

United States District Court, D. New Jersey.
In re LUCENT TECHNOLOGIES, INC., Securities Litigation.
Case No. 00 CV 621 (ALJ).
November 3, 2000.

Consolidated and Amended Class Action Complaint

Plaintiff, Teamsters Locals 175 & 505 D&P Pension Trust Fund (the "Pension Trust Fund" or "Lead Plaintiff"), whose address is 4815 Maccorkle Avenue SE, Charleston, West Virginia 25304, alleges the following against Defendants, whose address is 600 Mountain Avenue, Murray Hill, New Jersey 07974.

INTRODUCTION

Lead Plaintiff, by its undersigned attorneys, on behalf of itself, the other plaintiffs in this litigation, and the Class it seeks to represent, for its Consolidated and Amended Class Action Complaint, makes the following allegations, based upon the investigation conducted by, and under the supervision of, its counsel, which investigation included the review and analysis of information related to the relevant time period, including, *inter alia*, United States Securities and Exchange Commission ("SEC") filings by Lucent Technologies, Inc. ("Lucent" or the "Company"), press releases, news articles, and other media reports (including those disseminated in print and by electronic media), reports of securities analysts and investor advisory services, and interviews with numerous former employees of Lucent. Except as alleged herein, the underlying information concerning Defendants' misconduct and the particulars thereof are not available to Plaintiff and the public and lie within the possession and control of Defendants and other Lucent insiders. Accordingly, Lead Plaintiff believes that additional substantial evidentiary support will exist for the allegations set forth herein after a reasonable opportunity for discovery.

NATURE OF THE ACTION

1. This is a class action on behalf of all purchasers of the common stock of Lucent between October 26, 1999, and January 6, 2000, inclusive (the "Class Period"), seeking to pursue remedies under the Securities Exchange Act of 1934 (the "Exchange Act").
2. This case arises from Defendants' efforts to conceal from the investing public the fact that Lucent was experiencing pervasive and material difficulties which were adversely impacting its revenues and profits, as well as its relationships with clients and customers.
3. A 1996 spin off from AT&T, Lucent had been endowed at its inception with a dominant position in the market for telecommunications equipment. By mid-1999, however, Lucent had squandered that advantage. As the telecommunications industry shifted from transmission of voice to data, new technologies and products developed and new entrants into the market place began to compete with Lucent. Lucent represented that

it was at the forefront of competition in these new arenas and publicly projected continuing dramatic growth. However, the true situation at Lucent belied Defendants' representations.

4. By the beginning of the Class Period, senior management knew that the Company was confronting severe but undisclosed problems. First, it had fallen seriously behind in the development of OC-192 -- the optical networking system that had become the product of choice for Lucent's potential customers. Second, it was widely recognized within Lucent that its cost structure made it difficult, if not impossible, to sell its products at competitive prices. Third, because it had resisted outsourcing the manufacture of component parts for many of its products, in certain areas of critical importance it had lost the ability to obtain needed parts in sufficient quantities to meet production schedules or delivery requirements. Fourth, problems of product design, reliability and timeliness of deliveries were widespread, causing customer dissatisfaction and withdrawal of orders. Fifth, problems developed with AT&T, its most important customer, stemming from Lucent's unwillingness to manufacture to AT&T's specifications, AT&T's desire to diversify its sources of supply, and Lucent's inability to adequately develop major new products as rapidly as its competitors. Sixth, demand was declining for its important power switch product line, and major new products in the wireless, software, and other areas proved to be disappointments. Sixth, internal control, financial accounting, and information systems were grossly deficient, making it impossible to understand and evaluate important aspects of what was happening in the Company.

5. In addition, the accounts receivable situation at the Company was out of control, with hundreds of millions, if not billions, of dollars of receivables going uncollected but remaining on the books for long periods of time, in part because those receivables represented phony sales that never should have been booked, in part because Lucent's collection people were too poorly trained to understand how to deal with the issues being raised by the customers, and in part to avoid the adverse impact on Lucent's financial statements from making a serious effort to write off uncollectible receivables.

6. By the fall of 1999, Lucent had purportedly met or exceeded analysts' expectations (which reflected the "guidance" regularly provided by Lucent management) for fourteen straight quarters. By the beginning of the Class Period, however, Lucent's management knew that the heady growth it had regularly announced was diminishing, and that it was confronting the very serious problems described above.

7. Indeed, by the beginning of October 1999, Lucent senior executives had informed Defendant McGinn, Lucent's President, Chief Executive Officer and Chairman that Lucent needed to drastically reduce the projections of revenue and profit it was providing to the analyst community because important new products were not ready for sale and sales of older products were in decline. McGinn refused, and Lucent failed to cut back its aggressive public guidance to reflect these realities.

8. Instead, prior to and during the Class Period, Defendants took various steps to conceal the eroding nature of Lucent's business from the investing public. Among other things,

Defendants misrepresented the demand for the Company's optical networking products -- an area of crucial importance to the investing public -- without disclosing the knowledge of Lucent's senior *management that demand had* shifted dramatically away from the optical networking products Lucent was actually able to ship, and had moved to an optical networking system (OC-192) that Lucent had delayed developing and would not be able to ship in volume for many months. Defendants knew that as a result, potential customers were deserting Lucent and buying from companies (such as Nortel) that were already shipping OC-192 product.

9. Defendant also made a policy decision to artificially inflate reported sales by shipping product that was not yet ready for delivery. In September 1999 Lucent's senior management told the Company's directors at a meeting in Nuremberg, Germany that Lucent's strategy was to ship products notwithstanding design and technical problems, and to solve those problems later. Although that decision was designed to increase reported sales, it exacerbated an existing problem of poor product quality, which had a further adverse impact on customer acceptance and sales.

10. Third, during the summer of 1999 and thereafter, Lucent management was aware of, and condoned, a widespread practice among Lucent sales personnel of artificially inflating sales figures in order to meet the sales quotas established for them by management, particularly at the end of each fiscal quarter. Sales revenue was booked even though the customer had not yet agreed to the sale, channels were "stuffed" by strong-arming distributors to take product they did not yet want on the understanding that the product would sit in a warehouse and could ultimately be returned, and other devices were used to effectuate recognition of revenue prematurely. As a result, the investing public was misled as to Lucent's success in growing revenues and meeting its public guidance.

11. Finally, in full recognition of the massive problem of uncollectible accounts receivable at Lucent, Defendants allowed, at a minimum, hundreds of millions of dollars of worthless accounts receivable to remain on the books in order to avoid making a charge against earnings in connection with major accounts receivable write off.

12. As alleged in detail below, senior management at Lucent engaged in conscious, or at least reckless wrongdoing by participating in the reported dissemination of public statements that misrepresented and concealed true facts concerning major problems afflicting Lucent. Furthermore, they had strong reasons why it would be in their interests to artificially inflate the market price of Lucent stock. Lucent was engaged in an aggressive program of acquiring companies using Lucent shares as a major component in making those purchases. The higher the price of the stock, the cheaper the purchase from Defendants' point of view. In addition, Defendant Peterson, together with many other Lucent officers, cashed in on the inflated value of Lucent shares by selling them for aggregate proceeds of approximately \$26.8 million.

13. Despite Defendants' scheme to conceal the deteriorating nature of Lucent's business from the investing public, on January 6, 2000 these problems caused Lucent to announce

that the Company's revenues were not increasing as the Defendants had assured the market but rather the Company's results for the first fiscal quarter of 2000 would fall materially short of analysts expectations for reasons which included a disappointing performance with respect to optical networking. According to the release, the Company announced that it would report quarterly and yearly earnings of only \$0.36 per share and \$1.40 per share. In response to the Company's shocking disclosure, on January 6, 2000, Lucent's share price plunged more than 27% or \$20 per share to \$52.19 a share.

JURISDICTION AND VENUE

14. The claims asserted herein arise under and pursuant to Sections 10(b) and 20(a) of the Exchange Act [[15 U.S.C. §§ 78j\(b\)](#) and [78t\(a\)](#)] and Rule 10b-5 promulgated thereunder by the Securities and Exchange Commission ("SEC") [[17 C.F.R. § 240.10b-5](#)].

15. This Court has jurisdiction over the subject matter of this action pursuant to [28 U.S.C. §§ 1331](#) and [1337](#) and Section 27 of the Exchange Act [[15 U.S.C. § 78aa](#)].

16. Venue is proper in this District pursuant to Section 27 of the Exchange Act, and [28 U.S.C. § 1391\(b\)](#). Many of the acts charged herein, including the preparation and dissemination of materially false and misleading information, occurred in substantial part in this District. Additionally, Defendants maintain their chief executive offices and principal place of business within this District.

17. In connection with the acts alleged in this complaint, Defendants, directly or indirectly, used the means and instrumentalities of interstate commerce, including, but not limited to, the mails, interstate telephone communications and the facilities of the national securities markets.

PARTIES

18. By order of the Court dated April 26, 2000, the Pension Trust Fund was provisionally appointed Lead Plaintiff. The Lead Plaintiff purchased the common stock of Lucent at artificially inflated prices during the Class Period and has been damaged thereby. The Lead Plaintiff has previously filed a certification with the Court authorizing its participation in this action as mandated by Section 21D(a)(2)(A) of the Exchange Act.

19. The names of all plaintiffs named in the actions consolidated by the Court's February 25, 2000 Order are hereby incorporated by reference as additional plaintiffs in this action. They have also previously filed their certifications authorizing their participation.

20. Defendant Lucent Technologies, Inc., is a Delaware corporation with its principal place of business and chief executive offices located at 600 Mountain Avenue, Murray

Hill, New Jersey 07974. According to the Company's press releases, Lucent purports to be a leading designer, builder and installer of a wide range of public and private networks, communications systems and software, data networking systems, business telephone systems and microelectronics components; including the manufacture of integrated circuits and optoelectronic components for the computer and telecommunications industries.

21. The following Defendants collectively referred to as the "Individual Defendants" at all times relevant to this action, served in the capacities listed below and received substantial compensation related thereto:

(a) Defendant Richard A. McGinn ("McGinn") served as Lucent's President, Chief Executive officer and Chairman of its Board of Directors. McGinn served as an executive officer of the Company from February, 1996, until he was fired by the Company's Board of Directors on October 22, 2000. McGinn signed the Company's 1999 Annual Report on Form 10-K (the "1999 10-K"). During the Class Period, McGinn was quoted frequently in the news media and in press releases and other publicly disseminated materials.

(b) Donald K. Peterson ("Peterson") served as Lucent's Chief Financial Officer, and Executive Vice President. McGinn has served as an executive officer of the Company since February, 1996. Peterson signed the Company's 1999 Annual Report on Form 10-K (the "1999 10-K"). During the Class Period, Defendant Peterson realized more than \$5.4 million in proceeds from sales of his personal holdings of Lucent shares.

22. Because of the Individual Defendants' positions with the Company, they had access to the adverse undisclosed information about its business, operations, products, operational trends, financial statements, markets and present and future business prospects via access to internal corporate documents (including the Company's operating plans, budgets and forecasts and reports of actual operations compared thereto), conversations and connections with other corporate officers and employees, attendance at management and Board of Directors meetings and committees thereof and via reports and other information provided to them in connection therewith.

