UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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

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

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I. Preliminary Statement

The issue on this motion is whether Defendants Kenneth E. Lewis and Joe L. Price engaged in "highly unreasonable conduct representing an extreme departure from the standards of ordinary care" by concealing Merrill Lynch & Co., Inc.'s ("Merrill") "historically large" fourth quarter 2008 losses, and failing to disclose until after the merger closed the $138 billion taxpayer bailout necessitated by Merrill's losses. *In re Bank of America Corp. Sec., Deriv. & ERISA Litig.*, No. 09 MD 2058 (PKC), 2010 WL 3448194, at *33, 56 (S.D.N.Y. Aug. 27, 2010) (internal quotation marks omitted) (the "August 27 Opinion"). The Second Amended Complaint ("SAC") sufficiently alleges that they did. Based on internal documents and sworn testimony of Bank of America Corp.'s ("BoA" or the "Company") senior executives and counsel, among others, the SAC alleges extraordinary new facts demonstrating that Lewis and Price (i) recognized that their concealment of Merrill's "terrible" losses defrauded the market, which they knew expected Merrill to report a profit (¶¶104, 107, 166-72);[1] (ii) internally acknowledged that their concealment of the taxpayer bailout similarly defrauded a market that believed that BoA was superior to its competitors precisely because it did not need government assistance (¶¶166-72); (iii) defied the advice of their counsel and other senior executives to disclose Merrill's losses (¶¶103-17); (iv) lied to their in-house General Counsel, Timothy Mayopoulos, to ensure that no such disclosure was made (¶¶113-14, 124-27); and (v) summarily terminated Mayopoulos when he questioned their decision to conceal the losses (¶¶139-42).

As alleged in the SAC, Lewis and Price knew that investors held a view of Merrill that was fundamentally at odds with the undisclosed truth. Specifically, Lewis and Price knew that the market expected Merrill to report a substantial profit and did "not have an inkling" that Merrill was "deep in the red." ¶¶104, 107, 166-72. As Lewis and Price also knew, this disparity – which BoA's own Treasurer described as what "we know relative to what they know" – caused Mayopoulos and BoA's

[1] All citations to "¶__" are to the SAC. All emphasis is added unless otherwise noted.

outside counsel, Wachtell, Lipton, Rosen & Katz ("Wachtell"), to advise BoA that it had to disclose Merrill's $7.5 billion October loss a week before the shareholder vote on the merger. ¶¶104-09, 167. For the same reason, Jeff Brown, BoA's Treasurer, issued a striking admonition to Defendant Price that the failure to disclose Merrill's losses could leave them talking "through a glass wall over a telephone." ¶¶121-22. Rather than heed this advice, as Merrill's losses continued to spiral out of control, Lewis and Price took a series of extraordinary steps to ensure that no disclosure was made, and that the merger was approved and consummated.

For instance, after Mayopoulos and Wachtell "all agree[d]" that BoA "must" disclose Merrill's "terrible" $7.5 billion October loss before the shareholder vote, Price pressured Mayopoulos to unilaterally reverse that decision because, as recorded in Mayopoulos's notes, he knew that disclosure would result in a "neg." shareholder vote. ¶¶104-09, 113-17. Then, even as the fourth quarter losses more than doubled in the weeks leading up to the vote, bringing Merrill to the brink of insolvency, Price repeatedly deceived Mayopoulos by deliberately understating the true extent of Merrill's losses by billions of dollars. ¶¶113-14, 124-27. Through this deception, Lewis and Price ensured that Mayopoulos would not again advise disclosure of Merrill's crippling losses, and that BoA's shareholders, oblivious to Merrill's true financial condition, would vote overwhelmingly to approve the merger. Two business days after the shareholder vote, when Mayopoulos finally learned in a BoA Board meeting the true severity of Merrill's losses and sought to confront Price, BoA immediately terminated Mayopoulos, escorted him from the premises, and replaced him as General Counsel with someone who had not practiced law in 15 years, in the midst of the largest merger in BoA's history. ¶¶139-42.

After removing this obstacle to their plan for continued nondisclosure, Lewis and Price secretly contacted Secretary of the Treasury Henry Paulson and demanded a $138 billion taxpayer bailout to complete the deal, stating falsely that Merrill's massive losses – almost all of which they knew were

incurred before the vote – had only recently accelerated, and now gave BoA grounds to invoke the "material adverse effect" clause ("MAC") of the merger agreement. ¶¶143-45. At the same time that Lewis and Price were obtaining the taxpayer bailout, they and their counsel were internally acknowledging in a series of stunning emails that their concealment of Merrill's losses and the bailout was defrauding the market – the very crux of Lead Plaintiffs' fraud claim. As Lewis and Price knew, the market had been led to believe that Merrill was "more healthy than they are," and that BoA was in better financial condition than its competitors precisely because it did not "need government assistance." ¶¶166-72. As reflected in contemporaneous notes taken by Wachtell, on December 19, 2008, or twelve days before the merger closed, BoA's most senior officers internally acknowledged that their failure to disclose Merrill's losses and the bailout had created a "fundamental issue of lack of credibility" with investors, who "don't know what is coming." ¶¶170-72. These same notes further establish that BoA's most senior officers knew that if the losses and bailout were disclosed prior to the merger's close, it would cause the deal to "f[a]ll apart" and "confirm [the] materiality of the fourth quarter losses." *Id.* Thus, Lewis and Price decided to conceal this highly material information for more than three weeks in order to ensure that the merger was consummated. ¶¶154-55, 171-72.

It is rare to have such highly specific facts establishing conscious misbehavior at the pleading stage. These facts establish that Lewis and Price not only knew about Merrill's historic losses as they were occurring, but also knew that that their failure to disclose them had affirmatively misled the market. Nothing more is required to plead, or even prove, their scienter. Yet, in their motion to dismiss the SAC, Lewis and Price fail to confront any of these new facts. Instead, they make a series of untenable arguments that fundamentally misconstrue the SAC, ignore this Court's prior rulings, and require the Court to resolve factual disputes and draw inferences in their favor. For example, Lewis and Price contend that they believed that BoA's and Merrill's risk disclosures sufficiently informed investors of Merrill's financial condition. *See* Bank Defendants' Mem. Of Law In Support Of Their

Motion To Dismiss Claims, And New Plaintiff Classes, Asserted In The Consolidated Second Amended Class Action Complaint ("Def. Mem.") at 15-16. However, the SAC specifically alleges that Lewis and Price knew that these risk disclosures were meaningless, as they understood that their statements had led the market to expect Merrill to report a profit, and that investors had "no inkling" that Merrill's historic losses "were coming." ¶¶82, 83, 85-86, 94, 107, 166-72. Indeed, Mayopoulos, Wachtell, and Brown all recommended disclosure of Merrill's losses precisely because they recognized that these boilerplate risk disclosures – which remained unchanged from risk disclosures in SEC filings in previous quarters – did not warn investors of Merrill's historic losses. Even setting these facts aside, the Second Circuit has discredited this exact argument, holding that it raises "serious concerns" and underscoring that "we have never held that [risk] disclosures may, as a matter of law, negate allegations of fraudulent intent." *Press v. Quick & Reilly, Inc.*, 218 F.3d 121, 130 (2d Cir. 2000) (Sotomayor, J.).

Lewis and Price also argue that Price's "consultations" with counsel negate any inference of scienter. *See* Def. Mem. at 25, 27-28. This argument cannot be credited, given the SAC's allegations that Price repeatedly lied to both Mayopoulos and Wachtell about the extent of Merrill's losses, and that BoA terminated Mayopoulos when he sought to confront Price about this deception. ¶¶113-14, 124-27, 139-42. Indeed, Mayopoulos testified to Congress that he never received complete and accurate information regarding Merrill's losses. ¶127. Given this testimony, it is inconceivable that Lewis and Price can establish the fact-intensive reliance-on-counsel defense at any stage of the proceedings, much less on this Rule 12(b)(6) motion.

The Bank Defendants[2] also attempt to refute the cogent and compelling inference of scienter by arguing that all they had were unreliable "estimates" and "forecasts" of Merrill's losses. *See* Def. Mem. at 7, 10. However, their conduct and emails show that Lewis and Price knew that the loss reports were reliable, and unequivocally showed that Merrill was suffering "terrible" losses. *See, e.g.*, ¶¶101-

[2] The "Bank Defendants" are BoA, Lewis, Price, Neil A. Cotty, the members of the BoA Board, and Banc of America Securities, LLC, as set forth in n.1 of the Bank Defendants' brief.

10. Significantly, when Lewis and Price went to the highest levels of the Government to request <u>over one hundred billion dollars</u> in taxpayer aid in mid-December, they provided the same "intra-quarter" loss reports cited in the SAC to the country's most senior banking regulators as <u>proof</u> of Merrill's fourth quarter losses, and reliable evidence of BoA's resulting need for public funds. ¶146. If these loss reports were definite and firm enough to provide to the Government as justification for the $138 billion taxpayer bailout, they were certainly reliable enough to provide the justification for a disclosure to investors in BoA's securities.

Lewis and Price additionally contend that they had no motive to conceal Merrill's losses or the bailout because the SAC supposedly alleges that they wanted to terminate the transaction by invoking the MAC. *See* Def. Mem. at 16, 18, 19, 43. However, the SAC does <u>not</u> allege that Lewis and Price wanted to terminate the merger. To the contrary, the SAC alleges that Lewis was, in his own words, "drooling" over the prospect of obtaining Merrill. ¶63. While the law is clear in the Second Circuit that no allegations of motive are necessary (*see Ganino v. Citizens Utils.*, 228 F.3d 154, 169 (2d Cir. 2000)), the SAC alleges that Lewis and Price were determined to complete the merger at any cost – including by concealing highly material information from the investing public. ¶¶63, 154-55, 171-72.

Finally, Lewis and Price seek to reargue the Court's decision that there was a duty to disclose Merrill's losses under Section 10(b). *See* Def. Mem. at 34-41. This argument ignores this Court's exhaustive August 27 Opinion and longstanding Second Circuit authority. *See Bank of America Corp.*, 2010 WL 3448194, at *34, 43. As the Court recognized in soundly rejecting this argument the first time around, the Second Circuit has repeatedly held that a material omission in a proxy may be simultaneously actionable under both Section 14(a) and Section 10(b). *Id.*; *see also Wilson v. Great Am. Indus., Inc.*, 855 F.2d 987, 991 (2d Cir. 1988). Defendants have not cited a case to the contrary.

In sum, the SAC adequately alleges that Lewis and Price, and therefore BoA, acted with scienter in failing to disclose Merrill's losses and the taxpayer bailout. Accordingly, the Court should

deny Defendants' motions to dismiss the SAC.

II. Factual Background

A. Lewis And Price Knew They Were Defrauding Investors By Failing To Disclose Merrill's Losses

Lewis, Price, and BoA principally argue that the risk warnings contained in BoA's and Merrill's SEC filings about "turbulent market conditions" belie any contention that they acted with scienter in failing to disclose Merrill's historic fourth quarter losses. Def. Mem. at 15. This assertion is at odds with the SAC, which shows that these Defendants knew that these purported risk disclosures did not adequately inform the market of Merrill's historic losses or true financial condition. Indeed, Defendants' internal notes and emails show that Lewis and Price contemporaneously knew that the market was expecting Merrill to report a substantial profit for the fourth quarter, and that investors did "not have an inkling" that Merrill was "deep in the red." ¶¶15, 86, 94, 107. Moreover, BoA's internal emails, Wachtell's notes, and the sworn testimony of BoA's senior officers show that, during the fourth quarter, Lewis and Price were acknowledging internally that their failure to disclose Merrill's losses had misled investors and resulted in a "fundamental issue of lack of credibility" with the market. ¶171.

Specifically, on November 13, just ten days after the Proxy was issued, Mayopoulos met with senior Wachtell partners to discuss whether BoA had a duty to disclose Merrill's "terrible" losses. ¶¶104-09, 166. The contemporaneous handwritten notes of senior Wachtell partner Eric Roth show that, at this meeting, the lawyers discussed that analysts' consensus expectations were for Merrill to report a substantial profit for the fourth quarter, but that, in reality, Merrill would be "deep in the red." ¶107. In fact, in conjunction with this meeting, an internal summary of analysts' expectations for Merrill's fourth quarter was prepared, which showed that the vast majority of analysts expected Merrill to report a healthy profit after supposedly having undergone a "clean-up prior to its year-end merger with Bank of America." *Id.* It was at this November 13 meeting – and after the lawyers had acknowledged that the market had no idea that Merrill was experiencing such "terrible" October losses

– that both Wachtell and Mayopoulos decided that BoA needed to make a supplemental disclosure regarding Merrill's losses prior to the shareholder vote on the merger, and even went so far as to advise BoA of the date by which such a disclosure had to be made. ¶¶108-09.

BoA's lawyers were not the only ones who recognized that Lewis and Price were defrauding the market by not disclosing Merrill's losses. For example, BoA's Treasurer, Jeff Brown, who reported directly to Price, was so concerned about that deception that he told Price that BoA should disclose Merrill's losses to investors before the shareholder vote. ¶122. When Price refused to do so, Brown warned Price that he "didn't want to be talking through a glass wall over a telephone" if BoA did not disclose the losses – a remarkable admonition from a senior corporate officer. *Id.* Similarly, in late November, Merrill's auditor, Deloitte & Touche, informed Merrill that the losses were "material subsequent events to what occurred at the end of September that would be relevant for parties that were voting on [the merger]" and "sizable enough [to] probably warrant disclosure." ¶123.

Then, in a series of stunning emails among BoA's lawyers and senior officers that were exchanged two weeks before the merger closed, BoA internally acknowledged that the failure to disclose Merrill's losses (and the taxpayer bailout) was affirmatively misleading investors – and that disclosure of such facts would inevitably cause the deal to "f[a]ll apart" and "confirm materiality of the fourth quarter losses." ¶¶167-71.

On December 17, Brown emailed Price following a conversation between Brown and Standard & Poor's ("S&P"). In that email, Brown warned Price that he was "concerned" because S&P was "not expecting poor results from ML this quarter," and S&P had in fact noted "substantial improvements in ML risk/balance sheet management." ¶167. As Brown further told Price, "in light of ML's 4Q performance that we know relative to what they know," S&P "clearly think[s] ML is more healthy than they are" because "they have shed the worst risks." *Id.* Brown also told Price that S&P was differentiating BoA from its competitors precisely because BoA did not "need government assistance."

¶168. Brown's unequivocal email should have served as a clarion call for Price – a powerful warning from one of the Company's most senior officers that the market and BoA's shareholders did not know the truth about Merrill's financial condition. Yet, Price ignored Brown's entreaties.

