far from being memorialized in a single document, the parties' various views on the prospective terms were reflected in disparate emails and notes. *See* AC ¶¶ 116, 124, 128, 134. And once a definitive enforceable agreement was reached, the Bank promptly disclosed it (*see* BofA 1/16/09 8K (Ex. 44)), which further undercuts Plaintiffs' speculative and unsupported allegations of scienter.

C. There was no actionable misrepresentation or omission post-vote regarding fourth quarter interim results or forecasts and, in any event, no "strong inference" of scienter is pled.

Plaintiffs do not seriously dispute that there is no requirement that companies make mid-quarter disclosure of interim results or forecasts; financial results are reported after each quarter ends. *See* pp. 24-27, *supra*; Mem. 34-39, 48-49. Rather, Plaintiffs argue that after the vote, the

Bank had a "duty to update" to disclose Merrill's fourth quarter interim results or forecasts. *See* Opp. 70-72. The prior statements Plaintiffs argue supposedly trigger a duty to update did not discuss interim results or forecasts for the fourth quarter. *See* Opp. 71; Mem. 56-67. Rather, they were "vague statements of optimism or expressions of opinion" that did not trigger any duty to update. *IBM*, 163 F.3d at 109-10; *see* pp. 28-29, *supra.*

Finally, Plaintiffs' Rule 10b-5 claim requires particularized pleading of facts giving rise to a "strong inference" of scienter. Mem. 25-26, 50. Plaintiffs do not come to grips with the reality that, by waiting to disclose earnings until after the conclusion of the fourth quarter, the Bank Defendants acted in accordance with the quarterly reporting regime established by law. *See* Mem. 33-39, 48-49. Indeed, the fourth quarter results here were announced on January 16, 2009 (BofA 1/16/09 8K (Ex. 44)) — some six weeks before the deadlines for filing the Bank's and Merrill's 10-Ks (*see* Form 10-K, Instruction A(2)(a), 17 C.F.R. § 249.310 (requiring 10-K filings "60 days after the end of the fiscal year")) — a fact the Second Circuit has held militates against any inference of scienter. *See Rombach*, 355 F.3d at 176-77. There is no claim here that any Bank Defendant engaged in insider trading ahead of the January 16 announcement, and the purported motives Plaintiffs cite for the alleged delay of that announcement (*i.e.*, to avoid calling into question statements Defendants made as to benefits of the merger or their judgment and competency), *see* Opp. 87, do not give rise to the strong inference of scienter required to overcome the obvious non-culpable inference that the Bank Defendants simply acted in accordance with standard disclosure practices. *See* pp. 24-28, *supra*; Mem. 55-56.

CONCLUSION

For the foregoing reasons, as well as those set forth in the Bank Defendants' Memorandum, the Complaint should be dismissed with prejudice.

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