23. It is appropriate to treat the Individual Defendants as a group for pleading purposes and to presume that the false, misleading and incomplete information conveyed in the Company's public filings, press releases and other publications as alleged herein are the collective actions of the narrowly defined group of defendants identified above. Each of the above officers of Lucent, by virtue of their high-level positions with the Company, directly participated in the management of the Company, was directly involved in the day-to-day operations of the Company at the highest levels and was privy to confidential proprietary information concerning the Company and its business, operations, products, growth, financial statements, and financial condition, as alleged herein. Said Defendants were involved in drafting, producing, reviewing and/or disseminating the false and misleading statements and information alleged herein, participated in issuing "guidance" to securities analysts concerning Lucent, were aware or recklessly disregarded that the

false and misleading statements were being issued regarding the Company, and approved or ratified these statements in violation of the federal securities laws.

24. As officers and controlling persons of a publicly-held company whose common stock was, and is, registered with the SEC pursuant to the Exchange Act, traded on the New York Stock Exchange (the "NYSE"), and governed by the provisions of the federal securities laws, the Individual Defendants each had a duty to disseminate promptly, accurate and truthful information with respect to the Company's financial condition and performance, growth, operations, financial statements, business, products, markets, management, earnings and present and future business prospects, and to correct any previously-issued statements that had become materially misleading or untrue, so that the market price of the Company's publicly-traded securities would be based upon truthful and accurate information. The Individual Defendants' misrepresentations and omissions during the Class Period violated these specific requirements and obligations.

25. The Individual Defendants participated in the drafting, preparation, *and/or* approval of the various public *and* shareholder and investor reports and other communications complained of herein and were aware of, or recklessly disregarded, the misstatements contained therein and omissions therefrom, and were aware of their materially false and misleading nature. Because of their Board membership and/or executive and managerial positions with Lucent, each of the Individual Defendants had access to the adverse undisclosed information about Lucent's business prospects and financial condition and performance as particularized herein and knew (or recklessly disregarded) that these adverse facts rendered the positive representations made by or about Lucent and its business issued or adopted by the Company materially false and misleading.

26. The Individual Defendants, because of their positions of control and authority as officers and/or directors of the Company, were able to and did control the content of the various SEC filings, press releases and other public statements pertaining to the Company during the Class Period. Each Individual Defendant was provided with copies of the documents alleged herein to be misleading prior to or shortly after their issuance and/or had the ability and/or opportunity to prevent their issuance or cause them to be corrected. Accordingly, each of the Individual Defendants is responsible for the accuracy of the public reports and releases detailed herein and is therefore primarily liable for the representations contained therein.

27. Each of the Defendants is liable as a participant in a fraudulent scheme and course of business that operated as a fraud or deceit on purchasers of Lucent common stock by disseminating materially false and misleading statements and/or concealing material adverse facts. The scheme: (i) deceived the investing public regarding the demand for Lucent's products, the competitiveness of its products, the revenues from Lucent's business and the intrinsic value of Lucent common stock; and (ii) caused plaintiff and other members of the Class to purchase Lucent common stock at artificially inflated prices.

PLAINTIFF'S CLASS ACTION ALLEGATIONS

28. Plaintiff brings this action as a class action pursuant to [Federal Rule of Civil Procedure 23\(a\) and \(b\)\(3\)](#) on behalf of a Class, consisting of all persons who purchased Lucent common stock between October 26, 1999, and January 6, 2000, inclusive (the "Class Period") and who were damaged thereby. Excluded from the Class are Defendants, the officers and directors of the Company, at all relevant times, members of their immediate families and their legal representatives, heirs, successors or assigns and any entity in which Defendants have or had a controlling interest.

29. The members of the Class are so numerous that joinder of all members is impracticable. Throughout the Class Period, Lucent common shares were actively traded on the NYSE. As of November 30, 1999, there were approximately 3,141 million shares of Lucent common stock *issued and outstanding*. While the exact number of Class members is unknown to plaintiff at this time and can only be ascertained through appropriate discovery, plaintiff believes that there are thousands of members in the proposed Class. Record owners and other members of the Class may be identified from records maintained by Lucent or its transfer agent and may be notified of the pendency of this action by mail, using the form of notice similar to that customarily used in securities class actions.

30. Plaintiff's claims are typical of the claims of the members of the Class as all members of the Class are similarly affected by Defendants' wrongful conduct in violation of federal law that is complained of herein.

31. Plaintiff will fairly and adequately protect the interests of the members of the Class and has retained counsel competent and experienced in class and securities litigation.

32. Common questions of law and fact exist as to all members of the Class and predominate over any questions solely affecting individual members of the Class. Among the questions of law and fact common to the Class are:

(a) whether the federal securities laws were violated by Defendants' acts as alleged herein;

(b) whether statements made by Defendants to the investing public during the Class Period misrepresented material facts about the business operations, financial statements of Lucent; and

(c) to what extent the members of the Class have sustained damages and the proper measure of damages.

33. A class action is superior to all other available methods for the fair and efficient adjudication of this controversy since joinder of all members is impracticable. Furthermore, as the damages suffered by individual Class members may be relatively small, the expense and burden of individual litigation make it impossible for members of

the Class to individually redress the wrongs done to them. There will be no difficulty in the management of this action as a class action.

SUBSTANTIVE ALLEGATIONS

Background Facts: Lucent's Business and Operations

34. Lucent's business consists of the design, and manufacture of telephone systems, telecommunications systems and software, data networking systems, and microelectronic components. Lucent conducts its research and development activities through Bell Laboratories. The Company or its predecessors have supplied products to virtually every local and long distance telephone company in the Country. Lucent's data networking and telecommunications equipment historically was based on copper wireline technology and switches which carried voice and data over electrical currents.

The Company

35. During the Class Period, the Company classified its business into three segments: Service Provider Networks ("SPN"), Enterprise Networks, and Microelectronics and Communications Technologies ("MCT").

36. The Service Provider Network segment includes the product groups responsible for Lucent's optical networking, switching solutions, wireless networking and software solutions. It also includes Lucent's data networking business for service provider customers. In the first quarter of 2000, the Company transferred its optic components business from its MCT segment to its Service Provider Networks segment.

37. The Enterprise segment included the Company's Business and Communication Systems ("BeC") division. BCS develops, sells and installs telephone and data networks for business customers. This segment was spun off from Lucent as Avaya Communications, ("Avaya") an \$8 billion company on October 2, 2000.

38. During the Class Period, Lucent's Microelectronics and Communications division designed and manufactured high performance integrated circuits, power systems, and optical components. On July 21, 2000, Lucent announced its plan to spin-off the MCT division in the first quarter of 2001.

Historical Background -- Lucent Inherits the Bell System Business

39. Until 1995, the telecommunications equipment businesses operated by Lucent during the Class Period were conducted by various subsidiaries and divisions of AT&T. Specifically, AT&T's Western Electric subsidiary served as AT&T's manufacturing arm and Bell Labs conducted its research and development activities. Until 1984, these Lucent predecessors were sister organizations of AT&T's wholly owned local telephone service providers collectively known as the Bell Operating Companies ("BOCs"). The

BOCs purchased substantially all of their telecommunications equipment from Western Electric and other Lucent predecessors.

40. In 1974, the federal government sued AT&T, Western Electric, and Bell Labs alleging that they had violated Section 2 of the Sherman Act ([15 U.S.C. §2](#)). The federal government alleged that the AT&T entities had monopolized the majority of the nation's markets for telecommunications equipment. Among other things, the federal government alleged that AT&T used its control of its BOCs in local service to monopolize and thwart competition in the (a) long distance telephone service market, and (b) the telecommunications equipments markets.

41. In 1982, after the District Court had denied AT&T's motion to dismiss, AT&T and the government agreed to settle the litigation by entry of a consent decree, now known as the Modified Final Judgment ("MFJ"). In approving the consent decree, Judge Harold Greene of the District of Columbia, noted that "the government alleged, and there was proof, that AT&T used its control over the local [BOCs] to force them to buy products from Western Electric, even though other equipment manufacturers produced better products or products of identical quality at lower prices." [United States v. AT&T, 552 F. Supp. 131, 163 \(D.D.C. 1982\)](#).

42. The MFJ prohibited the BOCs from discriminating in the procurement of products and services between AT&T and other telecommunications equipment suppliers.

43. Pursuant to the MFJ, AT&T divested the BOCs into seven Regional Bell Operating Companies (RBOCs) in 1984, leaving AT&T to consist of its long distance and telecommunications equipment businesses. However, as Judge Greene recognized, "the costs of entering the telecommunications business [was] still substantial" and "entrenched customer preferences in favor of AT&T" would not evaporate immediately but only diminish only over the long term, when more competitors emerged and such competitors were able to offer comparable or better products and services. [Id. 552 F. Supp. at 165-66, 172](#).

44. Accordingly, for many years after the implementation of the consent decree, AT&T continued to be the dominant provider of telecommunications equipment in the United States, because, among other reasons, the RBOCs had invested billions of dollars in networks built on Western Electric and other AT&T provided equipment. As a result, these customers were unlikely to jettison their investment by switching suppliers. Thus, despite the fact that other equipment manufacturers produced better products at lower prices, AT&T continued to have a captive market to whom they were able to charge non-competitive prices for telecommunications equipment.

Lucent is launched into a marketplace as the technology upon which its monopoly rests is becoming archaic.

45. On September 30, 1996, AT&T completed the spin-off of the telecommunications equipment portion of its business as Lucent. By the time of the spin-off, the market for

telecom-munications equipment was poised to undergo a sea change, as new wireless and optical technology were emerging which would eventually make Lucent's near monopoly power in the old electrical technology far less important. In this new world, if Lucent was to maintain its market share, Lucent would have to effectively develop and market the newer technology products by the time that customers began to demand them.

46. For nearly two years following Lucent's IPO, the Company was able to continue to generate strong sales of products to its historic customers, based on the inherited flow of business from AT&T. The Company became an investor favorite and the most widely-held stock in the United States. Lucent was followed by numerous analysts who favorably commented on the Company's potential.

47. However, behind the positive numbers, there were significant problems growing at Lucent which threatened the Company's ability to compete. According to public statements by ten individuals employed at Lucent's North Andover optical manufacturing facility during the relevant time --namely, Dan Tymann, a Manufacturing Director, Nathan Tyman, a Buyer at the facility, David B. Ashley, a Manufacturing Director, Karen M. Ashley a Senior Manager in Product Management, Vimalkumar J. Patel, a Test Development Engineer, Meredith A. Hatten, a 10G Program Manager or Customer Project Manager, Molly A. Broadley, a Project Manager, Brenda A. Conkel, a Material Allocation and Prioritization Manager, Michael A. Hickey, a member of the technical staff, and James F. Wholley, a Buyer at the facility (collectively, "the North Andover employees group"), Lucent's Bell Labs development unit, which had once been the an industry leader, had lost its technological prowess, and Lucent had fallen behind in the development of new telecommunications technology. Furthermore, it was widely recognized within Lucent that the Company had continual production problems with its products, and that the Company's products were much more expensive than those of their competitors.