Accordingly, two days later, on December 19, Brown took his concerns directly to BoA's in-house counsel. ¶170. That day, Brown forwarded an email he had received from a member of his department regarding a conversation between that employee and Moody's, in which Moody's spoke positively about the merger and made clear that Moody's also had no idea of Merrill's dire situation. In his email, Brown stated: "Moody's comment on the deal – <u>again another sign agencies don't know what is coming</u>." *Id.*

In response, in-house disclosure counsel arranged a meeting with Brown and Wachtell that took place on December 19, 2008.[3] ¶171. Senior Wachtell partner Peter Hein's notes of that meeting show that, at the time that BoA's most senior executive officers decided not to disclose Merrill's losses or the bailout, they knew that (i) this information was highly material to investors; (ii) the market had no idea that Merrill had suffered massive losses in the fourth quarter; (iii) disclosure of these material facts before the merger closed would cause rating agency downgrades and result in the deal falling apart; and (iv) BoA was misleading the market by not disclosing these facts. ¶172. Specifically, Hein's notes demonstrate that concealment of these facts had resulted in a "<u>fundamental issue of lack of credibility</u>" with the market, and that any "belated" disclosure of this information would have an "<u>adverse impact on perception of rating agencies (who do not have an inkling this is coming)</u>," cause the deal to "f[a]ll apart" and "<u>confirm [the] materiality of the fourth quarter losses</u>." ¶171.[4] No disclosure of Merrill's

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[3] Defendants' attempt to downplay the significance of these warnings by dismissing Brown as a "non-lawyer" (Def. Mem. at 33 n.57) should be rejected. Brown was BoA's Treasurer and one of the Company's most senior officers, and his emails clearly put Price on notice that the market was being misled by the continued concealment of Merrill's losses.

[4] The Bank Defendants contend that the phrase "f[a]ll apart" in Hein's notes refers to "what might happen if a MAC were declared," and not to what would happen if Merrill's losses were disclosed. Def. Mem. at 45. This contention fails, as it raises fact issues that cannot be resolved on this motion and contradicts the notes themselves, which make clear that BoA's senior officers recognized that the merger would "f[a]ll apart" if Merrill's losses were "disclosed … belatedly" to a market

losses or the $138 billion bailout was made prior to the close of the merger.

Tellingly, in their brief, Lewis, Price, and BoA have failed to address any of these emails. Their failure to do so speaks volumes.

B. BoA's Senior Officers Recognize That Merrill's Staggering Losses Should Be Disclosed In Advance Of The Shareholder Vote

Lewis and Price not only knew that Merrill's catastrophic losses contradicted the expectations they had cultivated in the market, but also knew that they were required to disclose this information before the shareholder vote. As an initial matter, the Court has found that Defendants Lewis and Price knew of Merrill's losses as they occurred and, in particular, that they knew of, or recklessly disregarded, Merrill's massive October 2008 losses as of the filing of the Proxy on November 3, 2008. *Bank of America Corp.*, 2010 WL 3448194, at *33.

Immediately after the merger was announced, BoA placed 200 people at Merrill to continuously monitor Merrill's financial condition, and installed Neil Cotty, BoA's Chief Accounting Officer, as Merrill's interim CFO. ¶95. Cotty acted as a direct liaison between Merrill and Lewis and Price. *Id.* According to John Thain, Merrill's CEO, Cotty participated in regular meetings and discussions concerning Merrill's financial results and "was totally up-to-speed on what was happening" throughout the fourth quarter. ¶96. Similarly, Thain stated that BoA's senior executives personally received regular updates as the fourth quarter progressed and, in fact, "were getting [our] daily profit and loss statement" and had full knowledge of Merrill's losses "step-by-step" during the fourth quarter. ¶97. Lewis admitted to Congress that he received "detailed financial reports" regarding Merrill "every week." ¶¶99-100. As the Court held, these allegations establish that, "By the time the Joint Proxy issued, the stormy forecast for the fourth quarter was not merely a projection: the storm had arrived. <u>These losses were a known fact to company insiders, yet were not disclosed to BofA's shareholders</u>."

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that had been led to believe Merrill was healthy. ¶171. Further, the entire purpose of the December 19 meeting reflected in these notes was to discuss Brown's "concerns" over BoA's misleading statements, and not the MAC. ¶¶166-72.

Bank of America Corp., 2010 WL 3448194, at *33.

Moreover, while the Bank Defendants initially argued that Merrill's massive losses did not arise until after the December 5 shareholder vote (¶145), their internal documents establish that these losses occurred contemporaneously with the Proxy's issuance, and that Lewis and Price immediately recognized how devastating Merrill's losses were. For example, on November 5, 2008, a month before the vote was scheduled to take place, Cotty emailed Price concerning Merrill's October results with the striking notation: "Read and weep."[5] ¶101. Similarly, Merrill's Corporate Controller acknowledged how poor Merrill's results were in an email to Cotty, telling him that the "[n]umbers speak for themselves." *Id.* Recognizing that BoA could be required to disclose Merrill's massive, unexpected losses in advance of the merger, Price contacted Mayopoulos on November 12 to "ask the disclosure question." ¶¶102-03. Informed that BoA expected Merrill's fourth quarter loss to be approximately $8.9 billion pre-tax, or $5 billion after-tax, Mayopoulos told Price that "a disclosure was likely warranted" because "$5 billion is a lot of money." ¶103.

Wachtell agreed that BoA had to disclose Merrill's "terrible October" losses. ¶¶108-09. Specifically, after meeting with Price on November 12, Mayopoulos discussed Merrill's losses and BoA's disclosure obligations with Wachtell. ¶104. Wachtell's research on this issue concluded that BoA had a "duty to bring to sh[areholders] all info[rmation] material to vote" "@ time of vote under federal proxy" law.[6] ¶105. The following day, Mayopoulos and other BoA in-house counsel met with

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[5] Notwithstanding the Court's holding that Defendants were aware of Merrill's losses when the Proxy was issued, Lewis, Price, and BoA contend that the SAC alleges that they "first received information about [Merrill's] October results on November 5, two days after the Proxy was filed." Def. Mem. at 22-23. This is contrary to the SAC and the Court's decision. As the Court recognized, the SAC alleges that the Bank Defendants were aware of Merrill's losses as they occurred, and these losses were reflected in the daily P&L reports they were receiving. Nothing in the November 5, 2008 email that Price received – which only makes clear that Defendants immediately understood how devastating Merrill's October losses were – supports the Bank Defendants' contention that they were previously unaware that Merrill was suffering terrible losses in October. Moreover, regardless of whether Defendants knew that Merrill's October losses were $6.1 billion or $7.5 billion (as they ultimately turned out to be) when the Proxy was issued, they knew that Merrill had suffered disastrous losses in October, but did not disclose that fact to shareholders in the Proxy.

[6] The Bank Defendants attempt to dismiss this memo as "over nine years old." Def. Mem. at 27 n.48. However, this memo constituted the only research that Roth or anyone at Wachtell reviewed in concluding that disclosure was required. Presumably, if Wachtell believed that the research required updating, the firm would have conducted additional research on

senior Wachtell partners and unanimously agreed that there "must be some discl[osure]" of Merrill's losses by November 28, 2008 – a week before the shareholder vote – and informed Price of their conclusion. ¶¶106, 108-09, 264. This conclusion was driven, in part, by the recognition that Merrill's October losses, which placed it "deep in the red," stood in stark contrast to analysts' expectations that Merrill would report a profit for the fourth quarter. ¶107. In addition, Mayopoulos's and Wachtell's joint determination that BoA was required to disclose Merrill's losses reflected their recognition that the risk disclosures in the Proxy and other materials did not already adequately inform investors of Merrill's true condition. Although Price agreed to inform Thain of counsel's advice to disclose Merrill's losses, when Price met with Thain on November 14, 2008, Price did not do so. ¶111.

By the time he met with Thain on November 14, Price already knew that Merrill's fourth quarter pre-tax loss had grown to approximately $11 billion, including a $2 billion goodwill writedown that Price had been informed about the previous day. ¶110. That writedown was driven primarily by the failure of Merrill's 2006 acquisition of First Franklin Financial Corporation, a sub-prime loan originator. ¶93. Within two days of meeting with Thain, Price knew that Merrill's losses had grown even larger – to at least $13 billion pre-tax, $8.5 billion after tax.[7] ¶112.

C. Price Misleads Counsel To Prevent Disclosure Of Merrill's Losses

Faced with an increase in Merrill's losses from $8.9 billion to $13 billion in the four days since in-house and outside counsel had advised disclosure, Price set out to convince in-house counsel to withdraw that advice so that the objective of obtaining the "long coveted" Merrill would not be frustrated. On November 18, 2008, Price went back to Mayopoulos to discuss the risk that disclosing

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the issue. The Bank Defendants also wrongly contend that the SAC fails to allege that the "substance" of this memo "was shared with anyone at the Bank." *Id.* To the contrary, the substance of this memo was the basis on which Wachtell informed Mayopoulos and Price that BoA was required to disclose Merrill's losses. ¶¶104-09.

[7] Incredibly, Lewis, Price, and BoA contend that this allegation is misleading because the November 16 email upon which it is based states that "Cotty has a pretax loss of $10.942 billion," and not that Merrill "had a pretax loss of $10.942 billion." Def. Mem. at 8. Cotty was Merrill's interim CFO, received daily updates on Merrill's losses, and was "totally up-to-speed" on Merrill's fourth quarter losses. ¶¶95-97. Obviously, Cotty was the senior officer at Merrill responsible for determining Merrill's losses, and the fact that Price referred to Cotty's calculations shows that he had confidence in his numbers. ¶112.

Merrill's losses would likely cause shareholders to reject the merger. ¶113. As the top of Mayopoulos's notes of that meeting reflect – underlined for emphasis – he and Price discussed "What happens if neg. shh vote?" *Id.* While Price impressed upon Mayopoulos the consequences of disclosing Merrill's losses, he concealed from Mayopoulos that Merrill's mounting quarterly pre-tax losses now totaled $13 billion ($8.5 billion after-tax).[8] *Id.*

Two days later, Price and Mayopoulos informed Wachtell that BoA would not disclose Merrill's losses. ¶¶114-15. In explaining that decision to Wachtell, Mayopoulos – still unaware that Merrill's after-tax losses had reached $8.5 billion – now took the position that Merrill's losses were not material because the $5 billion after-tax loss of which he and Wachtell had been informed was within the range of quarterly losses that Merrill had incurred over the previous five quarters ($2 billion to $9.8 billion after-tax per quarter). *Id.* As Mayopoulos later testified, he conducted no legal research (nor did any other BoA lawyer) in concocting his novel "materiality" analysis. ¶116. Moreover, neither Mayopoulos nor Price asked Wachtell to opine on BoA's changed position concerning disclosure. ¶¶116-17. Price, who attended the meeting with Wachtell and knew that Mayopoulos based his rationale for non-disclosure on a materially incorrect understanding of the extent of Merrill's losses, again did not inform either Mayopoulos or Wachtell that those losses now totaled at least $13 billion pre-tax, or $8.5 billion after taxes.[9] ¶115.

[8] While the Bank Defendants concede that Mayopoulos's notes of his meeting with Price prominently ask "What happens if neg. shh. vote?" (emphasis in original), they make the inappropriate (and implausible) factual argument that this only meant that Mayopoulos was curious to know what the merger agreement provided for in the event shareholders voted against the merger. Def. Mem. at 21 n.37. Of course, even if the Court were to credit this factual interpretation – which it should not – the Bank Defendants fail to explain what aroused Mayopoulos's curiosity at this point in time. As Mayopoulos testified, he was curious because he knew that shareholders would likely vote the merger down if they were advised of Merrill's massive losses. ¶113.

[9] The supposition that the Wachtell lawyers on this call should have spoken up if they disagreed with Price's and Mayopoulos's conclusion must be rejected. Def. Mem. at 27-28. Wachtell had already informed BoA that disclosure was required, and was not being asked to opine on BoA's unilateral rejection of this advice. ¶117. Thus, it is hardly surprising that Wachtell would not offer any unsolicited comment on this issue. At best, the Bank Defendants' contention raises a fact issue that is incapable of resolution on a motion to dismiss.

D. Prior To The Shareholder Vote, Merrill's Losses Escalate So Substantially That BoA Considers Whether It Has Grounds To Invoke The MAC

The continued escalation of Merrill's losses in November prompted BoA to consider whether it had grounds to argue that a MAC had occurred. ¶118. Reflecting how material these losses were to the terms of the deal, that debate continued until just days before the shareholder vote. *Id.* For example, on December 1, 2008, Price, Mayopoulos, and Greg Curl (BoA's Vice Chairman of Corporate Development) met to discuss whether BoA had grounds to terminate the merger pursuant to the MAC. ¶119. Although Price knew that Merrill's losses were far greater than Mayopoulos had been told, he continued to conceal that fact from Mayopoulos. Indeed, an email sent to Price later that day calculated Merrill's losses for October and November, including the goodwill writedown, at approximately $15 billion pre-tax, or almost $10 billion after tax, with an additional $1 billion loss expected in December 2008 – facts that Price withheld from Mayopoulos.[10] ¶120. Mayopoulos, still under the false impression that Merrill's fourth quarter after-tax losses were expected to be only $5 billion, advised Price and Curl that BoA did not have grounds to invoke the MAC. ¶119.

On December 3, 2008 – two days before the shareholder vote – Lewis, Price, Cotty, and Thain met to discuss Merrill's staggering fourth quarter losses. ¶124. At that meeting, Lewis and Price specifically revised Merrill's loss report to include an additional $2 billion of losses for November. *Id.* The revised loss report set Merrill's November losses at $4.9 billion, and total fourth quarter losses in excess of $14 billion pre-tax, or approximately $9 billion after taxes. ¶125. However, as Lewis and Price knew, and as the first page of the loss report emphasized, this stated loss figure did not include the "goodwill writeoff" Merrill had been forced to take. ¶126. With that $2.2 billion goodwill writedown for Merrill's subprime lending arm included, Merrill's expected fourth quarter losses were now more

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[10] The contention that Lewis and Price did not know on December 1 that Merrill's October and November losses now totaled approximately $15 billion makes no sense, and in any event raises an issue of fact. Def. Mem. at 9-10. Indeed, Lewis, Price, and BoA concede that an email from Cotty to Price on that date indicates that Merrill's losses for October and November were then believed to be $12.7 billion, not including the $2.2 billion goodwill writedown BoA knew Merrill had decided to take two weeks earlier. Def. Mem. at 9.

than $16.2 billion pre-tax, and more than $10.5 billion after-tax. *Id.* Thus, by Lewis's and Price's own admission, Merrill's fourth quarter losses now exceeded by at least $700 million even the arbitrary $9.8 billion after-tax loss threshold that Mayopoulos had set for disclosure during the November 20 meeting with Price and Wachtell. ¶126.