48. By 1998 Lucent's traditional customers-- the RBOCs--were facing competition from start-up telecommunications service providers commonly called Competitive Local Exchange Carriers ("CLECs"). The CLECs were creating wireless and optical networks which could be built without Lucent's wireline based technology, and which were far faster and more efficient. As a result of the new competition in their marketplace, the RBOCs were becoming more interested in obtaining the most technologically advanced products available in order to compete.

49. Thus, Lucent was facing increasing demand for advanced technology just as it was becoming apparent to Defendants that Lucent lacked the ability to develop such technology in a timely or effective manner. As a result, Lucent was having increasing difficulty achieving the revenues that analysts were expecting.

50. In order to maintain the positive market response Lucent had enjoyed as a result of the sustained growth experienced by the Company in its first two years, despite the Company's problems, Defendants continued to issue rosy guidance for the Company, projecting increasing revenue growth.

PROBLEMS IN LUCENT'S OPTICAL NETWORKING BUSINESS

(a) Nature of the Optical Networking Business

51. Optical networking products are designed to increase capacity into Internet portals by using pulses of light to transmit millions of phone connections simultaneously through thin optical fibers, rather than the old generation copper wire infrastructure.

52. The primary customers for optical networking products are the RBOCs, CLECs, Internet service providers and major corporations.

53. Optical networking technology is in demand because customers want faster connections and because the volume of information flowing through public networks has nearly tripled in the past three years. In addition, over the next three years, the traffic is expected to increase tenfold. As a result, the market for optical networking equipment which was \$31 billion in 1999, is projected to triple to \$90 billion by 2003.

54. The demand for optical networking products is inversely related to the demand for Lucent's conventional large scale switching products. As regional telephone companies make the transition to optical networking, they will necessarily require less conventional copper wire electrical equipment. Thus, increases in optical networking products sales negatively impact Lucent, unless Lucent is the provider of the new technology.

55. The transmission capacity or bandwidth in optical networking technology has increased exponentially since the technology was introduced in 1995. Advances in optical networking products technology have impacted two aspects of the product, speed and capacity.

56. OC-192 is the fastest class of fiberoptic networking technology, and enables users to transmit 10-gigabits of data per second. OC-192 was developed by Nortel Networks in the mid-1990s. Before Nortel's development of OC-192, the standard of technology was OC-48 which transferred data at only 2.5 gigabits per second. OC-192 products are 400% faster and have 16 times the network capacity of 2.5 gigabit products. During the summer/fall of 1999, Lucent had 2.5 gigabit product line but was seriously behind in developing an OC-192 product that was ready for shipment.

57. Lucent's optical networking products were manufactured in its North Andover, Massachusetts facility. During the Class Period, these products consisted of the WaveStar family of products.

58. During the relevant time, Lucent's optical business was a material portion of Lucent's overall business, accounting for approximately 25% of Lucent's reported sales, according to an SG Cowen 10/99 report.

59. Analysts covering the Company viewed Lucent's optical networking division as a very important part of Lucent's future. For example, in a Credit Suisse First Boston analyst report issued in November 1999, James Parmelee described the Optical Networking Division as one of the Lucent's "key top-line catalysts" for Financial Year 2000.

(b) Problems in the Optical Networking Division

60. Although Nortel Networks installed its first OC-192 product in mid 1997, and was experiencing increasingly strong demand for the product, Lucent made a very bad strategic decision to postpone development of an OC-192 product. Specifically, in August of 1997 Defendant McGinn convened a secret meeting in Red Bank, New Jersey to discuss strategy for optical networking development. Thereafter, Lucent's senior management, including McGinn decided to cut spending on development of faster equipment in favor of developing a product with more capacity but far less speed than OC-192. Defendants apparently expected Lucent's customers to continue to purchase the Company's 2.5 gigabit product until Lucent's OC-192 product was ready at some future time, notwithstanding that Nortel was already shipping OC-192. Nortel's orders for OC-192 were significant. For example, Qwest (also a Lucent customer) ordered \$150 million in networking gear from Nortel in 1997, and \$600 million more in June of 1999.

61. By the Fall of 1999, although two years had passed since Nortel had introduced its product, Lucent was still attempting to sell its 2.5 gigabit product, and its OC-192 product was lagging in development. At the time of their original decision not to press ahead vigorously with OC-192, Defendants apparently misread the market and did not anticipate that customers, intent on keeping ahead of their competitors, would quickly shift their demand from the older 2.5 gigabit technology to OC-192 products. By the beginning of the Class Period, however, Defendants knew that they had made a major misjudgment, that demand for the 2.5 gigabit product had significantly diminished as the demand for OC-192 skyrocketed and that Lucent was losing business to its competitors who could offer OC-192.

62. Although Lucent's competitor Nortel had \$11.8 billion in outstanding orders as of the beginning of the Class Period, according to pleadings filed by the North Andover employees group, and according to other former optical networking group employees, Lucent was experiencing declining demand for its optical networking products.

63. At least from the summer of 1999 on production at Lucent's optical networking facility was very slow because of the lack of work. Machines often lay idle as employees sat on the production floor reading magazines.

64. According to knowledgeable persons including but not limited to the North Andover employees group, by the Summer of 1999, Lucent management was well aware that the Company was seriously behind in the development of an OC-192 product, and that potential customers were, in part, going elsewhere to buy OC-192, and in part withholding purchases from Lucent until its OC-192 product was ready. During and after

the Summer of 1999, these facts were discussed by optical networking personnel in meetings with Lucent senior management including Harry Bosco, the Group President for Optical Networking.

65. In addition, prior to and throughout the Class Period, Lucent had great difficulty meeting production and delivery schedules so as to satisfy even the diminished demand for its older generation DWDM and Wavestar products. For example, as alleged in more detail below, Lucent encountered problems with manufacturing its 2.5 gigabit products and had begun outsourcing some of its optical components requirements, but at least until March of 2000, Lucent did not have procedures in place to inspect the quality of the fiber optic components that were outsourced. As a result, Lucent experienced significant quality control problems and the 2.5 gigabit products that it manufactured often failed to work properly.

66. As a result, even with decreased demand, the Company was unable to meet its own timetable for production and shipment of its optical products. The majority of customers orders were shipped late. For example, Qwest Communications had placed a order for Lucent optical data networking gear product in July of 1999. However, by January of 2000, Qwest had ripped out the Lucent product because some components of the product came late, and others did not work at all. The employees involved in Lucent's optical networking WaveStar project openly discussed the fact that the 10G WaveStar product was not working properly and that deadlines were going to be delayed. This problem persisted far into the Class Period. For example, British Telecom had ordered a WaveStar product for December 1999, which was not shipped as scheduled.

PROBLEMS WITH NUMEROUS OTHER PRODUCTS

67. Lucent's product problems were not limited to the optical group. *By* at least mid-1999, and extending through the Class Period, the Company was having a great deal of difficulty meeting forecasts and sales projections with respect to its wireless products. For example, employees recognized that Lucent “fell flat on their face” with the product they were working on, the “Wireless Broadband.” This is a product Lucent management had claimed would be a big seller. The Wireless Broadband product which Lucent developed in-house was poorly received in the marketplace because, like its fateful decision regarding OC-192, the Company had made a strategic mistake in developing a product that did not have the features that customers were demanding. In order to finally bring a competitive product to market in April 2000, the Company had to buy a 30% share in TeraBeam, a company which had developed a competitive wireless broadband access product.

68. Nor were Lucent's Networking division's Software Group meeting that group's sales projections.

69. At least by the Fall of 1999, the Data Networking division was experiencing both production and demand problems. The Company was missing shipment and release dates for products sold within that division. One cause of that problem was the fact that Lucent's sales representatives were selling products which were still in the design phase. For example, in April, 1999, Lucent sales representatives were selling customers like GT Group Telecom a 7R/E voice switch which was still being designed. Although GT Group Telecom was a recipient of Lucent financing, it was free to buy its products from anywhere, and the company eventually decided to buy from another supplier which had product ready to ship. In addition, as a result of its inability to effectuate timely delivery of product, the Company lost a \$200 million "Internet Working Contract" to Nortel.

70. At the same time, Lucent's Power Supply Division was losing market share with its largest customer, AT&T, because Lucent's products did not meet AT&T's specifications. Lucent had over-designed the product with unnecessary functions, but failed to meet the customers specified requirements.

71. By the beginning of the Class Period, Lucent had lost two additional important contracts. Specifically, Lucent had lost a significant AT&T contract for telecommunications switches called 5ESS (Lucent's main product during 1999) to Nortel because AT&T wanted to expand its suppliers base of suppliers. In addition, by the fourth quarter of fiscal 1999, Lucent's Octel division (the voice messaging group) had lost to Ericsson a significant contract with the Saudi Arabian government. Lucent had secured the contract in the first or second quarter of 1999. The initial portion of the contract was valued at \$600 million, but the entire value of the activity contemplated -- and lost -- was \$6 billion.

72. Overall, Lucent's relationship with AT&T was weakening, not strengthening. Prior to the Class Period, Lucent was in *discussions* with AT&T concerning an anticipated \$1 billion contract under which Lucent would provide AT&T with 80-channel DWDM fiber optic systems. AT&T was Lucent's most important single customer, representing 12% of Lucent's business during fiscal 1999. By early or mid-November, 1999 that contract had been lost for reasons which included the fact that Lucent's management had made a publicly undisclosed strategic decision to stop manufacturing to meet AT&T requirements which exceeded or differed from the marketplace generally. AT&T requirements for the particular product involved included a network management system that was important to AT&T but which was not required by other customers. Lucent determined that it would not longer meet that requirement of AT&T, and AT&T went to another supplier that would meet that requirement.

73. In addition, Lucent lost a potential \$1 billion contract with AT&T to NEC because NEC managed to qualify its 400 series product for production for AT&T, and Lucent had difficulty qualifying its 400 series product in time to meet AT&T's schedule.

*INABILITY TO PRICE COMPETITIVELY AND LACK OF ACCESS TO SUPPLIES OF
CRITICAL COMPONENTS*

74. As Judge Greene recognized in the MFJ decision, the product line which Lucent inherited from AT&T was not competitively priced. However, for several years thereafter, as noted above, Lucent enjoyed a captive market based on the fact that its customers had significant capital invested in Lucent's technology, and were reluctant to jettison that infrastructure. By the beginning of the Class Period, developments in technology had freed Lucent's customers from its hold and such customers had numerous other supplier options.

75. However, the Company's products continued to be significantly more expensive than those of its competitors. As a result, by the fall of 1999, the Company was consistently losing contract bids on the basis of price, in its international network service division and optical networking group among others to competitors such as Nortel, Cisco, and Ericsson. Even with his or her employee discount, it was cheaper for a Lucent employee to buy a telephone from a corner store than to buy a Lucent telephone.

76. One reason for the relatively high cost of Lucent's products was that Lucent had made a strategic decision to vertically integrate its production, instead of outsourcing its components needs. With regard to the optical networking group, Lucent senior management made the decision not to outsource despite the fact that they had received written reports from employees documenting the fact that Lucent would not be able to compete with those companies who specialized in component manufacturing because, among other reasons, these manufacturers sought maximum gross profit margins of 8%, while Lucent prices were set to realize approximately 40% returns.

77. By the middle of 1999, when Lucent senior management finally realized that its decision not to outsource was unworkable, the Company began to try to secure limited amounts of components from other manufacturers. However by that time, optical networking components were scarce, and Lucent's competitors had already placed orders which consumed the entire output capacity of the industry. Further, since Lucent's competitors had placed very large orders for their full component requirements, suppliers chose to fill those large orders first, and Lucent's smaller orders were left unfilled. As a result, during the Class Period, Lucent's optical networking group routinely was forced to halt production while waiting for necessary components. Further, because Lucent failed to implement an adequate quality control procedure for component outsourcing at least until March of 2000, Lucent did not evaluate the quality of the component parts it did receive. The Company often accepted components of substandard non-production grade and quality. With respect to optical networking components, they were often dirty, or out of geometric tune, and therefore would not function properly. Because of the increasing pressure to ship product during the Class Period, the Company nevertheless installed substandard components and shipped such products to customers.

LUCENT'S INTERNAL CONTROL, FINANCIAL REPORTING, AND OTHER INFORMATION SYSTEMS WERE GROSSLY DEFICIENT, MAKING IT EVEN MORE DIFFICULT TO MANAGE THE COMPANY.

78. Prior to and during the Class Period, Lucent had grossly deficient internal controls, and therefore had problems tracking costs and managing budgets. Often there was great confusion as to how much money was coming in and how much was going out; as to whether various units were making a profit, and even how many employees the Company had.

79. During 1999, Lucent was attempting to shift its computer/information system over from a Legacy system to an SAP system. The attempted implementation of the SAP system created havoc with respect to performing many basic operations throughout the Company. The Power Systems Group, for example, was unable to order parts for a substantial period of time because it could not figure out how to pay their suppliers using SAP. In the BCS division, the conversion made it very difficult to ship equipment: orders could be entered into the system but one could not get a “material on job” date. In many cases, deals were lost when the date for delivery turned out to be several months away. It was widely recognized within Lucent that the SAP implementation caused a tremendous backlog, and that customers were not getting their products delivered and implemented in a timely fashion, in part because of the complications created by SAP.

80. Significant problems also existed in the financial reporting, internal control and information systems in Lucent's operations in Europe. In September 1999 a Price Waterhouse consultant to Lucent who was trying to clean up Lucent's European billings expressed concern because nothing was online, the books were a mess, and he was “appalled” at how disorganized things were.

81. The horrible condition of Lucent's internal controls, information and financial reporting systems represented a serious impediment to rapid, effective activity by Lucent in the effort to meet the competitive pressures that were expanding on all sides, and to adapt to the rapidly changing new technological and marketing environment.

82. Prior to and throughout the Class Period, it was widely recognized within Lucent that the Company was having enormous problems collecting its accounts receivable. The reasons for this problem included the large number of sales that had been recorded prematurely, the fact that long periods of time frequently elapsed before delivery and installation after a sale was recorded, and the fact that collections personnel at Lucent were poorly trained and did not have the experience or knowledge necessary to deal with the issues being raised by customers about billings. It was not at all unusual for accounts receivable to be 150/180 days old.

83. Management made an abortive effort to try to clean up the accounts receivable situation during the early and middle part of 1999. However, the training only focused on smaller accounts, ignoring the fact that most end of quarter abuses in recording of sales

happened with respect to the global and big business accounts. As discussed below, management's effort to address the accounts receivable problem essentially terminated just prior to the Class Period because management wanted to avoid the adverse impact on earnings of a major charge for uncollectible accounts receivable.

84. The enormity of Lucent's accounts receivable problem is exemplified by the results of various investigations by task forces that looked into the situation shortly prior to the beginning of the Class Period. For example, one investigator examined the accounts receivable situation at two different Lucent sites, each of which had \$100-200 million on the books Lucent could not account for. Investigation indicated that the shortfalls resulted largely from customers having been billed improperly, not billed at all, or double billed. At the end of the investigation, the money was simply written off without an attempt to achieve any collections. Further exemplifying the common knowledge within Lucent that receivables were vastly overstated, anything that was less than \$50,000 was written off automatically, without even an investigation.

Lucent's "Guidance" to Market Analysts

85. Throughout the Class Period, Lucent regularly disseminated material information about its businesses through the conduit of securities analysts employed by Wall Street investment banks. Specifically Lucent, like other publicly-held companies, managed expectations for earnings by providing "guidance" to analysts. In particular, Defendant McGinn participated in regular conference calls with analysts on the Bloomberg forum among other places, during which he issued guidance on Lucent's business, results and future earnings. These analysts communicated that guidance to the marketplace, which in turn then influenced investors buying decisions and the Company's share price. As a result, Lucent was under pressure to meet analysts' earnings projections in order to continue to grow market capitalization and increase the value of the company's stock.

86. The importance of the sort of guidance that Lucent provided to securities analysts is evident from the fact that recently, the SEC took action to stem the selective disclosure of material information to analysts. See [65 FR 51716](#), 17 C.F.R. 240, 243, and 249, [SEC Release Nos. 33-7881](#), [34-43154](#), *Selective Disclosure and Insider Trading*, ("Regulation FD"). Regulation FD, which took effect October 23, 2000, provides that when a Company, or person acting in its behalf, discloses material non-public information to securities market professionals and company insiders, it must also publicly disclose such information. *Id.* In adopting the regulation, the SEC stated that its purpose was to address the threat to integrity of securities markets posed by the behavior of publicly-held companies in making disclosures to analysts. *Id.*

LUCENT'S DECEPTIVE ACCOUNTING AND FINANCIAL REPORTING

(a) *Overview*

87. Prior to the Class Period, Lucent enjoyed exceptional revenue and earnings growth, resulting in a dramatic *increase in* the price of its common stock. However, beginning in at least 1999, the demand for the Company's products began to stall. In an attempt to mask the waning demand for Lucent products, Defendants engaged in a series of manipulative accounting practices. These practices violated Generally Accepted Accounting Principles ("GAAP") and created the false impression that Lucent's favorable growth rate continued unabated and that the demand for Lucent's products continued to be robust.

88. GAAP are those principles recognized by the accounting profession as the conventions, rules, and procedures necessary to define accepted accounting practice at a particular time. As set forth in Financial Accounting Standards Board ("FASB") Statement of Concepts ("Concepts Statement") No. 1, one of the fundamental objectives of financial reporting is that it provide accurate and reliable information concerning an entity's financial performance during the period being presented. Concepts Statement No. 1, , 42, states:

Financial reporting should provide information about an enterprise's financial performance during a period. Investors and creditors often use information about the past to help in assessing the prospects of an enterprise. Thus, although investment and credit decisions reflect investors' and creditors' expectations about future enterprise performance, those expectations are commonly based at least partly on evaluations of past enterprise performance.

89. *Regulation S-X [17 C.F.R. § 210.4-01(a)(1)]* states that financial statements filed with the SEC that are not prepared in conformity with GAAP are presumed to be misleading and inaccurate. The representations by the defendants that Lucent's financial statements were prepared in accordance with GAAP were materially false and misleading because the financial statements materially inflated and distorted the Company's true financial performance during the Class Period.

90. In an attempt to mask the waning demand for the Company's products, the defendants caused Lucent's employees to engage in improper revenue recognition practices, and/or knowingly acquiesced in and condoned those practices. These practices afforded Lucent the ability to meet analysts' earnings estimates. Among other things, to meet these numbers, according to pleadings filed by the North Andover employees group, Lucent engineered end-of quarter pushes to meet its earnings estimates, "by whatever means necessary" often at the expense of Lucent's longer term business objectives, reputation, product reliability and customer satisfaction.

91. It was recognized throughout Lucent that, at the end of each quarter, sales personnel would engage in a widespread practice of booking sales prematurely and improperly to be able to report the sales numbers mandated by management. As a result of these improper revenue recognition practices, Lucent's accounts receivable began to swell.

92. In a process that was condoned and encouraged by Lucent management, Lucent employees often reclassified the age of accounts receivables. This practice served two purposes: (1) it helped conceal Lucent's improper revenue recognition; and (2) it reduced the need to reserve for receivables that remained uncollected for an extended period of time. These practices helped maintain the appearance that the Company's financial growth was continuing at historic levels when, in fact, it was not.

93. In addition, hundreds of millions, if not billions, of uncollected receivables remained improperly on the books, in part because the receivables were phony, and in part because Lucent's collections personnel were grossly untrained and inexperienced, and were unable to deal effectively with the numerous problems and issues raised by unsatisfied customers.

(b) Class Period Background: Lucent's Premature Recognition Of Revenue

94. GAAP provides that revenue should not be recognized until it is realized or realizable and earned. FASB Concepts Statement No. 5, ¶ 83. The conditions for revenue recognition ordinarily are met when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the seller's price is fixed or determinable, collectibility of the sales price is reasonably assured and when the entity has substantially performed the obligations which entitle it to the benefits represented by the revenue. Generally, revenue should not be recognized until an exchange has occurred and the earnings process is complete. A transfer of risk has to occur in order to effect an "exchange" for the purposes of revenue recognition. FASB Concept Statement Nos. 2 and 5; FASB Statement of Financial Accounting Standards ("SFAS") No. 48; Accounting Research Bulletin ("ARB") No. 43; Accounting Principles Board ("APB") Opinion No. 10; and American Institute of Certified Public Accountants ("AICPA") Statement of Position ("SOP") 97-2.

95. Pursuant to Lucent's revenue recognition policy, Lucent recognizes revenue on the sale of products when the products are delivered or the service is performed, all significant contractual obligations have been satisfied, and the collection of the sales price is reasonably assured.

96. During the Class Period, Lucent violated its own revenue recognition policy and GAAP when defendants caused customer service representatives to invoice orders, thereby recognizing and reporting revenue on the order, even though the customer had not yet committed to purchasing the order. As such, persuasive evidence of an agreement is not exist, the sale price was not fixed or determinable, and the collectibility of the sales price was not reasonably assured and an exchange for purposes of revenue recognition for purposes of revenue recognition at the time Lucent recognized and reported revenue on such orders.

97. To the detriment of unsuspecting investors, Lucent's management directed or knowingly condoned and encouraged the process in which customer service representatives would invoice orders, thereby recognizing and reporting revenue on the

order, even though the customer had not yet committed to purchasing the order. In such a situation, persuasive evidence of an agreement does not exist, the sale price is not fixed or determinable, and the collectibility of the sales price is not reasonably assured, and an exchange has not occurred for purposes of revenue recognition for purposes of revenue recognition at the time Lucent recognized and reported revenue on such orders. In many instances, invoices on such contingent orders were generated on or near the last day of the quarter so that the sales representatives could meet their quarterly sales performance quotas. Lucent recognized and reported revenue on such orders, in violation of GAAP, even though its customers had not yet agreed to purchase the orders.

98. Thereafter, Lucent employees culled the invoices associated with such “orders” to prevent them from being mailed to the unsuspecting customers. After the end of the quarter, the “order” often would be reversed, and Lucent employees re-invoiced the customers when they actually agreed to purchase the order.