Accordingly, Lewis and Price understood that if Mayopoulos learned of Merrill's true financial condition, he would again – under his own rationale – be forced to advise disclosure, thus eliminating any pretense that BoA had a legal basis to continue concealing Merrill's losses from BoA shareholders and investors. Therefore, when Price met with Mayopoulos (about an unrelated topic) on December 3 after the meeting with Lewis, Cotty, and Thain, Price continued to mislead Mayopoulos as to the magnitude of Merrill's losses. ¶127. Specifically, as Mayopoulos has repeatedly testified, including to the U.S. Congress, Price informed Mayopoulos that the $5 billion after-tax forecast for Merrill's losses had only been revised upward to "$7 billion after taxes" – or $3.5 billion less than Price knew the losses to be, and well below Mayopoulos's arbitrary threshold.[11] *Id.*

E. BoA Terminates Its General Counsel To Prevent Disclosure Of Merrill's Losses Before The Merger Closed

On December 5, 2008, oblivious to Merrill's losses, BoA shareholders voted to approve the merger. On December 9, two business days after the shareholder vote, Lewis and Price met with the BoA Board concerning Merrill's fourth quarter losses. ¶139. Mayopoulos was present at that meeting. Price presented to the Board the $14 billion pre-tax loss figure ($9 billion after taxes) that Lewis, Price, Thain and Cotty had discussed on December 3 and that was contained in the revised December 3 loss report. *Id.* That presentation excluded the $2.2 billion goodwill writedown, which would have brought Merrill's total pre-tax loss to $16.2 billion and $10.5 billion after-tax. *Id.* Mayopoulos later testified

[11] The Bank Defendants contend that Mayopoulos could not recall what time on December 3 he spoke with Price, and thus Mayopoulos's testimony cannot establish that Price had received the revised loss report before meeting with Mayopoulos. *See* Def. Mem. at 33 n.56. However, the SAC specifically alleges that Price met with Mayopoulos after receiving the revised loss report. ¶127. This allegation is based directly on Price's sworn testimony to the New York Attorney General.

that he was "surprised" by the size of the loss, and sought to confront Price after the meeting to ask him "what's changed; why it's changed; [and] what does it mean with respect to whether we should make a disclosure or not." ¶140. Mayopoulos was denied an audience with Price that day, and determined to meet with Price the next day. *Id.*

The next morning – before Mayopoulos could speak to Price – BoA summarily terminated Mayopoulos without explanation and immediately escorted him from the premises without even the opportunity to collect his belongings. ¶¶141-42. Prior to his abrupt termination, Mayopoulos had served as BoA's General Counsel for five years, and had been told by Lewis that he would be the General Counsel of the combined company.[12] ¶141. Even as BoA executives worked frantically to close one of the largest mergers in Wall Street history, BoA replaced Mayopoulos as General Counsel with Brian Moynihan, who had not practiced law in 15 years, did not have an active license to practice law, and was transferred to a non-legal executive position weeks after the merger closed. ¶141.

F. Lewis And Price Secretly Obtain A Massive Taxpayer Bailout

Although Lewis, Price, and BoA argue that the SAC alleges that they wanted to terminate the merger after the shareholder vote (*see* Def. Mem. at 43), this argument constitutes a fundamental misreading of the SAC. The SAC alleges that Lewis and Price wanted to complete the merger at all costs – including at the cost of not disclosing to shareholders information that this Court has already held was highly material and required to be disclosed before the vote occurred. Indeed, within days of

[12] Lewis, Price, and BoA contend that the "SAC pleads no facts connecting [Mayopoulos's] termination to his disclosure advice" because the SAC does not allege that (i) Price was aware that Mayopoulos wanted to speak with him; (ii) Mayopoulos expressed his disclosure concerns to anyone; or (iii) Price had any involvement in Mayopoulos's termination. Def. Mem. at 34. This argument fails. Price was aware that Mayopoulos was at the December 9 Board meeting during which Price informed the BoA Board of losses that were materially higher than those he had presented to Mayopoulos just days earlier. Immediately after the meeting, Mayopoulos attempted to speak with Price but was told he was unavailable for the day. ¶140. It is not plausible that no one told Price – the Bank's CFO – that Mayopoulos – the Bank's General Counsel – wanted to speak with him, especially when the request came right after this critical Board meeting. Moreover, the notion that Price was not involved in Mayopoulos's immediate termination, weeks before the close of the largest merger in BoA's history, when they had been working closely together on it for months, is similarly implausible. In addition, the Bank Defendants' contention that Judge Rakoff "soundly rejected the allegation that Mayopoulos's termination had anything to do with his Merger-related advice" is sheer fiction. In fact, Judge Rakoff – who did not purport to resolve this issue – found that "plausible" contrary inferences of scienter could be drawn connecting Mayopoulos's termination with his disclosure advice. *SEC v. Bank of America Corp.*, No. 09 Civ. 6829 (JSR), 2010 WL 624581, at *3 (S.D.N.Y. Feb. 22, 2010).

the vote, Lewis and Price acknowledged, based principally on the same information that was available to them before the vote, that Merrill's losses were so significant that BoA likely had grounds to invoke the MAC, and immediately sought government assistance in order to ensure that the transaction closed – without disclosing any of these facts to investors. ¶¶139-46.

Specifically, at the December 9 Board meeting noted above, Price acknowledged to the Board that the "magnitude" of the losses set forth in the December 3 loss report was "quite significant." ¶139. On December 12, 2008, just two days after Mayopoulos had been fired, Lewis and Price received a report showing that Merrill's pre-tax losses were now forecast to be at least $18 billion for the quarter. ¶143. By this time, Lewis had formally informed the BoA Board that Merrill's losses gave BoA grounds to invoke the MAC. ¶143. Had Lewis or Price wanted to terminate the merger, as the Bank Defendants contend, they undoubtedly could have disclosed the losses, confronted Merrill, and invoked the MAC. As the SAC alleges, however, rather than doing so, Lewis and Price secretly went to the Government and requested a massive taxpayer bailout. ¶¶145-65.

Thus, on December 17, Lewis and Price called Treasury Secretary Henry Paulson and told him that BoA had grounds to terminate the merger and was "strongly considering" doing so. ¶144. In a meeting later that day with Secretary Paulson and Federal Reserve Chairman Ben Bernanke, Lewis and Price attempted to explain Merrill's $18 billion pre-tax fourth quarter loss. ¶145. Lewis and Price represented to Secretary Paulson and Chairman Bernanke that Merrill's losses were so large that BoA had grounds to invoke the MAC and terminate the merger, but proposed that, in order to avoid that outcome and salvage the deal, BoA would need a massive taxpayer bailout to account for Merrill's losses, including an asset guarantee of tens of billions of dollars. ¶¶145-46.

Moreover, to justify their position that BoA had grounds to invoke the MAC, Lewis and Price falsely told regulators that Merrill's losses had arisen only after the shareholder vote. ¶145. In order to allow Paulson and Bernanke to evaluate this claim and BoA's need for a bailout to absorb Merrill's

losses, Paulson and Bernanke requested Merrill's loss reports. ¶¶146-47. As set forth above, while Lewis and Price contend on this motion that the loss reports they received during the fourth quarter were always preliminary or incomplete because they contained "wild-ass guesses" (Def. Mem. at 5), Lewis and Price provided the Government with the same intra-quarter loss reports that they had received and relied upon throughout the fourth quarter – the same loss reports upon which the allegations of the SAC are based. ¶¶146-47. After analyzing this data, regulators concluded that Lewis's claim that Merrill's losses arose after the vote was "not credible." ¶¶147-51.

On December 19, 2008, Lewis and Price again spoke with Secretary Paulson and Chairman Bernanke to inform them that Merrill's losses had increased to more than $21 billion (pre-tax), adding urgency to BoA's demand for a bailout. ¶152. Significantly, these additional losses consisted principally of the $2.2 billion goodwill charge that Lewis and Price had been aware of since mid-November 2008. *Id.* Directly contrary to the arguments that the Bank Defendants advance in their brief, at no time did Lewis or Price tell the Government that the goodwill charge was "irrelevant" because it would be eliminated in the merger, and was only a "non-cash" "potential charge for the end of the quarter." Def. Mem. at 11-12, 29. Rather, Lewis and Price included this goodwill charge as further evidence of the severity of Merrill's losses, and to obtain the bailout. ¶152.

Lewis then reiterated to Secretary Paulson that BoA had grounds to invoke the MAC and that, in order to complete the merger, BoA required the Government to either directly purchase Merrill's toxic assets or provide an asset guarantee to BoA. *Id.* In response, the Government informed Lewis that the grounds he was using to justify invoking the MAC (*i.e.*, Merrill's losses) had existed before the shareholder vote, and thus, if he attempted to invoke the MAC now, the market would know that he had misled investors about Merrill's financial condition and the impact of the merger on BoA. ¶153. Secretary Paulson and Chairman Bernanke pointedly warned Lewis that invoking the MAC "after three months of review … and public remarks by the management of [BoA] about the benefits of the

acquisition would cast doubt in the minds of financial market participants … about the due diligence and analysis done by the company, its capability to consummate significant acquisitions, its overall risk management processes, and the judgment of its management." *Id.*

On December 21, 2008, Lewis again secretly spoke with Secretary Paulson concerning BoA's belief that it had grounds to invoke the MAC and Lewis's request for a bailout. ¶154. Because regulators had concluded that Lewis, Price, and BoA were fully aware of Merrill's losses before the shareholder vote (¶¶147-51), Secretary Paulson bluntly told Lewis that if BoA attempted to invoke the MAC now – after choosing to conceal the losses from shareholders voting on the merger – Lewis and BoA's senior management would be fired. ¶154. Lewis replied: "That makes it simple. Let's de-escalate." ¶155. Paulson also agreed to Lewis's request for a bailout to enable BoA to complete the merger. ¶156. BoA executives immediately began working with federal regulators to design a bailout package. *Id.* The following day, Lewis – who recognized that BoA's shareholders would suffer for "two to three years" as a result of his decision to proceed with the merger – took the astounding step of contacting Chairman Bernanke seeking an "immunity" letter certifying that the Government had "ordered him to proceed" with the merger "for systemic reasons," which he could "use as a defense" in anticipated shareholder lawsuits. ¶¶156-57. Bernanke denied Lewis's request. ¶157.

G. Lewis And Price Conceal The Bailout Until After The Merger Closes

As the Court has found, Lead Plaintiffs' allegations "detailed" in "non-conclusory" terms that before the merger closed, "a definitive agreement was reached between [BoA] and federal regulators [that] was <u>intentionally not memorialized in order to avoid public disclosure</u>." *Bank of America Corp.*, 2010 WL 3448194, at *43. On December 22, 2008, Lewis and Price informed the BoA Board that the Government had agreed to provide BoA with a taxpayer bailout, and deliberated over "the importance of the timing of the announcement of the commitment of the Fed and Treasury." ¶¶160-62. Based on his understanding that the Government would have to disclose the bailout if it were reduced to writing,

and that if the bailout were disclosed prior to the merger closing, the merger would "f[a]ll apart," Lewis determined that BoA would not enter into a written agreement prior to the close of the merger. ¶162. Lewis informed the BoA Board of his decision in an email that day, telling them that BoA did not want the Government to commit the terms of the bailout to writing because that would require "public disclosure, which of course we do not want." ¶¶162, 253. Lewis reiterated the need for secrecy regarding the bailout in a subsequent meeting with the BoA Board. As notes of the BoA Board's December 30, 2008 meeting reflect, Lewis admonished the members of BoA's Board not to "leak/disclos[e]" this information. ¶¶164, 253.

When subsequently questioned by the New York Attorney General about his reasons for failing to disclose the bailout to BoA investors prior to the close of the merger, Lewis falsely claimed that Secretary Paulson "instructed" him not to disclose the taxpayer bailout. ¶254. After the New York Attorney General publicly exposed this lie, Lewis unequivocally recanted his false statement in sworn congressional testimony. ¶¶254-56. Secretary Paulson has also made clear in sworn congressional testimony that he did not instruct Lewis not to disclose the bailout. ¶255. In truth, as the SAC alleges, Lewis and Price themselves determined to conceal from investors Merrill's losses and the bailout in order to ensure that their acquisition of Merrill would proceed.

III. Pleading Standards

A Rule 12(b)(6) motion must be denied if the complaint in question "contain[s] sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'" *Ashcroft v. Iqbal*, 129 S. Ct. 1937, 1949 (2009). In reviewing a complaint under Rule 12(b)(6), the court must take all factual allegations as true and draw "all reasonable inferences … in favor of the plaintiffs." *Bank of America Corp.*, 2010 WL 3448194, at *2. Rule 12(b)(6) "does not require detailed factual allegations," (*Iqbal*, 129 S. Ct. at 1949), but a complaint must describe sufficient facts to "raise a right to relief above the speculative level" (*Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 555 (2007)). On a motion to dismiss,

the court may consider "documents attached as exhibits to the complaint or incorporated into the complaint by reference" or documents that are "integral to the plaintiff's claim." *In re Gildan Activewear, Inc. Sec. Litig.*, 636 F. Supp. 2d 261, 268 n.3 (S.D.N.Y. 2009) (internal quotation marks and citations omitted). The court's function, however, is "not to weigh the evidence that might be presented at a trial," but merely to "determine whether the complaint itself is legally sufficient." *Ebusinessware, Inc. v. Tech. Srvs Group Wealth Mgmt. Solutions*, *LLC*, No. 08 Civ. 09101 (PKC), 2009 WL 5179535, at *18 (S.D.N.Y. Dec. 29, 2009) (Castel, J.) (quoting *Goldman v. Belden*, 754 F.2d 1059, 1067 (2d Cir. 1985)).[13]

Recognizing that the SAC easily satisfies these standards, the Bank Defendants argue for a still further heightened standard of "greater precision" because Lead Plaintiffs have had access to some limited discovery, which Lead Plaintiffs did not conduct. *See* Def. Mem. at 14 (quoting *Billard v. Rockwell Int'l Corp.*, 683 F.2d 51 (2d Cir. 1982)). The Bank Defendants are wrong, and no court has ever adopted this argument. Contrary to this claim, *Billard* does not require any standard more stringent than that already applied by the Court in its August 27 Opinion. In *Billard*, rather than imposing a heightened pleading standard whenever plaintiffs have had discovery, the Second Circuit merely found that the complaint as alleged was insufficient because it "fail[ed] to state the time, place [and] persons responsible" for the alleged fraud, and that Rule 9(b) required "greater precision" than plaintiffs had offered. 683 F.2d at 57.[14]

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[13] The Bank Defendants rely on *In re Optionable Sec. Litig.*, 577 F. Supp. 2d 681, 690 (S.D.N.Y. 2008) in urging the Court to ignore the SAC's well-pled allegations because the sources of Lead Plaintiffs' information purportedly contradict these allegations. Def. Mem. at 5 n.11. The Bank Defendants' reliance is misplaced. The court in *Optionable* rejected allegations based on the plain language of the document from which plaintiffs quoted, whereas here, the Bank Defendants rely on their own interpretation in an attempt to contradict the language from the sources quoted in the SAC. *See, e.g.*, Def. Mem. at 21 n.37 (arguing that Mayopoulos statement "What happens if neg. shh. vote?" only meant that Mayopoulos was "curious" to know what would happen under the merger agreement if shareholders voted against the merger). The Bank Defendants' efforts to spin a counter-narrative based on the documents and emails referenced in the SAC raise factual issues not suitable for resolution on a motion to dismiss, and are fundamentally at odds with the requirement that the Court draw all reasonable inferences in favor of Lead Plaintiffs. *Bank of America Corp.*, 2010 WL 3448194, at *2.

[14] *United States v. New York City Health and Hospital Corporation*, No. 95 Civ. 7649 (LMM), 2000 WL 1610802 (S.D.N.Y. Oct. 27, 2000), a False Claims Act case that the Bank Defendants also cite for the "greater precision" standard, fails for the

IV. Lewis And Price Acted With Scienter In Failing To Disclose Merrill's Losses

In its August 27 Opinion, the Court held that Lead Plaintiffs adequately alleged that Merrill's "fourth quarter losses were material, that all defendants were aware of the losses as they occurred, and that they had a duty to disclose them." *Bank of America Corp.*, 2010 WL 3448194, at *54. The Court dismissed Lead Plaintiffs' Section 10(b) claim for failure to disclose these losses solely because the Court held that the Consolidated Amended Class Action Complaint ("AC") did not "sufficiently allege how the failure to disclose the losses was 'highly unreasonable' and 'represent[ed] an extreme departure from the standards of ordinary care.'" *Id.* at *53 (quoting *Kalnit v. Eichler*, 264 F.3d 131, 142 (2d Cir. 2001) (emphasis in original)). To resolve that deficiency, the SAC sets forth a host of remarkable new facts taken from the internal documents and sworn testimony of Defendants, BoA's counsel, and others, which establish that Lewis and Price knew they were defrauding the market by concealing Merrill's historic losses. When "all of the facts alleged [are] taken collectively," as they must be, they fully demonstrate that Lewis and Price departed so extremely from the standard of ordinary care that "the danger [of misleading investors] was either known to [them] or so obvious that [they] must have been aware of it." *Id.* at 47, 53 (quoting *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 322-23 (2007) & *Kalnit*, 264 F.3d at 142).[15]

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same reason. There, the court found allegations sufficient to meet the standard of Rule 9(b) where the complaint "allege[d] specific facts about the contract underlying the fraud and when and how the fraudulent claims were submitted." *Id.* at *3.

[15] Lewis, Price, and BoA contend that, in order to state a Section 10(b) claim, Lead Plaintiffs must allege the exact date when Lewis and Price should have disclosed Merrill's losses. *See* Def. Mem. at 22. This is not the law. Even if it were, this Court has held, and the SAC specifically alleges, that Defendants were required to disclose Merrill's losses beginning on November 3, the date the Proxy was issued. *See Bank of America Corp.*, 2010 WL 3448194, at *34; *see also* ¶226. Notably, BoA internally determined to make a disclosure one week before the shareholder vote – clear evidence that Lewis and Price knew that, at a minimum, disclosure was required before the vote. ¶109. Defendants' duty to disclose was further heightened when Lewis and Price learned on December 3 that Merrill's losses had increased to a staggering $16.2 billion. ¶¶124-26.

For this reason, Lead Plaintiffs' Section 10(b) claim relating to Merrill's losses begins on November 3, and not on September 18, as the Bank Defendants contend. *See* Def. Mem. at 5. The Section 10(b) Class Period – which includes claims relating to both Merrill's losses and the secret bonus agreement – begins on September 18 because that is when Defendants filed the merger agreement, which contained false and misleading statements concerning the secret bonus agreement – a claim that this Court has already sustained. *See Bank of America Corp.*, 2010 WL 3448194, at *74.

A. Lewis And Price Knew That Their Concealment Of Merrill's Losses Defrauded The Market

The SAC alleges that Lewis and Price knew that the market expected Merrill to be profitable in the fourth quarter of 2008 and did "not have an inkling" that Merrill was suffering losses of historic proportions. ¶¶107, 171. Lewis and Price further knew that this striking disparity between the market's expectation and Merrill's "terrible" financial condition – a gap between what "we know relative to what they know" – drove the advice from counsel and BoA executives to disclose Merrill's losses. ¶¶104, 107-09, 167, 264. Notwithstanding this knowledge, Lewis and Price intentionally concealed Merrill's losses from investors during the largest merger in BoA's history and, by doing so, knew that they had defrauded the market and created a "fundamental issue of lack of credibility" with investors. ¶¶171-72.

These facts alone are more than sufficient to establish scienter at the pleading stage. Courts uniformly recognize that a defendant engages in "highly unreasonable" conduct when it possesses knowledge of facts which indicate that its disclosures are misleading or incomplete, but nonetheless conceals those facts from investors. *See, e.g.*, *In re Am. Int'l Grp., Inc. 2008 Sec. Litig.*, No. 08 Civ. 4772 (LTS), 2010 WL 3768146, at *16-17 (S.D.N.Y. Sept. 27, 2010) (Swain, J.) (scienter adequately pled where defendants "deliberately declined [] to disclose [known] risks to the marketplace"); *In re Alstom SA Sec. Litig.*, 406 F. Supp. 2d 433, 458-59 (S.D.N.Y. 2005) (Marrero, J.) (scienter adequately pled where defendants acted "highly unreasonabl[y]" by failing to disclose exposure to company in known financial peril); *In re Globalstar Sec. Litig.*, No. 01 Civ. 1748 (SHS), 2003 WL 22953163, at *6-7 (S.D.N.Y. Dec. 15, 2003) (Stein, J.) ("highly unreasonable" conduct alleged where defendants possessed "specific information which called into doubt their stated projections," but failed to disclose it); *In re Keyspan Corp.*, No. 01 Civ. 5852 (ARR), 2003 WL 21981806, at *16 (E.D.N.Y. July 30, 2003) (scienter alleged where defendants "were aware of serious problems at [subsidiary company] that threatened that company's fundamental health" but "[n]evertheless, … did not publicly reveal these

problems").[16]

Rather than confront these facts, the Bank Defendants principally argue that they did not intentionally mislead the market because BoA's and Merrill's SEC filings warned of "a 'turbulent' and 'tumultuous' economic forecast for the quarter." Def. Mem. at 15. It is impossible to reconcile Lewis's and Price's asserted belief that their risk disclosures were sufficient with their knowledge that the market expected Merrill to be profitable in the fourth quarter, and their own internal recognition that they had misled the market by concealing Merrill's losses. Indeed, Mayopoulos, Brown, and Wachtell all informed Lewis and Price that they had to disclose Merrill's historic losses precisely because these risk warnings did not adequately inform the market of Merrill's losses.[17] ¶¶105-09, 122-23.

Lewis and Price also knew these risk disclosures were insufficient to warn of Merrill's catastrophic losses because they were virtually identical to the disclosures that Merrill had issued for the first three quarters of 2008, during which Merrill lost an average of $6.5 billion per quarter – $1 billion less than Merrill lost in October alone, and almost $10 billion less than Merrill lost in the two months preceding the shareholder vote.[18] ¶91. Moreover, in the months leading up to the merger, Defendants repeatedly told the market that Merrill had "a much lower risk profile" as a result of

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[16] The Bank Defendants' reliance on *L.L. Capital Partners, L.P. v. Rockefeller Center Properties*, 921 F. Supp. 1174, 1183 (S.D.N.Y. 1996), for the proposition that internal disagreements over whether to disclose information does not support an inference of scienter (Def. Mem. at 33 n.57) fails. Unlike the repeated warnings to disclose here, *L.L. Capital Partners* does not involve internal warnings or debates over disclosure, and is thus inapposite.

[17] While the Bank Defendants now contend that they always believed their risk disclosures were adequate, and that they simply had not "focused" on their risk disclosures at the time of the November 13 meeting (Def. Mem. at 26), the Proxy had been issued ten days before the November 13 meeting. Obviously, all of the participants at this meeting were well aware of the purported "risk disclosures" in the Proxy and BoA's and Merrill's other SEC filings – indeed, certain of the participants at that meeting drafted these documents. At no time during that meeting did the lawyers say that they did not need to disclose the losses because of the existing risk disclosures. To the contrary, the lawyers agreed that a disclosure was necessary precisely because they understood that the risk disclosures did not adequately warn investors of Merrill's staggering losses. At best, the Bank Defendants' contention raises a fact issue that cannot be resolved on this motion.

[18] *Compare* Merrill's Nov. 5, 2008 Form 10-Q, Singer Decl. Ex. B, at 83 ("Turbulent market conditions in the short and medium-term will continue to have an adverse impact on our core business") *with* Merrill's August 5, 2008 Form 10-Q, Singer Decl. Ex. C, at 78 ("Market conditions in the short- and medium-term will continue to have an ongoing adverse impact on our businesses") *with* Merrill's May 6, 2008 Form 10-Q, Singer Decl. Ex. D, at 70 (stating that "challenging market conditions [would] continue to have an ongoing impact on our business," and specifying various "negative" and "adverse" effects that its "businesses" and "products" would suffer if adverse market conditions persisted or worsened). Conspicuously, the Bank Defendants' excerpts of these filings attached to the Park Declaration omit these pages.

"reduc[ing] exposures and de-leverag[ing] the balance sheet prior to the closing of the Bank of America deal," and, thus, that the merger "should significantly enhance our earnings." ¶¶83, 85, 86. For precisely these reasons, Lewis and Price knew that the analyst community believed that the worst was behind Merrill, and that their generic risk disclosures gave investors no reason to expect that Merrill was experiencing historic losses in the fourth quarter. ¶91. Accordingly, the statements on which Lewis and Price rely cannot immunize them from liability. *See Bank of America Corp.*, 2010 WL 3448194, at *33-34 (finding risk disclosures insufficient because "[b]y the time the Joint Proxy issued, the stormy forecast for the fourth quarter was not merely a projection: the storm had arrived"); *Heller v. Goldin Restructuring Fund, L.P.*, 590 F. Supp. 2d 603, 618 (S.D.N.Y. 2008) (securities laws provide "no protection to someone who warns his hiking companion to walk slowly because there might be a ditch ahead when he knows with near certainty that the Grand Canyon lies one foot away"); *Edison Fund v. Cogent Inv. Strategies Fund, Ltd.*, 551 F. Supp. 2d 210, 226 (S.D.N.Y. 2008) ("If a party is aware of an actual danger or cause for concern, the party may not rely on a generic disclaimer in order to avoid liability").

Notably, the Second Circuit, in a unanimous opinion authored by now-Justice Sotomayor, declined to adopt the argument the Bank Defendants advance here. *See Press*, 218 F.3d at 130. In *Press*, plaintiffs alleged that defendants, a group of broker-dealers, violated Section 10(b) by failing to disclose that they received fees from money market funds into which they swept their clients' funds. The district court dismissed plaintiffs' claim on the ground that, as the Bank Defendants argue here, "assorted disclosures in the fund prospectuses … negated any possible inference that defendants intended to deceive their customers." *Id.* The Second Circuit rejected that analysis, stating that "we have never held that such disclosures may, as a matter of law, negate allegations of fraudulent intent. The district court's scienter analysis thus raises <u>serious concerns</u>."[19] *Id.* Given that the Second Circuit

[19] The *Press* court sustained the district court's decision on alternative grounds that are not at issue here.

has discredited the Bank Defendants' argument, this Court should not accept it here.

Finally, the contention that Lewis and Price lacked scienter because they supposedly were not aware of their duty to disclose Merrill's losses (Def. Mem. at 24-25) is contrary to the scienter standard articulated by this Court. *Bank of America Corp.*, 2010 WL 3448194, at *53 (stating that Lead Plaintiffs must allege "conduct which is highly unreasonable and which represents an extreme departure from the standards of ordinary care to the extent that the danger was either known to the defendant or so obvious that the defendant must have been aware of it") (internal quotations and citation omitted). Even assuming that ignorance of the law was a defense, the fact that Mayopoulos and Wachtell advised Price that BoA was required to disclose the losses satisfies this purported standard. Moreover, even after Mayopoulos reversed the disclosure advice, Price knew that, in reality, Merrill's losses exceeded the arbitrary threshold for materiality set by Mayopoulos. Thus, even under Mayopoulos's revised analysis, Price knew that BoA had an affirmative disclosure obligation.

B. Lewis And Price Acted Highly Unreasonably In Disregarding Counsel's Advice To Disclose Merrill's Losses, And In Subsequently Misleading Counsel

Lewis and Price also disregarded the advice of BoA's General Counsel and Wachtell to disclose Merrill's losses, further demonstrating their highly unreasonable conduct. As set forth above, on November 13 – just ten days after the Proxy was issued – BoA's General Counsel and Wachtell jointly agreed that BoA was required to disclose Merrill's losses, and informed Price of their determination.[20] ¶¶103-09, 111, 264. Though it was agreed that Price would inform Thain of counsel's recommendation

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[20] The claim that Mayopoulos and Wachtell did not agree that "there must be disclosure of Merrill's 'losses' or that there must be disclosure 'beyond what was in the Proxy'" (Def. Mem. at 25-26) is contradicted by the allegations in the SAC. Lewis, Price, and BoA concede that the subject of the November 13 meeting was whether Merrill's October losses had to be disclosed. *Id.* at 25. As they further concede, the handwritten notes of that meeting reflect that counsel had "<u>all agree[d] must be some discl[osure]</u>." *Id.*; *see also* Park Decl. Ex. 21. The document speaks for itself, and supports the allegation that counsel agreed that disclosure of Merrill's losses was required. Significantly, the Bank Defendants offer no <u>other</u> explanation as to what potential disclosure was being discussed at that meeting other than disclosure of Merrill's losses. Further, given that the Proxy had been filed just ten days earlier and that Wachtell was a primary drafter of the Proxy, the only reasonable inference to be drawn from this document is <u>not</u> that counsel somehow forgot about the Proxy, but that counsel recognized that the Proxy's disclosures were insufficient to alert investors to Merrill's October losses. *See MacDonald v. Safir*, 206 F.3d 183, 190 (2d Cir. 2000) (on Rule 12(b)(6) motion, the court is "to view all reasonable inferences that can be drawn from [the complaint's] allegations <u>and documents</u> in the light most favorable to the plaintiff").

to disclose Merrill's losses, Price did not do so when he met with Thain the following day. ¶111. Instead, immediately following a meeting with Price, Mayopoulos reversed his disclosure decision because Price and Mayopoulos knew that, if the losses were disclosed, shareholders would vote the merger down.[21] ¶¶113-14.