99. In certain instances, Lucent employees did not reverse and re-invoice a prematurely recognized order. Rather, a “dummy” invoice, would be manually generated by Lucent employees when Lucent's customers actually agreed to purchase the order. The “dummy” invoice was generated so that it could be issued to Lucent's customers without the transaction being reflected in Lucent's accounting system as the invoice for the order had previously been recorded. This process was known as “closing out” an order among Lucent's sales force. As a result, when Lucent's customer first received the manual invoice, in many instances, Lucent's system already reflected the customer receivable as being “past due.”

100. According to numerous individuals employed by Lucent during the relevant time in Lucent's BCS division, Optical Networking Group, and international businesses, the recognition of revenue on “orders” related to prospective sales of products which had not yet occurred was a widespread practice throughout the Company, including but not limited to those divisions. Lucent's sales force agreed to engage in such conduct because Lucent sales commissions were paid when revenue was recognized, regardless of whether the customer actually paid for the product.

101. Another tactic employed by Lucent to prematurely recognize revenue, was known as “CNRing” an order. This technique allowed the Company to “close out” and invoice the order when the product was shipped but not yet installed. Although Lucent attempted to divide these “sales” into two components: equipment and installation, so that it could recognize revenue related to shipped equipment prior to its installation, in practice, it was difficult to allocate the billing among equipment and installation. As a result, Lucent generally billed 100% of the order at the time the product was shipped. Lucent's recognition of revenue on “CNRing” transactions was improper as the installation of Lucent's equipment was a significant obligation essential to the functionality of the delivered equipment which remained unperformed at the time revenue was recognized. As such, revenue was not earned and the collectibility of the sales price was not reasonably assured on such transactions when revenue was recognized by Lucent. Often sixty days or more elapsed from the date of shipment before installation occurred.

(c) Lucent's Uncollectible Accounts Receivable And Its Manipulation of Accounts Receivable Reserves

102. Although the investing public did not understand why Lucent's receivables were growing, the magnitude of Lucent's premature revenue recognition practices is evidenced, in part, by its ballooning accounts receivable balance. For example, *during the six months ended September 30, 1999, Lucent's accounts receivable increased by approximately \$1.7 billion, or 19%, from \$9.1 billion to \$10.8 billion, but its reserve for uncollectible receivables increased by only 3.7%. Indeed, as a result of Lucent's premature revenue recognition practices, Lucent's customer service representatives often ignored outstanding invoices and did not attempt to collect them.*

103. Furthermore, as alleged at „127 below, in late summer of 1999, an abortive push by management to clean up the Company's accounts receivable was essentially abandoned. Area Vice Presidents, among others, stopped getting feedback or being measured by progress on receivable reductions, and compensation was no longer impacted by such measures. Specifically, the Company abandoned a program to link these individuals remuneration with their success in reducing receivables. Thereafter, uncollectible accounts receivable again trended upwards.

104. Defendants knew or recklessly disregarded that the magnitude of the increase in Lucent's receivables during, at least, the six months ended September 30, 1999 was unprecedented and highly irregular. In furtherance of their scheme to misrepresent the Company's operating results, the defendants compounded Lucent's misleading accounting and reporting of revenues by failing to timely and adequately reserve for uncollectible receivables.

105. GAAP requires that financial statements account for existing uncertainties as to probable losses. Such loss contingencies should be recognized and reported as a charge to income when: information existing at the date of the financial statements indicates that it is probable (*e.g.*, a likely chance) that an asset has been impaired or a liability has been incurred; *and the amount of such loss can be reasonably estimated.* SFAS No. 5, „ 8.

106. GAAP also requires that financial statements disclose contingencies when it is at least reasonably possible (*e.g.*, a greater than slight chance) that a loss may have been incurred. SFAS No. 5, „ 10. The disclosure shall indicate the nature of the contingency and shall give an estimate of the possible loss, a range of loss or state that such an estimate cannot be made. *Id.*

107. The SEC considers the disclosure of loss contingencies to be so important to an informed investment decision that it promulgated Regulation S-X [[17 C.F.R. § 210.10-01](#)], which provides that disclosures in interim period financial statements may be abbreviated and need not duplicate the disclosure contained in the most recent audited financial statements, *except* that, “where material contingencies exist, disclosure of such matters shall be provided even though a significant change since year end may not have occurred.”

108. As noted above, by September 30, 1999, Lucent's accounts receivable had mushroomed to an unprecedented level. In furtherance of their scheme to inflate Lucent's operating results, Lucent management encouraged and condoned the common practice of improperly reclassifying the age of Lucent's outstanding receivables, if necessary to meet quarterly numbers. For example, receivables which were outstanding for more than 90 days, in part as a result of Lucent's improper revenue recognition practices noted above, were often reclassified at the end of the quarter in Lucent's accounting records as current receivables by Lucent employees. These reclassifications reduced the risk that Lucent's premature revenue recognition practices would be detected, and reduced the apparent risk the receivable would go uncollected, thereby avoiding a possible charge to earnings which would result from an increase in the reserve for uncollectible receivables.

109. The defendants knew or recklessly disregarded the fact that Lucent's receivables remained uncollected over an unusually long period of time, and that GAAP required that Lucent establish an adequate reserve in its financial statements to account for probable uncollectible receivables. Nonetheless, in violation of GAAP, Lucent's financial statements failed to adequately reserve for uncollectible accounts receivable. For example, while Lucent's accounts receivable increased by approximately \$1.7 billion, or 19%, from \$9.1 billion to \$10.8 billion during the six months ended September 30, 1999, its reserve for uncollectible accounts during the same period increased by only 3.7%. Indeed, Lucent's reduced accounts receivable reserve is ostensibly justified, in part, by the defendants' improper reclassification of the age of its outstanding accounts receivables.

110. Notwithstanding the defendants' awareness of the true age of Lucent's receivables and the growing receivable balance, Lucent failed to adequately reserve for uncollectible receivables in, at least, its September 30, 1999 financial statements. Had Lucent's accounts receivable reserve at September 30, 1999 been maintained at the same level that existed at March 30, 1999, its income during the September 30, 1999 quarter would have been reduced by approximately \$53 million, or approximately five percent.

111. As one example of the improper practice involved, in the fall of 1999, Lucent senior management rejected internal auditor's recommendations in order to avoid taking write-offs in the quarter. An internal audit conducted during September/October 1999, revealed that accounts receivable were overstated in an international division. The audit team determined that the proper course would be to take an immediate write-off. However, the division's management team reversed the audit team's recommendation stating that the division "could not afford to do so at th[e] time." The decision in this regard was made at the top level of Lucent management, and specifically involved Lucent's head of internal audits.

(d) The Advent of the SAP Conversion in 1999 Makes Clear to Lucent Senior Management that Sales are Being Improperly Recorded

112. During the first half of 1999, Lucent implemented a conversion from a Legacy accounting system to a SAP billing/accounting program. To the extent Lucent's

management was not already knowledgeable, implementation of the SAP program exposed pervasive discrepancy between the Company's recorded revenues and actual sales.

113. In early 1999, concurrent with the switch to SAP, Lucent began an effort to address problems with the Company's accounts receivables. For example, in early 1999, Bill O'Shea, the then Executive Vice President and Chief Executive Officer, Enterprise Networks held a meeting at Lucent headquarters with video conference to the branches and a live broadcast to the field. At the meeting, O'Shea explained that BCS's receivables problem was so grave the unit might not survive. Each division head was given the directive to ensure that bad sales not be recorded.

114. Similarly, beginning in April of 1999, operations managers in charge of accounts receivable at the Customer Care Centers (the accounts receivables arm of the BCS Division), such as Robin Jones in the Tuscon office, began to enforce an accounts receivable policy designed to reduce CNRring and early closing out of orders.

115. In addition, management began focusing on the fact that numerous manual adjustments were being made at the end of the quarter to increase revenue figures, a process that involved the efforts of employees to circumvent the difficulty of recording sales on the computer and avoid the requirements for valid sale imposed by the computer program. Management *was* clearly aware of the material amount of such manual adjustments and began taking some steps to address that problem. During mid-1999, Lucent headquarters issued a directive, which was communicated, among other ways, through a company-wide e-mail, that Lucent would no longer allow manual adjusting entries at the end of the quarter unless they were approved by head of the respective division. The e-mail explained that the reason for the policy change was that a continuation of the practice might get the Company "into trouble."

(e) Lucent's Abortive Attempt To Mitigate Its Deceptive Accounting And Financial Reporting Practices

116. *Defendants knew that Lucent's improper revenue* recognition and accounts receivable reserve manipulations would ultimately need to be remedied. In an attempt to mitigate the negative fall out associated with its improper accounting and financial reporting practices, Lucent begun the effort of ridding itself of its bloated receivables.

117. However, as alleged below in paragraphs 127-136, management's effort to address the receivables problem was essentially shelved and abandoned prior to the Class Period when it threatened to interfere with management's ability to report revenues and earnings that would match Wall Street's expectations.

118. During the quarter ended September 30, 1999, Lucent disclosed that it sold \$625 million of its accounts receivable to a non-consolidated qualified special purpose entity. This had the intended effect of reducing Lucent's accounts receivable by \$600 million at September 30, 1999.

119. In September 2000, Lucent and a financial institution arranged for the creation of a non-consolidated special purpose trust for the purpose of allowing Lucent to sell up to \$970 million in customer finance loans and receivables to the trust. Finally, during the quarter ended September 30, 2000, Lucent disclosed that it increased its accounts receivable reserve by approximately \$170 million.

**IMMEDIATELY PRIOR TO AND DURING THE CLASS PERIOD LUCENT SENIOR
MANAGEMENT TAKES STEPS TO MASK DECLINING *DEMAND AND OTHER*
*PROBLEMS AFFLICTING LUCENT'S PRODUCTS***

Lucent management decides to knowingly ship flawed products

120. In the beginning of the Class Period, Lucent's management was aware of the overwhelming array of problems confronting the Company as described above, and the consequent difficulty the Company would have in continuing to report revenues and earnings that would be consistent with the guidance Lucent's management had previously given stock market analysts.

121. Although Nortel, Lucent's closest competitor in the optical networking business had brought its OC-192 product to market in 1997, by the fall of 1999, Lucent's OC-192 product was still not ready for sale. As a result, Lucent's 24% share of the burgeoning optical networks market (in 1998 close to Nortel's 29% market share) was quickly declining as customers chose to buy OC-192 products produced by Lucent's competitors. The Company nonetheless represented that it had such a product for sale by, among other things, including the 10G product on its list of Products in its Annual Report form filed with the SEC on September 30, 1999.

122. In response to the growing pressure on the Company's sales from its inability to market an OC-192 product, its manufacturing problems with its older technology products, disappointments described above in the wireless, software, and power switch areas, and actual or threatened losses of major contracts with AT&T, the Saudi government, and other prospective customers, Defendants made a high level policy decision to ship product which they knew to be not ready for sale. They made this decision in order to fraudulently inflate the Company's "sales." That decision also violated GAAP's revenue recognition criteria, because revenue would not be earned, and the collectibility of the sales price would not be reasonably assured, on such transactions at the time that revenue was recognized by Lucent.

123. Specifically, according to statements by the North Andover employees group, at a meeting in Nuremberg Germany in September 1999, Lucent senior management informed the Company's directors that the Company had adopted a strategy of selling products to customers as quickly as possible despite design and reliability issues, and fixing such problems later.

124. This policy was implemented. For example, on several occasions during 1999 division directors ordered that product be shipped despite the existence of major flaws in the circuit pack portion of the product. During the last fiscal quarter of 1999, Lucent sold a WaveStar DWDM which was powered by circuit packs that were still in the test phase. Thereafter, the production packs failed and an employee had to replace all the circuit packs. Similarly, by the end of 1999 or beginning of 2000, Lucent began shipping its Pathstar product which did not work properly. Pathstar's problems arose from the fact that the product was shipped as it was still being tested and designed. When Lucent's technicians were unable to get the product to work to the customer's satisfaction, Lucent replaced the product with another switching product which was far more expensive, but without increasing the price. Other customers who complained about Pathstar's performance were also offered more expensive products as an even exchange replacement.

125. Also, Quality assurance auditors at the North Andover facility were instructed to ship product which had failed to meet Lucent's quality assurance standards. Product that was identified as having a defect, for example which failed to meet ANSII standards for soldering, were marked with red tags by quality assurance auditors. During the Class Period, management with increasing frequency directed quality assurance auditors to remove the red tags, rip them up and ship the defective product the way it was so that the Company could meet its numbers.

126. Furthermore, beginning in at least November 1999, Lucent shipped products throughout its product lines which were not ready for sale because the installation, engineering and maintenance manuals for such products were not ready for dissemination. As a result, Lucent's customers were thus unable to utilize products received.

Concurrent with the Advent of Problems in the Optical Networking Business and the Growth of Problems with other Products, Lucent *Abandons Its Efforts to Address the Company's A/R Problems*

During the Fourth Quarter of Fiscal Year 1999 and thereafter the *deceptive "sales" recognition schemes which had been slated to be eliminated* are instead used to boost revenue

127. At the same time that Lucent management was recognizing that revenues were increasingly hurt by the problems described above, they ceased their effort to clean up the premature revenue recognition and receivables problem. Sometime in the late summer of 1999, the management's push to clean up the Company's accounts receivable was essentially abandoned. Area Vice Presidents, among others, stopped getting feedback or being measured by progress on receivables, and compensation was no longer impacted by such measures. Specifically, the Company abandoned a program to link these individual's remuneration with their success in reducing DSOs. Thereafter, uncollectible accounts receivable again began to trend upwards.

128. In addition, *during 1999* the end-of-quarter pushes to meet earnings estimates “by whatever means necessary” which Defendants had sometimes used in 1998 became regular practice. As before, these manipulations occurred at the expense of Lucent's longer term business objectives, reputation, product reliability and customer satisfaction. For example, as noted above, by the fall of 1999 on several occasions management in Lucent's North Andover optical networking facility ordered that product which was known to contain defects be nonetheless shipped to customers.

129. In addition, it continued to be common practice for Lucent to recognize revenue before product had even been shipped to the customer. For example, in August or September 1999, Lucent's China Business Unit falsely recognized revenue on WaveStar product which was never sold. The circumstances of this false WaveStar “sale” were discussed on a conference call which included, among others, Ron Smith, an executive in the division, and other Lucent employees based in Shanghai. The order for approximately \$66 million was placed “just to book revenue” and the product, which was an obsolete model, was supposed to be stored in a warehouse near JFK rather than be shipped to the joint venture “customer” who did not want to be saddled with the product.

130. As another example, during, at least, the fourth quarter of 1999, the director of Lucent's Powers Systems Division loaded Lucent's distributors *with* product they did not yet require so that Lucent could report the sales. These Lucent distributors were to warehouse the product, until such time as Lucent bought it back. Lucent's recognition of revenue on these shipments was improper because the distributors did not agree to purchase or accept the risks and rewards of ownership of such products when they were shipped. To the contrary, Lucent agreed that such products could be returned at a later date. Accordingly, an exchange for purposes of revenue recognition did not occur at the time Lucent recognized and reported revenue on such product shipments, thereby resulting in improper revenue recognition. The distributors involved in the foregoing scheme included Pioneer Standard, Marshall Industries, Gates/Arrow Electronics and Avnet.

131. Similarly, Lucent's Internet Service Provider Division “strong-armed” re-sellers to take products. By this method, the Internet Service Provider Division “sold” \$59 million worth of product to Westcon, Inc. on the last day of Lucent's 1999 Fourth Quarter, so that revenues from that sale could falsely be reported as realized during that quarter.

132. In addition, prior to and during the Class Period, customers with credit problems often were released from “credit hold” status, near the end of fiscal quarters, so that revenue could be recognized on their orders. This practice, which enabled Lucent to meet quarterly analyst revenue estimates, violated GAAP and Lucent's *policy* that mandated that Lucent would not accept orders from customers on credit hold. For example, Patagonica, a South American company, had a \$5 million receivable outstanding for more than 90 days but was nevertheless released from credit hold and allowed to place new orders for \$1 to 2 million.

133. As the truth about the Company's floundering optical business and extent of sales shortfalls became known to Defendants, Defendants also attempted to mask their problems by cutting costs. By the fall of 1999, Lucent management had implemented stringent new policies designed to cut expenses, including the use of spending freezes and internal and external hiring freezes and layoffs. Beginning in the summer of 1999, employees in the Octel Messaging Division, and in the Power Systems Group and elsewhere, were told not to travel, and to keep expenses to a minimum. More specifically, the new policy required an E-band, or executive-level approval for any travel. In the Power Systems group, for example, a division manager would have to personally approve any travel by any of the 5000 employees in the division.

134. These extraordinary cost restrictions, which were not publically disclosed, reflected Defendants' great concern over Lucent's deteriorating earnings prospects and were sharply inconsistent with the bullish presentations made by defendants to the investigating public as described below.

135. As yet another part of their scheme to artificially boost the apparent demand for the Company's products, at the end of 1999 Lucent began offering generous lines of credit to CLECs and other companies, including many companies of questionable creditworthiness, to purchase its products so that the Company could mask the declining demand for its products and report sales. For example, according to a report published in *The Street.com*, Lucent entered into a \$250 million credit agreement with ICG Communications ("ICG") a troubled CLEC, to enable ICG to purchase Lucent products. As a result of that agreement, ICG has committed to buying at least \$175 million of equipment from Lucent. However, the value of the accounts receivable associated with the ICG purchases is questionable: The company is widely reported to be close to collapse, and its share price has fallen from \$39.25 to \$0.44.

136. By the end of 1999, according to an report published in *Barrons* on September 4, 2000, Lucent had provided \$1.85 billion in loans and loan guarantees to its customers to finance purchases of Lucent products.

Problems in Lucent's Optical Networking *And Other Businesses are Belatedly Revealed*

137. Despite Defendants' scheme to conceal the deteriorating nature of Lucent's business from the investing public, on January 6, 2000 Lucent was forced to issue a warning that disclosed that the Company would materially fail to meet analyst's earnings expectations for the first fiscal quarter of 2000 for reasons which included problems in optical networking, and in other areas of Lucent's businesses as well.

The Subsequent Market Reaction to *Defendant's Disclosure of those Problems*

138. Analysts reacted swiftly to Lucent's January 6 announcement.

139. In extremely heavy trading, Lucent's share price steeply fell as much as 27.89% or approximately \$20.00 per share to close at \$52.19 per share, a new 52 week low on January 6, 2000.

140. The market's surprise was not shared by Lucent employees, many of whom had fully had expected a serious shortfall to be announced during 1999.

141. According to a report published on October 23, 2000, on the Bloomberg service, the Lucent Board of Directors ultimately ousted Defendant McGinn as Chairman and Chief Executive Officer during a board meeting on October 22, 2000 after McGinn disclosed to the Board of Directors that the Company would once again miss earnings targets for the quarter.

142. According to an October 24, 2000 article in *The Wall Street Journal*, "the key strategic error that led to Lucent's decline was a misjudgment about the market for high speed optical equipment that allowed competitors, particularly Nortel Networks Corp., to gain a huge lead." The article also attributed Lucent's woes to the fact that Lucent had lost two large contracts, including one with Saudi Arabia, and had to set aside increasing reserves for bad debt.

143. According to the *The Wall Street Journal* article, several Lucent executives warned Defendant McGinn as long as a year before -- at the beginning of the Class Period --- that the Company needed to drastically cut its financial projections because its newest products weren't ready yet and sales of older one were going to decline. Confirming the recklessness of McGinn's and Lucent's conduct, according to the report, "McGinn, absolutely rejected the advice. He was in total denial."

FALSE AND MISLEADING STATEMENTS DURING THE CLASS PERIOD

The Class Period Begins as Lucent Announces "Better than expected fourth quarter profits" *and a restructuring of its operations*

144. The Class Period begins on October 26, 1999, when Lucent issued a press release entitled "EPS increases 47.6% to \$0.31 for Fourth Fiscal Quarter of 1999, Excluding One-time Events." The release which also announced a corporate restructuring, noted that Lucent's revenues for the quarter ended September 30, 1999 were \$10,575 million, an increase of 23.3% over the prior year's quarter. Among other things, Lucent announced that it had a better-than-expected fourth fiscal quarter 1999, the period ended September 30, 1999. For the fourth fiscal quarter of 1999, Lucent announced purported profits of \$972 million, or \$0.31 per share, compared with \$647 million, or \$0.21 per share reported in the same period the prior year; these purported earnings were \$0.02 *above* analysts' expectations. According to the release, Fourth Fiscal Quarter 1999 revenues from Systems for Network Operators increased 31.6%, revenues from Business Communications Systems increased 0.30% per share and revenues from Microelectronic Products increased 22.2%, in comparison to the prior year's quarter. The release stated:

Lucent enters the new millennium with momentum” said Richard McGinn, Lucent Technologies chairman and chief executive officer. “This was the strongest quarter and the strongest year in Lucent's history. We delivered on and exceeded our commitment to grow the top-line by 19 to 20 percent and earnings per share by 35 percent, excluding one time events.” “Our ability to provide customers with the systems, software, silicon and services they need to build end-to-end next-generation networks continues to win Lucent new business and strengthen our relationships with existing customers.” said McGinn. In fiscal 1999, Lucent announced more than \$11 billion in contract wins, including more than \$2 billion in September alone. McGinn noted that Lucent's growth in the fourth quarter was again driven by the company's focus on hot growth areas like optical networking, wireless networking and professional services.

145. Defendant McGinn's statements and the other statements in the October 26, 1999 Lucent press release referenced in , 144 above were materially false and misleading, and were known by Defendants to be materially false and misleading at the time of their publication, or were recklessly disregarded as such for the following reasons. It was materially false or misleading to characterize Lucent as “entering the new millennium with momentum”, winning new business, strengthening existing relationships, *and* enjoying growth *that* was “driven by the Company's focus on hot growth areas like optical networking, wireless networking and professional services” while failing to disclose the following materially adverse information that was known to Defendants:

(a) Rather than enjoying positive momentum, in a desperate attempt to meet earnings estimates, Defendants had instituted extraordinary spending and hiring freezes, endorsed the recognition of revenue on products which had not yet been sold to inflate purported revenues, were desperately playing catch up in optical networking, and had serious manufacturing, supply, cost, and quality assurance problems which impaired its ability to produce and perform.