It is well established in this Circuit that ignoring the advice of counsel is "highly unreasonable" conduct "which represents 'an extreme departure from the standards of ordinary care.'" *SEC v. McNulty*, 137 F.3d 732, 741 (2d Cir. 1998); *see also SEC v. Blinder, Robinson & Co., Inc.*, 542 F. Supp. 468, 476-477, 481 (D. Colo. 1982) (there is "no more telling indication of knowledge than the direct receipt of the advice" of counsel on disclosure; defendants "cannot hide behind legal advice that they chose to ignore"). In *McNulty*, the Second Circuit held that a defendant's refusal to heed his attorney's advice to omit misleading statements from an SEC filing was "conduct which is 'highly unreasonable' and which represents 'an extreme departure from the standards of ordinary care.'" 137 F.3d at 741. Here, Lewis and Price engaged in highly unreasonable conduct by ignoring counsel's advice to disclose Merrill's losses in advance of the shareholder vote. ¶¶103-17.

The SAC also establishes the inference that Lewis knew of counsel's position on disclosure because Price kept Lewis "informed all the time" on matters relating to the merger. ¶247. It is far more reasonable to infer that Price disclosed to Lewis that both BoA's General Counsel and senior Wachtell partners agreed that losses of $5 billion must be disclosed than to imagine that Price kept that fact – which presented the single most serious risk to the consummation of one of the largest mergers in Wall Street history – from Lewis. Accordingly, Lewis's refusal to disclose Merrill's losses in contravention

[21] The Bank Defendants alternatively argue that (i) the SAC does not allege that Price was ever informed that counsel had determined that there was a duty to disclose Merrill's losses (Def. Mem. at 26), and (ii) the SAC does allege this but those allegations should be disregarded because they are "conclusory" or "awkward[ly]" phrased (Def. Mem. at 26 n.46). These arguments are as meritless as they are inconsistent. The SAC alleges that Price was informed of counsel's determination that disclosure of BoA's losses was required. ¶264 ("BoA's in-house and outside counsel concluded that BoA needed to disclose these loss figures and informed Price of their conclusion"). In addition, the SAC alleges that Price was the one who was supposed to inform Thain that disclosure was required. ¶111. The Bank Defendants' attempt to read these allegations out of the SAC should be rejected.

of the advice of counsel was also highly unreasonable conduct that represented an extreme departure from the standard of care expected of officers of a public company. *McNulty*, 137 F.3d at 741.

Moreover, as courts regularly hold, allegations that a defendant lied to advisors to avoid disclosure of material facts establishes a powerful inference of scienter. *See, e.g.*, *United States v. Ingredient Tech. Corp.*, 698 F.2d 88, 96 (2d Cir. 1983) (fact that defendants lied to their attorneys and auditors about secret resale agreement is strong evidence of scienter); *Hughes v. Huron Consulting Group, Inc.*, No. 09 C 4734, 2010 WL 3087501, at *3 (N.D. Ill. Aug. 6, 2010) (scienter adequately alleged where defendant failed to disclose material facts to auditor); *SEC v. Lucent Tech. Inc.*, No. Civ. 04-2315 (WHW), 2005 WL 1683741, at *2 (D.N.J. July 18, 2005) (scienter requirement satisfied where complaint alleged that defendant "lied to the chief accountant"). Here, Lewis and Price not only ignored Mayopoulos's and Wachtell's advice, but Price also pressured Mayopoulos to reverse the disclosure decision, and then repeatedly lied to Mayopoulos so he would not advise them again that disclosure was required. Mayopoulos unequivocally testified to Congress, the SEC, and the New York Attorney General that Price gave him information that was materially inaccurate, and understated Merrill's losses by billions of dollars. ¶¶127, 265. There is no innocent explanation for why Price did not inform Mayopoulos about the true size of Merrill's losses – particularly given that Price had previously discussed Merrill's losses with Mayopoulos – and the Bank Defendants do not even attempt to invent one. The most compelling inference – if not the only inference – that can be drawn from these facts is that Price did not want Mayopoulos to know the full extent of Merrill's losses.[22]

Tellingly, when Mayopoulos discovered that he had been lied to and sought to confront Price, BoA terminated Mayopoulos without explanation and immediately escorted him from the premises. ¶¶139-42. The suspicious manner and timing of Mayopoulos's termination is also compelling evidence

[22] Price could not have forgotten to give Mayopoulos the revised loss figures on December 3 – Price met with Mayopoulos only hours after he had a "somber" discussion about Merrill's massive losses with Lewis, Thain, and Cotty. ¶¶124-27. Nor can Price claim that he did not give Mayopoulos the revised December 3 loss report because it was supposedly just an estimate. The loss report that Price provided Mayopoulos in November contained estimates as well. ¶¶102-03, 146.

of Lewis's and Price's scienter. *See Hall v. Children's Place Retail Stores, Inc.*, 580 F. Supp. 2d 212, 233 (S.D.N.Y. 2008) (CEO's resignation "add[ed] to the overall pleading of circumstantial evidence of fraud"); *In re Adaptive Broadband Sec. Litig.*, No. C 01-1092 SC, 2002 WL 989478, at *14 (N.D. Cal. Apr. 2, 2002) (finding "corporate reshuffling" highly suspicious and "one more piece to the scienter puzzle"). Moreover, BoA's decision to replace Mayopoulos as General Counsel with an individual who did not have an active law license and who had not practiced in 15 years is compelling evidence that Lewis and Price did not want BoA advised by a General Counsel capable of advocating for disclosure, as they knew Mayopoulos would. ¶141; *see In re New Century*, 588 F. Supp. 2d 1206, 1216 (C.D. Cal. 2008) (scienter adequately pled against auditor where, *inter alia*, "KPMG made conscious decisions to allow inexperienced staff, including first-year auditors in some instances, to conduct analyses of accounting and internal controls"). That inference is further supported by the fact that the new General Counsel was transferred to a non-legal position weeks after the merger closed. *Id.* The Bank Defendants have offered no competing innocent inference to be drawn from these facts. Def. Mem. at 34. Lewis's and Price's actions in terminating and replacing Mayopoulos create a cogent and compelling inference of their scienter in concealing Merrill's losses from BoA's investors.[23]

The Bank Defendants also contend that "the SAC does not allege any reason why Price would have been interested in misleading Mayopoulos." Def. Mem. at 28. In light of the specific allegations that Lewis and Price knew they were defrauding the market and deceived their own counsel, the SAC need not plead any motive allegation in order to establish scienter. *See Ganino*, 228 F.3d at 170. Nevertheless, the SAC alleges that Lewis and Price were highly motivated to acquire Merrill. Lewis had "long clamored" for Merrill and viewed it as "the final piece" of his plan to make BoA the

[23] The allegations concerning the deception and termination of Mayopoulos fully rebut the Bank Defendants' contention that Price "was not even in a position to alter Mayopoulos's advice." Def. Mem. at 30. Price was the second highest-ranking officer at BoA, and the Company summarily terminated Mayopoulos when he sought to confront Price after learning the truth about Merrill's losses. ¶¶139-42. The SAC alleges that Price pressured Mayopoulos to change his disclosure decision, impressing upon Mayopoulos the ramifications of disclosure, and then repeatedly lied to him. ¶¶113-14. Those were the very steps that prevented Mayopoulos from rendering an independent and informed legal opinion on disclosure.

country's biggest bank by assets, and Price and Lewis knew that disclosing the losses would kill the merger. ¶63. Thus, Lewis and Price were highly motivated to mislead Mayopoulos to ensure that Mayopoulos would not advise disclosure and investors would not learn the truth.

C. Lewis's And Price's Reliance On Counsel Defense Fails

Lewis's and Price's attempt to assert a reliance on counsel defense (*see* Def. Mem. at 25) is unavailing in light of Price's deception of Mayopoulos and Wachtell. The most basic tenet of the "reliance on counsel" defense is that defendants must have provided full and accurate information to counsel, which Lewis and Price repeatedly failed to do. *See*, *e.g.*, *United States v. Winans*, 612 F. Supp. 827, 848 (S.D.N.Y. 1985) ("Essential to any claim based on reliance on counsel is that the attorney must have been fully informed of all the relevant facts.").[24] While Lewis and Price further argue that they were entitled to assume that Wachtell "would speak up if they disagreed with" Mayopoulos's and Price's reversal of the decision to disclose Merrill's losses, this assertion also fails. Def. Mem at 27-28. The law is clear that Price was <u>not</u> entitled to rely on the <u>silence</u> of Wachtell – especially after having <u>misled</u> Wachtell as to the size of Merrill's losses. *See SEC v. Enterprises Solutions, Inc.*, 142 F. Supp. 2d 561, 576 (S.D.N.Y. 2001) (rejecting argument that a defendant can rely on counsel's silence); *SEC v. Nat'l Student Mktg. Corp.*, 457 F. Supp. 682, 711 n.68 (D.D.C. 1978) (defendant "did not rely upon actual advice of counsel, but, if at all, on counsel's silence, and this despite the fact that he never asked for a specific opinion . . . . This <u>blind inaction</u> hardly constitutes good faith reliance on counsel.").[25] Moreover, on the one occasion when Wachtell was actually asked whether BoA was required to

[24] The Bank Defendants' contention that Price gave Mayopoulos "all relevant information" on December 3 (Def. Mem. at 32) ignores the allegations of the SAC, including that Mayopoulos testified before Congress, the SEC, and the New York Attorney General that he was not given complete and accurate loss information on December 3 (¶¶127-28, 139-41). At best, the Bank Defendants' assertion raises an issue of fact that cannot be decided on this motion.

[25] Further, an assertion of reliance on counsel is a highly fact-intensive affirmative defense that cannot negate scienter at the pleading stage. *Siemers v. Wells Fargo & Co.*, No. C 05-04518 WHA, 2006 WL 2355411, at *9 (N.D. Cal. Aug. 14, 2006) ("If defendants wish to rely on advice of counsel defense, that would be a matter for an affirmative defense" subject to discovery); *SEC v. Martino*, 255 F. Supp. 2d 268, 285 (S.D.N.Y. 2003) (listing facts that must be established for defense to be invoked). Moreover, it is "not a complete defense, but only one factor for consideration." *Markowski v. S.E.C.*, 34 F.3d 99, 105 (2d Cir. 1994).

disclose Merrill's losses, Wachtell informed BoA that it was required to disclose a week before the shareholder vote. ¶¶104-11, 264. Given that Wachtell had already informed BoA that the losses should be disclosed the one time they were specifically asked, and was not asked to opine on Price's and Mayopoulos's reversal of that decision, it is not surprising that Wachtell did not openly question BoA's decision to ignore its advice.

D. Lewis Acted Highly Unreasonably In Deliberately Avoiding Legal Counsel In The Face Of Merrill's Historic Losses

Even if Defendant Lewis denies knowledge of Wachtell's and Mayopoulos's advice to disclose Merrill's losses, his conduct would still be highly unreasonable. In that case, Lewis's failure to consult counsel regarding disclosure demonstrates "'[a]n egregious refusal to see the obvious, or to investigate the doubtful'" which gives rise to a strong inference of scienter. *SEC v. Czarnik*, No. 10 Civ. 745 (PKC), 2010 WL 4860678, at *6 (S.D.N.Y. Nov. 29, 2010) (Castel, J.) (quoting *Novak v. Kasaks*, 216 F.3d 300, 308 (2d Cir. 2000)). Lewis has stated that he took no steps to personally determine whether disclosure was required or to ensure that Mayopoulos or Wachtell received accurate information about Merrill's losses. ¶249. Given the importance of the merger to BoA's investors, and the magnitude of Merrill's losses, the most plausible inference arising from Lewis's failure to personally consult with any advisor regarding disclosure is that Lewis did not want the losses to be disclosed so that the merger could proceed – and that he expected any reasonably-informed advisor to tell him that he must disclose the losses, which would kill the merger. Lewis's "'conscious avoidance of [such] knowledge'" satisfies the scienter requirement. *See Czarnik*, 2010 WL 4860678, at *11 (quoting *McNulty*, 137 F.3d at 737).

In addition, the Bank Defendants' contention that Lewis was neither required nor expected to seek legal advice regarding BoA's disclosure obligations in the face of Merrill's staggering losses is belied by the very authorities they offer in support of this contention. These authorities make clear that corporate executives cannot benefit from ostrich-like willful ignorance of their duties to shareholders, and in fact have an affirmative obligation to ensure that their company's disclosures are complete and

accurate. As the SEC has made clear:

> Serving as an officer or director of a public company is a privilege which carries with it substantial obligations. If an officer or director knows or should know that his or her company's statements concerning particular issues are inadequate or incomplete, he or she has an obligation to correct that failure.
>
> * * *
>
> [The defendant executives], given their positions as directors or senior officers and their particular knowledge of these transactions, should have inquired as to whether the securities laws required disclosure of this information. This inquiry could have included seeking the specific and fully informed advice of counsel.

Exchange Act Rel. No. 39157, 1997 WL 597984, at *6, Report of Investigation Pursuant to Section 21(a) of Sec. Exchange Act of 1934 Concerning Conduct of Certain Former Officers & Directors of W.R. Grace & Co. (Sept. 30, 1997) (*cited at* Def. Mem. at 30 n.53).

Similarly, Judge Cedarbaum in *Enterprises Solutions*, 142 F. Supp. 2d at 575-76 (*cited at* Def. Mem. at 28 n.50), not only rejected this defense, but held that a CEO's failure to seek informed legal advice regarding whether to disclose material facts affirmatively demonstrated scienter. There, the defendant CEO (Solomon) argued that the omission of material information concerning a prior bankruptcy was not intentionally misleading because he disclosed the information to his counsel and relied on them in good faith to tell him if the information needed to be disclosed in a prospectus. *Id.* In rejecting this argument, the court held:

> Solomon included information about the bankruptcy, along with a lot of other information, in the questionnaire responses he provided to counsel. But he never sought specific advice from counsel with respect to disclosure of the bankruptcy, nor did he receive specific advice that ESI was not required to disclose the bankruptcy. Good faith reliance on the advice of counsel means more than simply supplying counsel with information. Corporate executives have an independent duty to insure that proper disclosures are made. "Compliance with federal securities laws cannot be avoided by simply retaining outside counsel to prepare required documents." *Savoy Indus.*, 665 F.2d at 1315 n.28. Solomon's failure to insure that CEA's bankruptcy was disclosed demonstrates reckless disregard for the truth, satisfying the scienter requirement.

Id. Judge Cedarbaum's decision in *Enterprises Solutions* forecloses any argument that Lewis was entitled under the securities laws to sit idly by when he knew that BoA's shareholders and investors

were being deprived of highly material information regarding the most significant acquisition in BoA's history. *See also Czarnik*, 2010 WL 4860678, at *9 (one cannot "escape liability for fraud by closing his eyes to what he saw and could readily understand") (quoting *SEC. v. McNulty*, No. 94 Civ. 7114 (MBM), 1996 WL 422259, at *6 (S.D.N.Y. July 29, 1996), *aff'd*, 137 F.3d 732 (2d Cir. 1998)).[26]

Finally, the Bank Defendants' contention that the SAC does not allege a "red flag" signaling to Lewis that he should consult with counsel regarding BoA's disclosure obligations is also wrong. Def. Mem. at 30. The SAC alleges that Lewis knew that Merrill had suffered massive – and rapidly escalating – losses in the two months after the merger was announced, and that, absent disclosure, BoA shareholders would vote on one of the largest mergers in Wall Street history, or purchase BoA securities in the open market, completely oblivious to these losses. ¶¶246-49. It is difficult to imagine more significant "red flags" indicating the need to at least consult counsel and ask for advice.[27] In fact, it was Lewis who sought a letter from the Federal Reserve immunizing him from legal liability for violating his duty to disclose these facts – a clear indication that Lewis knew that he had violated his disclosure obligations. ¶¶157-59.

E. Lewis And Price Knew That The Reports Of Merrill's Losses Were Reliable, And Provided These Same Reports To The Government To Justify The Taxpayer Bailout

Lewis's and Price's assertion that they lacked scienter because all they had were unreliable "estimates" and "forecasts" of Merrill's monthly and quarterly losses is also baseless. Def. Mem. at 7, 10. The fact that Price and Lewis provided those same loss reports to the Secretary of the United States Treasury and the Chairman of the Federal Reserve to justify the taxpayer bailout of BoA eviscerates this argument. ¶146. Neither Lewis nor Price ever suggested to the Government that Merrill's losses

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[26] Defendants' reliance on *Take-Two Interactive Software Inc. Derivative Litigation*, 1:06 Civ. 5279 (LTS), 2009 WL 1066251, at *6-7 (S.D.N.Y. Apr. 21, 2009), is misplaced. The court there considered the reasonableness of a special litigation committee's investigation and dismissed plaintiffs' derivative claim on the grounds that the committee had retained an outside law firm that was independent and qualified. *Id.* The court's observations had nothing to do with scienter.

[27] Defendants' reliance on *In re Carter-Wallace, Inc., Sec. Litig.*, 220 F.3d 36, 39 (2d Cir. 2000), is misplaced because that case does not address when an executive should consult with legal counsel.

were uncertain "guesstimates" or that the loss reports could not be relied upon because the quarter was still underway. ¶¶144-46, 152. If the loss figures were reliable enough to provide to the Government to obtain the $138 billion bailout, they were reliable enough to be disclosed to shareholders voting on the merger. ¶146.

Further, the reactions of BoA executives to these reports – *e.g.*, "[r]ead and weep," "numbers speak for themselves," "ML lost $7B in October!" and Merrill "had a terrible October" – demonstrate that they knew these figures were as reliable as they were debilitating.[28] ¶¶101, 104. Merrill's own auditor acknowledged the reliability and certainty of these reports, explaining in his sworn testimony to the New York Attorney General that "It's not a forecast; it's more as the company knows it as a P and L on a day-to-day basis. They knew what November would look like before November closed." Singer Decl. Ex. A at 190 (testimony of Thomas Graham).[29] Indeed, as Lewis himself testified to Congress, Merrill's losses were "clear" prior to the shareholder vote.[30] ¶99. In any event, even if the loss reports did not represent "final" loss calculations, they demonstrated that Merrill had suffered catastrophic losses in the two months prior to the shareholder vote – losses that Lewis and Price knew were only worsening as the quarter progressed.

Lewis and Price also contend that their failure to disclose Merrill's $2.2 billion goodwill writedown is not indicative of scienter because that writedown (i) is not properly considered to be part of Merrill's fourth quarter losses, and (ii) was "irrelevant" to investors because BoA would ultimately

[28] The Bank Defendants' attempt to minimize Merrill's October losses by claiming that October 2008 was only the second-worst month in Merrill's 94-year (1,100 month) history is nonsense. ¶95. These losses were historic, material and, as the Court held, required to be disclosed. *Bank of America Corp.*, 2010 WL 3448194, at *19. Further, although Defendants argue that the $7.5 billion loss in October would not have completely wiped out the pre-tax profits for 2006 (Def. Mem. at 7 n.15), this one-month loss was larger than Merrill's annual pre-tax profits from 2001-2005. Singer Decl. Ex. E at F-2 & Ex. F at 17. Moreover, the Bank Defendants do not question that the $15.5 billion of combined losses in October and November far exceeded the pre-tax profits for all of 2006. By any metric, Merrill's pre-vote losses were highly material and required to be disclosed to shareholders.

[29] The SAC's allegations sufficiently allege knowledge of these losses, as the Court has found. However, to the extent that Defendants selectively rely upon evidence outside of the SAC and the Court considers it, Lead Plaintiffs offer for the Court's consideration certain representative evidence that directly contradicts Defendants' proffered (and extraneous) evidence.

[30] Accordingly, the cases cited by Defendants at footnote 54 regarding the disclosure of "forecasts" are irrelevant.

write off Merrill's historical goodwill in the merger under purchase accounting rules. Def. Mem. at 11-13, 29. This argument fails. Lewis and Price included the $2.2 billion goodwill writedown in the fourth quarter losses they presented to Secretary Paulson and Chairman Bernanke on December 19 so that they could argue that Merrill's losses had increased by $2.2 billion in the two days since they first requested a bailout. *See* ¶152. In doing so, Lewis and Price acknowledged that this goodwill writedown was highly relevant to Merrill's financial condition and justification for BoA's need for the bailout.[31] Indeed, this $2.2 billion goodwill writedown was not taken under purchase accounting rules. Rather, this writedown was primarily the result of a material impairment in the value of First Franklin and was treated as a fourth quarter loss prior to the shareholder vote.[32] ¶¶93, 100. In other words, Merrill had to record this goodwill writedown regardless of the merger to reflect that a previously valuable asset was now essentially worthless, a fact that was highly material given that the merger reflected management's valuation of Merrill's goodwill as of September 15, 2008.[33]

F. Lewis And Price Wanted To Consummate The Merger

The Bank Defendants also argue that the SAC alleges that they intended to exercise the MAC before the shareholder vote, and therefore had no motive to conceal Merrill's losses. Def. Mem. at 16, 18, 19. This argument is based on a misreading of the SAC. The fact that BoA executives discussed the MAC in advance of the shareholder vote reflects only their concern about Merrill's escalating losses, and not an intention to terminate the merger. ¶¶118-19. In fact, when Mayopoulos was

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[31] For this reason alone, the Bank Defendants' contention that this Court should conclude, as a matter of law, that the goodwill writedown was attributable to a decline in the price of BoA shares and did not relate to Merrill's fourth quarter must be rejected. Def. Mem. at 12-13. As the discussion of the goodwill writedown in Merrill's Form 10-K makes clear, the impairment analysis that resulted in that writedown took into account many factors other than BoA's stock price. Park Decl. Ex. 11 at 111. At best, this contention raises an issue of fact that cannot be resolved on this motion.

[32] While the Bank Defendants contend that the "sole basis for this allegation is an unsupported assertion made in a letter from the New York Attorney General" (Def. Mem. at 13 n.23), the SAC's allegations relating to the goodwill writedown are based on Defendants' own internal documents and sworn testimony. *See, e.g.*, ¶¶110, 123, 126.

[33] In addition, the Bank Defendants' contention that Merrill had disclosed in a prior quarter that First Franklin was so impaired that the entire business had to be written down is also incorrect. The disclosures the Bank Defendants cite merely stated that First Franklin was no longer initiating new mortgages and "currently not purchasing" mortgages (Park Ex. 3 at 74) – they said nothing about the future of the unit, its mortgage servicing rights or other income-generating activities related to its loans in its portfolio.

consulted regarding the MAC, Price lied about Merrill's losses to ensure the merger would proceed. *Id.* The SAC's motive allegations make clear that Lewis and Price wanted to complete the transaction at any cost, and engaged in highly deceptive conduct to achieve that goal. *See* ¶¶63-64, 67-68, 153-56, 248-62, 268.

For the same reason, the contention that Lewis had no motive to conceal Merrill's losses because he had significant holdings of BoA stock also fails. Def. Mem. at 17 n.28. This argument ignores the allegation that Lewis coveted Merrill as the "final piece" of his plan to make BoA the largest bank in the country and deliver him significant prestige and respect for which he had "long clamored." ¶59; *see, e.g.*, *JPMorgan Chase & Co. Sec. Litig.*, MDL No. 1783, 2007 WL 4531794, at *8 (N.D. Ill. Dec. 18, 2007) (desire to "reclaim the mantle of Wall Street superstar" and "increase [] prestige and reputation" constitute motive for fraud).[34] Therefore, Lewis and Price thought they would benefit in a concrete and personal way by closing the merger.

*   *   *

In sum, given these new facts alleged in the SAC, there is no serious dispute that Lewis and Price engaged in "conduct which is highly unreasonable and which represents an extreme departure from the standards of ordinary care" in failing to disclose Merrill's losses.

V. Lewis And Price Acted With Scienter In Failing To Disclose The Government Bailout

In its August 27 Opinion, the Court held that Lead Plaintiffs adequately alleged that (i) a definitive agreement between BoA and the Government existed prior to the merger closing; (ii) Lewis and Price were obligated to disclose the Government bailout to BoA shareholders and investors; and (ii) the bailout agreement "was intentionally not memorialized in order to avoid public disclosure." *Bank of America Corp.*, 2010 WL 3448194, at *42-43. The Court dismissed Lead Plaintiffs' Section 10(b) claim regarding Lewis's and Price's failure to disclose the bailout solely because the Court concluded

[34] Defendants' reliance on *Shield v. Citytrust Bancorp, Inc.*, 25 F.3d 1124, 1130 (2d Cir. 1994), which stands for the proposition that the mere "desire for continued employment" is insufficient to allege scienter, is misplaced.

that the allegations in the AC did not reflect "'highly unreasonable' conduct representing 'an extreme departure from the standards of ordinary care.'" *Id.* at *56 (quoting *Kalnit*, 264 F.3d at 142). The SAC now demonstrates that, at the same time Lewis and Price were soliciting the $138 billion taxpayer bailout from the Government, they were internally acknowledging that their concealment of Merrill's losses and BoA's resulting need for the bailout was deceiving the market (including rating agencies and investors).

Indeed, BoA's internal emails make clear that, at the time Lewis and Price decided to conceal the bailout, they knew that they were deceiving the market as to Merrill's true financial condition and BoA's need for Government assistance. *See* ¶¶166-72. Nonetheless, recognizing that disclosure of either the taxpayer bailout or Merrill's losses would cause the merger to "f[a]ll apart," Lewis and Price consciously chose to conceal the bailout from BoA shareholders and investors. ¶171. As Lewis expressly acknowledged in an email to the BoA Board on December 22, 2008, Lewis had determined that BoA would not reduce the terms of the bailout to writing precisely because doing so would require the Government to publicly disclose the bailout – which, as Lewis stated, "of course, we do not want." ¶¶162, 172.[35]

The Bank Defendants' motion does not substantively address these emails – an omission which speaks volumes about the strength of these allegations. As these emails make clear, Lewis's and Price's decision to conceal this information from BoA investors is nothing short of "'an extreme departure from the standards of ordinary care.'" *Bank of America Corp.*, 2010 WL 3448194, at *56 (quoting *Kalnit*, 264 F.3d at 142). Accordingly, the SAC adequately pleads that Lewis and Price acted with scienter with respect to the bailout allegations. *See supra* pages 22-23 (citing¸ *inter alia*, *In re Am. Int'l Grp., Inc.*, 2010 WL 3768146, at *16-17 (scienter adequately pled where defendants "deliberately

[35] Similarly, Lewis again explained to the BoA Board in a board meeting that "written assurances would not be received before January 1, 2009 . . . because any written assurances would require formal action by the Fed and Treasury, which formal action would require public disclosure." ¶164.

declined [] to disclose [known] risks to the marketplace")).

Further, contrary to the narrative that the Bank Defendants previously embraced – that they "were acting at the instruction of the Treasury Secretary during a moment of acute economic and political uncertainty" (*Bank of America Corp.*, 2010 WL 3448194, at *56) – the SAC makes clear that Secretary Paulson never ordered Defendant Lewis to conceal the taxpayer bailout, and that Lewis misrepresented his discussions with Secretary Paulson when Lewis testified to the New York Attorney General that he was "instructed" by Secretary Paulson not to disclose the taxpayer bailout. ¶¶254-56.[36] Lewis recanted these earlier statements during a June 2009 hearing before Congress, stating that "[n]either Secretary Paulson nor the chairman of the Federal Reserve, Mr. Bernanke, ever told me not to disclose something," adding that "nobody ever told us that we should not disclose a disclosable event." ¶255.[37]

In response to these remarkable new facts, the Bank Defendants misconstrue the SAC's allegations, falsely contending that Lewis and Price wanted to terminate the merger and asserting that, if they believed disclosing the bailout would have resulted in the merger falling apart, they would have been motivated to disclose it promptly. Def. Mem. at 43. However, the SAC does not allege that Lewis and Price "wanted" to invoke the MAC and terminate the merger. *Id.* (emphasis in original). Had Lewis or Price actually wanted to terminate the merger, they undoubtedly would have disclosed

[36] Defendants mistakenly state that the "sole source of this allegation is a characterization of [Lewis's] testimony in a letter from the NYAG." Def. Mem. at 46. To the contrary, the SAC references Lewis's NYAG testimony directly, and alleges merely that the subsequent NYAG letter publicly disclosed Lewis's attempted cover-up. *See* ¶254. As a result, this Court's holding in *Footbridge Ltd. Trust v. Countrywide Home Loans, Inc.*, No. 09 Civ. 4050 (PKC), 2010 WL 3790810 (S.D.N.Y. Sept. 28, 2010) (Castel, J.) does not apply.