(b) In particular, it was materially false and misleading to emphasize the Company's involvement in “hot growth areas like optical networking” in light of Defendants' knowledge, at the time, that Company was seriously behind in the development of its planned OC-192 product, that demand had shifted dramatically away from Lucent's existing optical networking product to OC-192, that customers were shifting their purchases to companies like Nortel that could already sell OC-192 product or were deferring purchases from Lucent until Lucent would be able to sell OC-192, and that demand had significantly diminished for the OC-48 optical networking product that Lucent was presently able to sell. As alleged above, these facts were discussed *at the highest levels of Lucent's management, including* Group President Harry Bosco, prior to the beginning of the Class Period.

(c) Lucent had adopted a policy of selling product to customers as quickly as possible despite design and reliability issues and of fixing such problems later.

(d) Lucent did not have an ability “to provide customers with the systems, software, silicon and services ... which were continuing to win Lucent new business.” Rather, the

Company was facing declining demand across its divisions and was losing market share to competitors. For example, Lucent was experiencing problems with meeting forecasts and sales projections for wireless products, in part because the Company's new products were not living up to their expectations. In addition, Lucent's data networking division was experiencing production and demand problems, and the Company was missing shipment and release dates for Lucent's switching products. Further, sales of switching products, previously the backbone of Lucent's sales revenues, were impacted by both the overall decline in the switching business as a result of the advent of optical and wireless products and by the fact that Lucent could not bring its newest product, the 7 R/E market, though Lucent's sales representatives were selling the product; and,

(e) Certain of the "contracts wins" which the release touted were actually losses. According to individuals formerly *employed at Lucent by the fall of 1999*, the Company had lost a \$200 million internet working contract to Nortel, lost two major AT&T contracts including an important power supply contract and a 5ESS switching contract worth approximately hundreds of millions of dollars, and the Company's wireless division had lost a significant contract with the government of Saudi Arabia, worth approximately \$6 billion according to a former employee. In fact, Lucent's power service division products was losing contracts and market share with its largest customer AT&T because its products did not meet AT&T specification.

(f) Revenue and profit figures set forth in that press release were materially false and misleading because they reflected the results of Lucent's practice of prematurely and falsely recognizing sales revenue, at the end of each quarter, in order to meet analysts expectations.

146. During a *Bloomberg Forum* conference call with analysts on October 26, 1999 to discuss Lucent's better than expected results, Defendant McGinn stated to analysts: "We are experiencing exceptionally strong growth in data networking for service providers, in wireless networks, [and] in optical networking ..." Later, in response to the question as to "whether optical networking was growing you know people are saying the market is growing at 40 to 50% a year, are you in that range?" Defendant McGinn stated, "I can tell you that you're right, that Optical is growing 40 to 50% and we're exactly the same range *even though we are the leader.*"

147. Defendant McGinn's statements on the October 26, 1999 conference call referenced in ,, 146 above were materially false and misleading, and were known by Defendants to be materially false and misleading at the time of their publication, or were recklessly disregarded as such for the reasons set forth in ,, 145 above and because:

(a) Lucent was not the leader in optical networking but was a quickly eroding second to Nortel, which had developed the OC-192 product in 1997;

(b) Lucent's. optical networking business was not growing 40 to 50% but was in decline, as customers rejected Lucent's older generation 2.5 gigabit products and Lucent was unable to market an OC-192 product;

(c)the Company was not experiencing strong growth in data networking, wireless and data and optical networking, but was losing material contracts with long-standing important customers, including AT&T, and one with the Saudi Arabian government to competitors among other reasons, because of design problems and non-competitive prices.

148. Defendant McGinn had actual knowledge that Lucent's optical networking business was not growing in the 40 to 50% range when he issued the statement that it was. As noted above, by October 1999, Lucent senior management openly discussed Lucent's problems producing optical networking products. Further, McGinn knew that *Lucent was well behind the* market leader Nortel, and consequently, Lucent's growth rate would not be similar to Nortel's or other competitors who had OC-192 products ready for sale. In addition, by October of 1999 McGinn knew that the Company's senior management had directed managers to implement policy to sell products to customers which they knew not to be ready for marketing because Lucent senior management knew that the Company could not keep up with its competitors.

149. On October 28, 1999 *BusinessWorld* reported specific comments made by defendant McGinn concerning the Company's purported restructuring. Defendant McGinn used this opportunity to further condition the market to believe that the Company was achieving results that the Company had projected when in reality it was not, by stating, the following:

“Four years ago, we set out a vision for the networks of the future and have worked relentlessly to become the world leader in communications networking,” said [defendant] McGinn.

“Today, we are focused on continuing our growth and share gain in the face of light-speed market changes, increasingly complex networks, and fortunately a wealth of opportunity,” he added.

* * *

“The realignment is intended to mirror the way we are approaching customers today - with converged network solutions,” said [defendant] McGinn.

“We are sharpening our focus on high-growth areas - such as data networking, optical networking, wireless, semiconductors, e-business and professional services - while speeding our growth in international markets. And, we will also be aligning our management structure to increase productivity and accelerate our response to customer needs.”

He said the four core businesses will address specific markets and *allow Lucent to approach customers “in a faster and more integrated fashion.”* [Emphasis added.]

150. The statements reproduced in paragraphs 149 above, were each materially false and misleading, and were known by Defendants to be materially false and misleading at the time of their publication, or were recklessly disregarded as such for the reasons set forth in ,,145 and 147 and because:

(a) Lucent was not “continuing their growth and share gain in the face of light speed market changes” and “sharpening [its] focus” on the high growth areas of data networking optical networking products, wireless products among others. Rather, Lucent was falling far behind its competition in the marketing of OC-192 products because Lucent had delayed its transition to OC-192 technology, and had design and other problems with both older technology 2.5 gigabit and with OC-192 products still in development, causing Lucent to lose its customers to competitors and hence its market share;

(b) In response to Lucent's inability to bring products to market which offered the latest in technology to compete with competitors on a timely basis, Lucent senior management informed the Company's directors to ship defective products which were not ready for marketing in order to inflate revenues. Consistent with this policy, the Company shipped *products across the Company's product lines which were not ready* -- including switches, optical, and wireless products. The result was increasing customer dissatisfaction, a mounting level of collectible accounts receivable, and increasing costs for repair and replacement.

151. The statements were also materially misleading and because Defendants failed to disclose the following adverse facts:

(a) that as a result of the materially adverse conditions, Defendants knew that they had no reasonable basis to claim that the Company could accelerate revenue growth through fiscal 2000 and beyond. According to an article published in *The Wall Street Journal* on October 24, 2000, as early as October of 1999, senior Lucent Executives had told Defendant McGinn that the Company needed to drastically cut its financial projections because its newest products weren't ready for sale and sales of older ones were going to decline.

152. In response to the materially false and misleading statements issued by the Defendants, shares of Lucent rose from a market price of \$59.00 per share immediately prior to the Company's October 26 announcement to over \$80.62 per share by November 18, 1999. Thereafter, based significantly on the guidance provided by the Company, the price of Lucent stock continued to rise throughout the Class Period, reaching a high of over \$84.00 per share on December 9, 1999, as Defendants' *materially false and misleading statements continued to mask the* financial troubles which were adversely affecting the Company's core operations, revenues, growth and earnings prospects.

153. Among other things, the materially false and misleading statements issued by the Company had the effect of misleading analysts. For example, on October 27, 1999, based substantially upon the Company's representations and the growth prospects presented

thereby, SG Cowen Securities Corporation ("SG Cowen") issued an analyst report which rated Lucent common stock a "Buy," and encouraged its customers to purchase this stock. In making his recommendations, the SG Cowen analyst stated:

Guidance, Annual EPS Remain Unchanged; Slight Quarterly Model Adjustments

Buy Rating Retained. Estimates Unchanged. \$75 Price Target Represents 47x C:00 EPS.

Guidance Remains The Same; Slight Model Changes; Publishing F01 Numbers. LU is maintaining its guidance of 19%-20% top line growth and 35% earnings growth for 2000. Given the results in Q4 :F99, we are slightly increasing our Q1 :00 revenue by \$100M to \$11.2B, and

lowering our gross margin estimate to 53.0% from 53.7%. Q1 :FOO EPS estimate remains unchanged at \$0.54. For FOO we have slightly adjusted our quarterly numbers, but are *maintaining our year estimate of \$1.53*, with revenues revised upward 200MM to \$44.9B. For F01 we are estimating top line growth of 17.6% with slight margin expansion to 49.9%, yielding EPS of \$1.85 (*20.4% Y/Y).

* * *

Buy Retained With \$75 Target Price Representing 47x COO EPS. *We believe this is a strong quarter, and continue to be confident in the overall business. We continue to see strong growth in optical, wireless, data and microelectronics.* Enterprise business continues to be weak, and a risk to growth. While we believe the company may be exchanging gross margin points for top line growth, the results on the bottom line have been positive. The Ascend business looks strong. The company's guidance of 17-20% revenue growth and faster EPS growth is unchanged. We expect the company to take action to: 1) reignite growth in the Business Communications Systems business; 2) continue to generate positive cash flows; and 3) continue to grow software and semiconductors. We also believe Q1 :F00 performance will depend on the generic load of software shipping as expected. *We are maintaining our Buy-2 rating and target price of \$75 based on 47x COO EPS. [Emphasis added].*

Based on a review of the information provided in part by the Company, and its analysis of the Company's reported record results and its stated growth prospects, SG Cowen estimated earnings per share of \$1.20 and \$1.53 for fiscal 1999 and 2000, respectively.

154. Only days after the announcement of the Company's purported restructuring, on November 2, 1999, the *Associated Press* reported that Lucent announced that it planned to cut over 1,700 jobs, or approximately 1% of its workforce. According to the *Associated Press*, Lucent officials said that improved repair and billing technology was behind the decision, which would purportedly take effect by the end of the year.

155. The statements contained in November 2, 1999, *Associated Press* article reproduced herein at , 154 above, were materially false and misleading, and were known by Defendants to be materially false and misleading at the time of their publication, or were recklessly disregarded as such, for the reasons stated herein in ,,,, 145, 147, 150, and 151 above, and because according to former employees of Lucent, Lucent's lay-offs were yet another example of Lucent's management's push to meet end of quarter numbers by any means possible, a desperate effort to cut costs and boost revenue, and to condition the market to believe that the Company was streamlining its operations, when in fact the Company had abandoned efforts to address accounting problems in the fall of 1999. It was also materially false and misleading to state that lay-offs resulted from a reduced need for repair and customer service in light of the design and reliability problem described above.