[37] These material inconsistencies in Lewis's sworn testimony regarding his failure to disclose the bailout strengthen the inference of his scienter. Absent an intent to deceive, there would have been no reason for Lewis to falsely state, under oath, that Secretary Paulson had ordered him to conceal the bailout. The most plausible – and, indeed, the only – inference that can be drawn from Lewis's conduct is that he knew of or recklessly disregarded his obligation to disclose the bailout to shareholders and investors and sought to exculpate BoA and himself from liability by falsely blaming Secretary Paulson for his actions. *See Novak*, 216 F.3d at 311-12; *SEC v. Lucent Techs., Inc.,* 363 F. Supp. 2d 708, 717 (D.N.J. 2005); *Rocker Mgmt., L.L.C. v. Lernout & Hauspie Speech Prods.*, No. Civ. A. 00-5965 (JCL), 2005 WL 1365465, at *13 (D.N.J. June 7, 2005). Further, in arguing that "no such 'cover-up'" existed, Defendants conveniently refer only to the June 2009 Congressional testimony of Lewis and Secretary Paulson, and conspicuously avoid referencing Lewis's prior false statements to the NYAG. *See* Def. Mem. at 47 n.88.

Merrill's losses and invoked the MAC. That is not what they did. To the contrary, rather than disclose these highly material facts, Lewis and Price secretly went to the Government and requested a bailout precisely because they wanted to complete the transaction. ¶¶144-46. The only logical inference to be drawn from these facts is that Lewis did not want to disclose the bailout in order to ensure that the merger closed without incident. ¶¶ 160-72, 251-53, 267.[38]

Beyond the fact that disclosure of the losses and the bailout would threaten to undermine the deal for which Lewis was "drooling," as the SAC's allegations make clear, Lewis and Price were personally motivated not to disclose the bailout because the Secretary of the Treasury had threatened to fire them if the merger was not consummated.[39] ¶154. Significantly, Secretary Paulson threatened to fire Lewis and Price if BoA abandoned the merger after concluding that Lewis and Price were aware of Merrill's massive losses before the vote, yet decided to conceal this information from BoA's shareholders. ¶¶147-51, 158-59. Lewis's and Price's desire to avoid termination and complete the merger are not generalized motive allegations that are "common to corporate officers," as the Bank Defendants contend. Def. Mem. at 21. Far from being common, the fact that the Secretary of the Treasury personally threatened to fire Lewis and Price if the merger did not close, and that Lewis himself expressed to Federal Reserve officials that he was concerned with losing his job, are concrete, specific facts that constitute compelling evidence of scienter.

Leis and Price also contend that they had no motive to conceal the bailout because it would be disclosed only weeks later, strategically timed to coincide with the release of fourth quarter earnings results for Merrill and BoA. Def. Mem. at 43-44. This motive argument ignores the critical fact that

[38] Lewis and Price argue that their alleged desire to obtain a written bailout agreement from the Government in December 2008 negates their scienter. *See* Def. Mem. at 46 (arguing that the SAC allegations make clear that "the Bank in fact wanted a written TARP agreement in December") (emphasis in original). However, this argument ignores the chronology of the SAC's well-pled allegations. The SAC alleges only that Lewis and Price sought a written TARP agreement until the Government informed them that a written agreement would have to be publicly disclosed. ¶¶ 162, 253. Once the threat of public disclosure was raised, Lewis retracted his request and informed the Board that BoA would not obtain a written agreement because he did not want the bailout to be publicly disclosed. ¶162.

[39] Indeed, the internal email of senior Federal Reserve officials confirms that Lewis was "worried about his own job." ¶252.

the merger was scheduled to close on January 1, 2009 and, thus, by concealing the bailout and Merrill's massive losses for "just a few weeks" (Def. Mem. at 44), Lewis and Price were able to consummate the merger. As Wachtell recognized in noting that disclosure of this information would cause the deal to "f[a]ll apart," disclosure of the taxpayer bailout (which would in turn have led to disclosure of Merrill's losses) would have caused the ratings agencies to downgrade BoA's and Merrill's credit ratings, and led BoA shareholders to file suit to enjoin the merger. These actions would almost certainly have prevented the merger from closing.[40] Thus, Defendants had a clear and compelling motive to delay the announcement of the bailout until after the merger closed.

Defendants' objective to minimize any possibility that shareholders or any other factor could "disrupt" the closing of the merger is consistent with Lewis's long-harbored desire to acquire Merrill.[41] *See* ¶63 (Lewis admitting he was "drooling" to acquire Merrill).[42] Thus, the fact that public disclosure of the bailout was "inevitable," and was only delayed for "a few weeks," does not, as Lewis and Price contend, negate the otherwise strong inference of scienter raised by the SAC. Def. Mem. at 44. To the contrary, Lewis's and Price's concealment of the bailout actually allowed them to <u>avoid</u> a potentially

[40] The Bank Defendants' contention that the threat of credit rating downgrades existed both pre-closing and post-closing misses the mark. Def. Mem. at 44-45. A pre-closing downgrade based on disclosure of the bailout or Merrill's losses would have led the merger to crater – a vastly different circumstance than a post-closing downgrade. Further, while the Bank Defendants cite to *Novak*, 216 F.3d at 307 and *South Cherry St., LLC v. Hennessee Group LLC*, 573 F.3d 98, 109 (2d Cir. 2009), for the proposition that the desire to maintain a credit rating alone does not give rise to a strong inference of scienter, here, Lead Plaintiffs have focused on the likely <u>consequences</u> of a credit rating downgrade, *i.e.*, the merger falling apart, not merely a generic desire to maintain a credit rating.

[41] The Bank Defendants attempt to dispute the meaning of the word "disrupt" in the handwritten notes of a BoA board member, suggesting that it refers only to potential disruption to the U.S. economy if BoA did, in fact, invoke the MAC. Def. Mem. at 46 n.85; Park Decl. at Ex. 26. Contrary to this contention, however, this discussion could not have been related to the MAC, as BoA had abandoned any consideration of invoking the MAC more than one week prior. *See* ¶157 (noting that, as of December 22, 2008, Defendants had confirmed their "willingness to drop the MAC"). The reasonable inference to be drawn from the document is that it refers to disruption flowing from disclosure of the bailout and the losses, which would have inevitably threatened the consummation of the merger.

[42] Lewis and Price contend that their interests were aligned with those of BoA shareholders, in part, because they were substantial holders of BoA stock. Def. Mem. at 17-18. First, the fact that Lewis and Price owned shares – which is true of most senior corporate officers – is irrelevant. Second, Lewis and Price misrepresent the extent of their BoA holdings by including shares of BoA stock held by members of the BoA Board, who have not been charged with fraudulent conduct as Section 10(b) defendants. ¶¶ 297-309. Third, restrictions on Lewis's and Price's ability to sell or otherwise dispose of their BoA holdings, including likely restrictions that were in place during the course of the merger transaction, cause their interests to diverge from those of other BoA shareholders and investors, who could have acted on the material information that Lewis and Price concealed. As a result, Lewis's and Price's BoA holdings should not, as they suggest, create an inference that their interests were aligned with those of other BoA shareholders and investors.

merger-killing "day of reckoning" (*id.*), as it ensured that the merger's consummation would not be disrupted by public disclosure of the bailout.

Moreover, while Lead Plaintiffs have alleged that Lewis and Price were motivated to conceal the taxpayer bailout from investors, under clear Second Circuit precedent, they need not plead any motive to adequately plead scienter. *See, e.g.*, *Ganino*, 228 F.3d at 168-69 (holding that scienter can be established "either (a) by alleging facts to show that defendants had both motive and opportunity to commit fraud, or (b) by alleging facts that constitute strong circumstantial evidence of conscious misbehavior or recklessness") (internal quotation marks and citation omitted); *Slayton v. Am. Express Co.*, 604 F.3d 758, 776 (2d Cir. 2010) (noting that "the absence of a motive allegation is not fatal" to establishing a strong inference of scienter) (citing *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 325 (2007)).

Viewed collectively, as they must be, these facts raise a strong and compelling inference that Lewis and Price believed that disclosing the bailout would derail the merger, and intentionally concealed it in order to ensure that the merger closed without incident.

Lastly, the Bank Defendants now contend, for the first time, that even if disclosure of the bailout was required by Item 1.01 of Form 8-K, SEC regulations provide that the "failure to file a report on Form 8-K that is required solely pursuant to Item 1.01" cannot give rise to a violation of Section 10(b). *See* Def. Mem. at 41 (citing 17 C.F.R. § 240.13a-11(c)). The Bank Defendants failed to raise this argument previously. In any event, this argument is unavailing because, as the Court recognized in holding that Lewis and Price were required to disclose the bailout "under Section 10(b) and Rule 10b-5," Plaintiffs do not solely rely on Item 1.01 of Form 8-K as the basis for Lewis's and Price's duty to disclose the bailout. *Bank of America Corp.*, 2010 WL 3448194, at *43; *see also* Additional Form 8-K Disclosure Requirements and Acceleration of Filing Date, 69 FR 15594-01, 15607 (Mar. 25, 2004) ("[I]f the company has a duty to disclose information that is the subject of any of the Form 8-K items

covered by the safe harbor for any reason apart from the Form 8-K requirement, the safe harbor will not provide protection from Section 10(b) and Rule 10b-5 that may arise from the company's failure to satisfy such separate disclosure obligation."). It is well-established in the Second Circuit that where, as here, "a corporation is pursuing a specific business goal and announces that goal as well as an intended approach for reaching it," Section 10(b) and Rule 10b-5 impose an independent "obligation to disclose other approaches to reaching the goal when those approaches are under active and serious consideration." *In re Time Warner, Inc. Sec. Litig.*, 9 F.3d 259, 268 (2d. Cir. 1993). Defendants' duty to disclose the taxpayer bailout under Section 10(b) is thus clear, as the Court has already found. Not only did the bailout represent a material change in BoA's "intended approach for" accomplishing the merger, but this undisclosed material information fundamentally modified the terms of the merger by altering the way in which BoA financed its acquisition of Merrill and transforming the combined company into a ward of the state – information that was highly material to investors purchasing BoA securities in the open market.

VI. Defendants' Failure To Disclose Merrill's Fourth Quarter Losses Is An Actionable Material Omission Under Section 10(b)

The SAC amply alleges material omissions in violation of Section 10(b) and Rule 10b-5 with respect to Merrill's fourth quarter 2008 losses. The Court has already considered and rejected the Bank Defendants' contention that the failure to disclose Merrill's losses was not an "actionable omission" under Section 10(b). Def. Mem. at 34-41. In its August 27 Opinion, the Court denied "defendants' motions to dismiss Securities Plaintiffs' '34 Act claims, to the extent that they are premised on a failure to disclose Merrill's losses of October and November 2008[.]" *Bank of America Corp.*, 2010 WL 3448194, at *34. The Court again rejected the Bank Defendants' "revisit[ed] arguments" that they did not have a duty to disclose Merrill's losses in its October 8 decision denying the Bank Defendants' motion for certification for interlocutory appeal. *In re Bank of America Corp. Sec., Deriv. & ERISA Litig.*, No. 09 MD 2058 (PKC), 2010 WL 4237304, at *2 (S.D.N.Y. Oct. 8, 2010). In so doing, the

Court made clear that the "August 27 Opinion thoroughly aired this issue." *Id.* ("[D]efendants revisit arguments as to whether plaintiffs adequately pleaded an obligation to provide intra-quarter updates beyond the required SEC Form 10-Q filings. The August 27 Opinion thoroughly aired this issue.").[43] For this reason alone, the Bank Defendants' <u>third</u> attempt to litigate this issue – which they did not even raise in their November 18, 2010 pre-motion conference letter – should be rejected.[44]

Moreover, contrary to the Bank Defendants' argument that a violation of Section 14(a) cannot give rise to a violation of Section 10(b), the Second Circuit has made clear that a duty to disclose arises under Section 10(b) where another statute or SEC regulation requires such disclosure. *See In re Scholastic Corp. Sec. Litig.*, 252 F.3d 63, 70 (2d Cir. 2001) (reversing dismissal of Section 10(b) claim where defendants failed to disclose trend information required under Item 303 of Regulation S-K); *In re Ames Department Stores, Inc. Stock Litig.*, 991 F.2d 953, 963 (2d Cir. 1993) (holding that a disclosure violation in a registration statement under Section 11 of the Securities Act for one class of an issuer's securities may give rise to a Section 10(b) claim by open-market purchasers of the same issuer's other publicly traded securities); *Glazer v. Formica Corp.*, 964 F.2d 149, 157 (2d Cir. 1992) (an affirmative duty to disclose under Section 10(b) may arise, *inter alia*, when a statute requires disclosure) (citing *Roeder v. Alpha Indus., Inc.*, 814 F.2d 22, 26 (1st Cir. 1987)). Other Circuit courts, as well as courts in this District, are in accord. *See, e.g.*, *In re Digital Island Sec. Litig.,* 357 F.3d 322, 329 n.10 (3d Cir. 2004) (under Section 10(b) and Rule 10b-5, "[a] duty to affirmatively disclose may arise when there is . . . a statute requiring disclosure") (internal quotation marks omitted); *In re NTL, Inc. Sec. Litig.*, 347 F. Supp. 2d 15, 37 (S.D.N.Y. 2004) ("[A] violation of Item 303 [of Regulation S-

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[43] The parties extensively briefed Defendants' duty to disclose Merrill's losses in connection with the motions to dismiss the AC and Defendants' request for interlocutory appeal. *See, e.g.*, Defs.' Mem. Supp. Mot. Dismiss Consolidated Am. Compl. (Dkt. No. 65), at 34-38, 48, 49; Pls.' Opp'n (Dkt. No. 135), at 37-42, 69-75; Defs.' Reply Mem. (Dkt. No. 165), at 24-30; Defs.' Mem. Supp. Interlocutory Appeal (Dkt. No. 309), at 7-12; Pls.' Opp'n Interlocutory Appeal (Dkt. No. 335), at 9-16.

[44] The Bank Defendants' contention that they did not have to disclose Merrill's fourth quarter losses because there was purportedly no "fundamental change" in Merrill's financial condition (Def. Mem. at 2-3) ignores the Court's prior decisions, which held that Defendants had a duty to disclose all material information to shareholders prior to the shareholder vote, and in any event, raises an issue of fact. *See Bank of America Corp.*, 2010 WL 3448194, at *19, 34.

K], in some circumstances, may give rise to a claim under Section 10(b) of the Exchange Act[.]").

Indeed, the Second Circuit and courts in this District have long made clear that material misstatements and omissions in a proxy statement violating Section 14(a) are actionable under Section 10(b) as well, as long as scienter is adequately pled. *See, e.g.*, *Wilson*, 855 F.2d at 991; *Shore v. Parklane Hosiery Co., Inc.*, 565 F.2d 815, 816-17 (2d Cir. 1977), *aff'd Parklane Hosiery Co., Inc. v. Shore*, 435 U.S. 1006 (1979); *SEC v. Parklane Hosiery Co., Inc.*, 558 F.2d 1083, 1085 (2d Cir. 1977); *Schlick v. Penn-Dixie Cement Corp.*, 507 F.2d 374, 380 (2d Cir. 1974); *In re AOL Time Warner, Inc. Sec. and "ERISA" Litig.*, 381 F. Supp. 2d 192, 204-05 (S.D.N.Y. 2004). Though this precedent is noticeably absent from the Bank Defendants' motion, even they concede (in a footnote) that "[c]ourts have permitted Section 10(b) claims when a proxy statement, at the time issued, was false and misleading." Def. Mem. at 39 n.70.[45] Consequently, the Bank Defendants' contention that the SAC does not allege an actionable omission is without merit.

Ignoring this precedent, and citing no authority in support of their contention, the Bank Defendants assert three policy arguments why the Court should not "bootstrap" an actionable omission under Section 10(b) onto the violation of a disclosure duty under Section 14(a). Def. Mem. at 38-41. These policy arguments are irrelevant given the Court's holding in this case and the precedent in this Circuit. But even if they were considered, these policy arguments are fundamentally flawed. First, contrary to the Bank Defendants' claim that it would be "inconsistent with the structure of the federal securities laws" to find their failure to disclose Merrill's losses actionable under Section 10(b), it is well-settled that the securities laws were enacted by Congress "to substitute a philosophy of full disclosure for the philosophy of caveat emptor and thus to achieve a high standard of business ethics in the securities industry." *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 151 (1972)

[45] As set forth above at p. 10 n.5, Defendants' contention that they did not know of Merrill's losses at the time the Proxy was issued is wrong. The SAC alleges that Lewis and Price knew of Merrill's October losses by the time the Proxy was issued, and the Court concluded (based on those unchanged allegations) that Merrill's losses were known by the time the Joint Proxy issued. *Bank of America Corp.*, 2010 WL 3448194, at *33.

(internal quotation marks and citations omitted).

Second, the Bank Defendants' contention that finding an actionable omission under Section 10(b) would create "intractable" problems of administration requiring endless interim financial disclosures is meritless. As this Court recognized in denying Defendants' prior motions to dismiss Lead Plaintiffs' "'34 Act claims, to the extent that they are premised on a failure to disclose Merrill's losses of October and November 2008," the law in the Second Circuit is well-settled that issuers are required to update a proxy before the vote to disclose material intervening events that have occurred since the proxy's issuance. *Bank of America Corp.*, 2010 WL 3448194, at *34; *see also Gerstle v. Gamble-Skogmo, Inc.*, 478 F.2d 1281, 1297 n.15 (2d Cir. 1973) (Friendly, C.J.) ("[W]e cannot suppose that management can lawfully sit by and allow shareholders to approve corporate action on the basis of a proxy statement without disclosing facts arising since its dissemination if these are so significant as to make it materially misleading, and we have no doubt that Rule 14a-9 is broad enough to impose liability for non-disclosure in this situation."). The existence of this clear obligation is further demonstrated by the fact that Defendants themselves updated the Proxy on two occasions before the vote in order to disclose events far less material than Merrill's losses. ¶¶136-37, 237. The actions of BoA's own lawyers – who advised that BoA was required to make a supplemental disclosure of Merrill's October losses no later than one week before the shareholder vote – also demonstrate the existence of this well-established duty. ¶109. Moreover, contrary to the Bank Defendants' contention that, under Section 14(a), disclosure need only be made at "some time prior to the vote" (Def. Mem. at 38-39), the Second Circuit has made clear that material information that becomes known after the issuance of a proxy should be disclosed immediately. *See Wilson*, 855 F.2d at 992 (Section 14(a) requires that management inform stockholders "immediately" once a significant development occurs).

Third, the Bank Defendants' contention that finding an actionable omission under Section 10(b) would create a risk of inconsistent recovery because the Bank could simultaneously be the victim in a

derivative Section 14(a) action and the perpetrator of a Section 10(b) fraud is meritless. As the Court has already held, Section 14(a) provides for both direct and derivative claims (*J.I. Case Co. v. Borak*, 377 U.S. 426, 431 (1964)), and "it is possible for both sets of plaintiffs to prevail without double recovery." *Bank of America Corp.*, 2010 WL 3448194, at *20. Hence, there is no reason why a Section 10(b) claim would create any risk of inconsistent recovery. For all these reasons, Lewis's and Price's failure to disclose Merrill's losses is also actionable under Section 10(b).

VII. Plaintiffs Have Standing To Assert Claims With Respect To Preferred Shares, Debt Securities, And Options

In the SAC, Lead Plaintiffs added Section 10(b) claims for investors who purchased or acquired certain BoA preferred securities, debt securities or call options, or who sold put options, during the Class Period.[46] Lead Plaintiffs also left intact and unchanged their Section 14(a) claim on behalf of holders of Series B preferred shares as of the record date who were entitled to vote on the merger. Defendants assert that Plaintiffs lack constitutional standing to bring Section 10(b) or Section 14(a) claims in connection with securities that Plaintiffs did not themselves purchase or hold (or sell in the case of put options). *See* Def. Mem. at 47-50. However, the AC originally asserted Section 10(b) claims in connection with numerous preferred securities that Lead Plaintiffs had not purchased, as well as a Section 14(a) claim in connection with the Series B preferred shares, which Lead Plaintiffs also did not own. *See* ¶¶1, 279, 288, 303, 327 and Appendix A of the AC. Defendants did not challenge Lead Plaintiffs' standing to bring these claims in their motions to dismiss the AC, presumably recognizing that their arguments are meritless. Indeed, federal courts have routinely rejected Defendants' argument.

Federal courts routinely hold that where, as here, claims are based on the same misleading statements and legal theory, all securities purchasers share a common injury that stems from the exact same conduct. Thus, a plaintiff who has purchased one type of security has constitutional standing to

[46] In addition, Lead Plaintiffs added a named plaintiff, Grant Mitchell, who purchased call options during the Class Period (Lead Plaintiffs and Mitchell together are hereinafter referred to as "Plaintiffs").

assert claims on behalf of purchasers of all affected securities. *See, e.g.*, *In re American Int'l Group, Inc. Sec. Litig.*, 265 F.R.D. 157, 167 (S.D.N.Y. 2010) ("*AIG*") (finding standing to bring Section 10(b) claims for bonds not purchased by plaintiffs because such claims are based on the same legal theory as the Section 10(b) stock claims and rely on the same material misstatements); *In re Dynex Capital, Inc. Sec. Litig.*, No. 05 Civ. 1897 (HB), 2009 WL 3380621, at *18 (S.D.N.Y. Oct. 19, 2009) (finding standing to bring claims regarding bonds plaintiffs did not purchase "because they allege that Defendants made the exact same misrepresentations with respect to" all securities); *Teamsters Local 445 Freight Div. Pension Fund v. Bombardier Inc.*, No. 05 Civ. 1898 (SAS), 2005 WL 2148919, at *7-8 (S.D.N.Y. Sept. 6, 2005) ("[P]laintiff has standing to represent a [Section 10(b)] class of all purchasers who relied on the same . . . material misstatements and thus suffered the same injury when the value of their securities declined.").[47]

The court's decision in *AIG* is on-point and illustrative. In *AIG*, plaintiffs brought Section 10(b) claims on AIG common stock, which they purchased, and two AIG bond offerings that plaintiffs did not purchase. *See* 265 F.R.D. at 164-66. The Court rejected the same argument that Defendants raise here and found that plaintiffs did have standing to bring Section 10(b) claims related to the bonds they did not own because "the claim is brought under the same legal theory as the remaining [Section] 10(b) and Rule 10b[-5] claims, and relies on many of the same material misstatements from AIG's public financial statements." *Id.* at 167. Like in *AIG*, the claims relating to the BoA preferred securities, debt securities and options rely on the same legal theories and factual allegations as the analogous claims for

[47] *See also In re Fleming Cos. Inc. Sec. & Deriv. Litig.*, No. Civ. A 503 MD 1530 TJW, 2004 WL 5278716, at *37 n.7 (E.D. Tex. June 16, 2004) ("At the pleading stage, Lead Plaintiff . . . has standing to assert a section 10(b) claim on behalf of purchasers of all securities [including bonds not purchased by Lead Plaintiff] . . . because the various purchasers' claims arise out of the same material misstatements."); *In re MobileMedia Sec. Litig.*, 28 F. Supp. 2d 901, 911 n.7 (D.N.J. 1998) (plaintiff who purchased equities had standing to bring claims on behalf of bondholders); *Endo v. Albertine*, 147 F.R.D. 164, 167 (N.D. Ill. 1993) ("[A] class of plaintiffs who purchased different types of securities may properly be certified with a representative party who only purchased one type of security."); *Tolan v. Computervision Corp.*, 696 F. Supp. 771, 775 (D. Mass. 1988) ("Put and call option trading on an underlying security is directly affected by the prospecti, representations and omissions of the issuer of the underlying security."); *In re Saxon Sec. Litig.*, No. 82 Civ. 3103, 1984 WL 2399, at *7 (S.D.N.Y. Feb. 23, 1984) ("[D]ebenture holders have an interest identical to that of the holders of common stock in demonstrating a common course of fraudulent conduct.").

common stock purchasers.

Defendants do not dispute that Plaintiffs have standing to bring Section 10(b) claims on behalf of common stock purchasers, purchasers of the single series of debt security purchased by Ohio PERS, and purchasers of options callable in January 2011. Moreover, there can be no dispute that the harm to purchasers of all BoA securities identified in the SAC stems from the same improper conduct alleged in the SAC. The Section 10(b) claims concerning the preferred securities, debt securities and options do not differ from the Section 10(b) claims brought on behalf of common stock purchasers; they are based on the same facts and same legal theory.[48] Accordingly, as the authorities cited above make clear, Lead Plaintiffs share a common injury with purchasers of all BoA securities identified in the SAC, and thus have constitutional standing to assert Section 10(b) claims on their behalf.

Just as there is no requirement that a plaintiff must have purchased each and every security on which it asserts a Section 10(b) claim, there is no such requirement for Section 14(a) claims either. The Section 14(a) claim on behalf of the Series B preferred stock holders on the Record Date is identical to that of BoA common stock holders. Further, the only standing requirement courts have recognized for Section 14(a) claims is that the plaintiff must have been entitled to vote on the merger. *See In re AOL Time Warner, Inc. Sec. & ERISA Litig.*, 381 F. Supp. 2d 192, 241 (S.D.N.Y. 2004); *see also United Paperworkers Int'l Union v. Int'l Paper Co.*, 985 F.2d 1190, 1197-98 (2d Cir. 1993) ("The SEC … promulgated Rule 14a-9 with the goal of preserving <u>for all shareholders who were entitled to vote</u> … the right to make decisions based on information that is not false or misleading."); *7547 Corp. v. Parker & Parsley Dev. Partners, L.P.*, 38 F.3d 211, 229 (5th Cir. 1994) ("We view Section 14(a) as protecting only interest-holders with voting rights."). Notably, Defendants have not cited a single case holding that any other Section 14(a) standing requirement exists. Lead Plaintiffs, as owners of BoA common stock on the Record Date, were indisputably entitled to vote on the merger, and thus have standing to

[48] In fact, all of these securities are encompassed in a single count and rely on the same misstatements and omissions and allegations of scienter. *See* ¶¶297-309.

assert a Section 14(a) claim on behalf of the similarly situated Series B preferred shareholders.[49]

Defendants' remaining arguments are misplaced. While Defendants contend that Lead Plaintiffs' transactions in certain preferred and debt securities do not demonstrate loss causation (*see* Def. Mem. at 47, 50), this argument is irrelevant. As set forth above, as purchasers of BoA common stock (among other securities), Lead Plaintiffs have standing to bring Section 10(b) claims in connection with BoA's preferred and debt securities <u>that were affected by the same misconduct</u>.[50]

In support of their arguments that Plaintiffs lack standing, Defendants primarily rely on cases involving mutual funds. These cases are inapposite because, at their core, they do not involve a common course of conduct that amounted to a fraud-on-the-market for all of the issuer's securities. Rather, the plaintiffs in those cases were found to lack standing for claims related to separate funds in which they had not purchased because each mutual fund is considered to be a different legal entity. Thus, in those cases, unlike here, the representative plaintiffs could not demonstrate that the class they sought to represent relied on the same set of false statements and omissions, facts and legal theory. For those reasons, unlike here, no common injury existed.[51]

In sum, as federal courts have regularly found, plaintiffs are not required to have purchased each and every security to have standing to represent purchasers of those securities so long as the facts and claims are identical, and the representative plaintiff has a case or controversy against each

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[49] Defendants mistakenly suggest that Lead Plaintiffs have asserted Section 14(a) claims on behalf of holders of all the preferred securities identified in the SAC. The SAC specifically alleges that these claims are asserted only on behalf of holders of BoA common stock and Series B preferred shares as of the Record Date who were entitled to vote on the merger. *See* ¶332. Thus, Defendants' argument that holders of the Series K preferred security lacked voting rights (*see* Def. Mem. at 48) is irrelevant, as Lead Plaintiffs do not assert a Section 14(a) claim for Series K shares. *See* ¶332.

[50] In their certifications, Lead Plaintiffs set forth their transactions in securities they sold before any corrective disclosures occurred only because the PSLRA requires Lead Plaintiffs to disclose all transactions in securities that are the subject of the SAC, not because Lead Plaintiffs were claiming that these transactions demonstrated that they had suffered losses in all identified BoA securities.

[51] *See Hoffman v. UBS-AG*, 591 F. Supp. 2d 522 (S.D.N.Y. 2008); *In re AIG Advisor Grp. Sec. Litig.*, No. 06 Civ. 1625 (JG), 2007 WL 1213395 (E.D.N.Y. Apr. 25, 2007); *In re Salomon Smith Barney Mut. Fund Fees Litig.*, 441 F. Supp. 2d 579 (S.D.N.Y. 2006); *In re Merrill Lynch Inv. Mgmt. Funds Sec. Litig.*, 434 F. Supp. 2d 233 (S.D.N.Y. 2006); *In re AllianceBernstein Mut. Fund Excessive Fee Litig.*, No. 04 Civ. 4885 (SWK), 2005 WL 2677753 (S.D.N.Y. Oct. 19, 2005); *Nenni v. Dean Witter Reynolds, Inc.*, No. Civ. A 98-12454-REK, 1999 WL 34801540 (D. Mass. Sept. 29, 1999).

defendant. Accordingly, Plaintiffs have constitutional standing here to allege claims on behalf of each of the securities at issue in the SAC, and Defendants' arguments should be rejected.

VIII. Conclusion

For the reasons set forth above, Defendants' motions to dismiss the SAC should be denied in their entirety.

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