156. On November 11, 1999, Lucent held its annual meeting with market analysts covering the Company. According to a November 12, 1999 Legg Mason Wood Walker Inc., report, the message at the meeting was “decisively bullish, as has become characteristic of the company.” Further, according to the report, management reiterated its 2000 guidance of 17% to 19% top line growth and earnings growth in excess of that rate.” Also according to the report, Management stated that optical networking was an “area[s] in which Lucent has the leadership position in a market and that have growth rates of at least 20%.” 157. Lucent's management's November 11, 1999 guidance to analysts, as reported by Legg Mason, specifically the statement regarding 17 to 19% top line growth, earnings growth in excess of that rate, and a market growth rate of 20% in optical networking was false and, Defendants had actual knowledge that such *statements were false at the time they were made*. Defendant McGinn had been informed by Lucent senior executives that Lucent needed to drastically cut financial projections because its newest products weren't ready yet and sales of older products were going to decline. They knew of the optical networking problems alleged above, including the fact that very little demand existed for the optical networking product Lucent was actually able to sell. Also, Lucent senior management knew that Lucent's recorded revenues did not accurately report sales as the Company engaged in a widespread practice of recording revenue before sales were completed.

158. On November 16, 1999, Morgan Stanley, Dean Witter (“Morgan Stanley”) issued an analyst report in which it issued a “Buy” recommendation and encouraged investors to purchase Lucent stock. In making its recommendation, the analysts relied, in substantial part, on the “guidance” provided by the Company regarding its foreseeable revenue and earnings growth. As evidence of this, immediately following the Lucent conference, the analysts reported, in part, the following:

Summary and Investment Conclusion

We believe that Lucent should be a core holding in the tele-com equipment space. The company has a strong market position in switching and access, wireless infrastructure, optical, and enterprise. The FY2000 revenue growth rate for the company remains in the 17-20% range with EPS growing at a higher rate. We believe that FY2000 should be an

impressive year for the company. We reiterate our Strong Buy rating and \$85 target price, 53 times our C2000 EPS estimate of \$1.61. The company, at its current level of 47 times our C2000 EPS estimate, is less expensive than its leading competitors.

Forecasts Stay Put

The company repeated prior projections of 17-20% revenue growth, gross margins in the mid-to-high 40% range, and operating margins in the mid-teen area. Results for FY2000 should be led by excellent margins and revenue growth from the networking and optical segments. We believe the company could slightly lower overall gross margins to increase market share, which should increase/maintain operating margins in the mid-to-high teen range. We see future improvement in the company's SG&A -- being targeted by 2-3 points for cost savings by management.

* * *

Optical's Not Good. It's Great

We are expecting Lucent's optical business, estimated to be about \$3.5-4.0 billion in FY1999, to increase by 60-70%. The company's DWDM products are expected to increase by 100%, and we believe that the company's OC-48 product should increase in the 50% range. The additional increase should come from the introduction of the company's OC-192 product (see below). Overall, the company's optical business should total almost \$6 billion in FY2000.

Wireless Continues to Ring in Results

Lucent's wireless infrastructure business strengthened in FY99, and we expect further upside in FY2000. The company should exceed the industry's 20-23% growth rate, and we believe margins will remain in the 50-55% range. While competitors have talked about a slowdown in certain international markets, Lucent discussed additional order growth abroad. Further upside to our estimates could result from China, where the company's business looks very promising.

* * *

Software Is Rising

Lucent's software business looks strong and should exceed the industry's 23% five-year CAGR. We believe that customers will look for integrated one-stop network solutions, which should benefit Lucent in software sales. The company's SoftSwitch product, which already has \$100 million in contracts, should be a leading product in this business... We believe that Lucent will add to its software portfolio in FY2000.

Nothing Micro About Microelectronic

Lucent's strong microelectronic business is often overlooked. The business was roughly \$3.7 billion in FY1999, growing over 20% over the preceding year (about 25% of sales are internal). *We believe that growth in this business should remain strong in FY2000, exceeding the market's growth rate.* The company has No. 1 market share in communication semiconductors and continues to grab share. [Emphasis added].

Contrary to the representations made by Lucent management to Morgan Stanley, Lucent's optical business was in decline, and its wireless and software businesses were losing customers.

159. Lucent management's guidance of 17-20% revenue growth, and gross margins in the mid high to 40% range, and operating margins in the mid teen area was false at the time it was issued. Defendants had actual knowledge of its falsity at the time it was made as-described in ,, 145, 147, 150, 151 and 155 above.

160. In the weeks that followed Lucent's conference, other analysts also published reports on Lucent, based primarily on the "guidance" provided by Defendants and their other public statements described above. For example, on December 7, 1999, Robertson Stephens issued a press release on *Business Wire* titled, "*Robertson Stephens Initiates Coverage of LU with a Buy Rating - Increasingly Strong in a Market Undergoing a Demand Tornado,*" in which it announced that it had initiated coverage of Lucent with a "Buy" rating. In addition to announcing this coverage and rating, the Robertson Stephens press release also stated, in part, the following:

"We are initiating coverage of Lucent Technologies with a Buy rating," said [analyst Paul] Silverstein. "In our view, Lucent offers investors an attractive proposition, distinguishing itself as one of the leading, and increasingly strong, competitors in a market undergoing a demand tornado. We believe the global market for communications infrastructure equipment is one of the strongest and fastest growing markets in the world."

"*We believe the company has particularly strong competitive positions in a number of the strongest and fastest growing market segments within the overall communications industry, including optical networking systems and components, wireless infrastructure, WAN packet switching and communications software*" said Silverstein. [Emphasis added.]

161. The analyst upgrades of Lucent did not end with the Robinson Stevens report on December 7, 1999. In fact, the positive analyst reports, which were based primarily on the guidance and other public statements provided by the Company described above, continued until moments before Lucent's belated disclosure that the Company would finally be unable to meet analysts' expectations. As evidence of this, on January 6, 1999, only hours before Defendants made their earnings shortfall announcement, Lehman Brothers issued an analyst upgrade on Lucent stock and raised the target price on Lucent to \$95.00 per share, from the previous target of \$90.00 per share.

162. On December 22, 1999, Lucent filed its 1999 Annual Report with the SEC. In a letter to shareholders which was included in that report, Defendant McGinn stated with regard to Lucent's business prospects, "demand has exploded for networking products and services -- optical, packet, broadband software, semiconductors, wireless and networking consulting -- all areas of major strength for Lucent." The document also contained the following statements about Lucent's business:

Optical networking, which boosts network bandwidth, or the capacity for carrying information, pumps information as pulses of laser light through hair-thin glass strands....With more than 4,000 systems serving customers around the globe, Lucent is *well ahead of its competitors* in the deployment of DWDM technology.

Another section of the Annual Report stated,

* * *

Lucent strengthened its relationship with AT&T in 1999, signing a four year, \$1 billion contract for equipment and services for the next phase of AT&T's nationwide digital PCS wireless network.

[Emphasis added].

163. The statement reproduced above in McGinn's letter to shareholders, and the other statements in the Company's Annual Report quoted above in ,, 162 were materially false and misleading, and were known by Defendants to be materially false and misleading at the time of their publication, or were recklessly disregarded as such for the reasons set forth in ,,,,145, 147, 150,151,155, and 159 above and because:

(a)demand for Lucent's products was not "exploding" rather, the Company was losing business in its optical, wireless, software and international divisions because of delays in new product development design problems and non-competitive pricing. As described in ,,,, 67-73 above, Lucent was not experiencing strong growth in wireless and data networking, but was losing material contracts in these areas, including contracts with AT&T and the Saudi Arabian government to competitors among other reasons, because of design problems and non-competitive prices.

164. On January 6, 2000, only weeks after the Company assured analysts and investors that the Company was poised to meet foreseeable earnings and revenue expectations, Lucent issued a press release, published on *PR Newswire*, in which it announced that results for the first fiscal quarter of 2000 would fall *materially short of analysts' expectations*. According to the press release, the Company announced that it would report quarterly and yearly earnings of only \$0.36 per share and \$1.40 per share respectively, compared with analysts' fiscal first quarter and full fiscal year 2000 estimates of approximately \$0.54 per share and \$1.53 respectively.

165. While the January 6, 2000 announcement provided certain rationales for Lucent's disappointing failure to meet Defendant's prior projections, the stock market's reaction to Lucent's disclosure was dramatic. On January 6, 2000, in composite trading which occurred after the close of trading in New York, Lucent shares fell as much as 27.89%, or approximately \$20.00 per share, to close at \$52.19 per share, a new 52-week low, on extremely heavy trading volume of over 21 million shares.

166. In fact, Lucent's own executives now concede that the Company's problems with OC-192 were the principle cause of Lucent's declining earnings. In an interview with *The New York Times*, published on October 16, 2000, William O'Shea characterized the cause of Lucent's problems this way: "It all boils down to kind of one fundamental thing, and that it, we made a decision around OC-192 and 10 gigabit optical systems that, frankly, we're still living with ... If we had made a different decision and had shown an optical business this year and this quarter the size of Nortel's, we wouldn't even notice the other things we've talked about."

Market Impact of the Deceptions

167. The market for Lucent's common stock was open, well-developed and efficient at all relevant times. As a result of these materially false and misleading statements and failures to disclose, Lucent's common stock traded at artificially inflated prices during the Class Period. The artificial inflation continued at least until the end of the Class Period. Plaintiff and other members of the Class purchased or otherwise acquired Lucent common stock relying upon the integrity of the market price of Lucent's common stock and market information relating to Lucent, and have been damaged thereby.

168. At all relevant times, the material misrepresentations and omissions particularized in this Complaint directly or proximately caused or were a substantial contributing cause of the damages sustained by plaintiff and other members of the Class. As described herein, during the Class Period, Defendants made or caused to be made a series of materially false or misleading statements about Lucent's business, prospects and operations. These material misstatements and omissions had the cause and effect of creating in the market an unrealistically positive assessment of Lucent and its business, prospects and operations, thus causing the Company's common stock to be overvalued and artificially inflated at all relevant times. Defendants' materially false and misleading statements during the Class Period resulted in Lead Plaintiff and the other members of *the Class purchasing the Company's common stock at artificially inflated prices*, thus causing the damages complained of herein.

SCIENTER ALLEGATIONS

169. As alleged herein, Defendants acted with scienter in that the Defendants knew that the public documents and statements issued or disseminated in the name of the Company were materially false and misleading; knew that such statements or documents would be

issued or disseminated to the investing public; and knowingly and substantially participated or acquiesced in the issuance or dissemination of such statements or documents as primary violations of the federal securities laws. As set forth elsewhere herein in detail, Defendants, by virtue of their receipt of information reflecting the true facts regarding Lucent, their control over, and/or receipt and/or modification of Lucent's allegedly materially misleading misstatements and/or their associations with the Company which made them privy to confidential proprietary information concerning Lucent participated in the fraudulent scheme alleged herein. Defendants were motivated to conceal the Company's true financial condition so that the Defendants could maintain their position at the Company; the Company could use Lucent stock to finance acquisitions of other companies which could develop the technology that Lucent itself could not, and so that Lucent insiders could sell their personal holding of Lucent shares for a significant profit.

170. As discussed elsewhere herein, by September 1999, Defendants were well aware that the Company was seriously behind in the development of its OC-192 product, and this fact was discussed by optical networking personnel with members of Lucent senior management, including Harry Bosco, the Group President of Optical Networking. Defendants knew that customers were going elsewhere for OC-192 product, and recognized the lack of any meaningful demand for the optical networking systems that Lucent was actually able to sell, in light of the virtual dearth of manufacturing activity in the optical networking system facility during the early and middle parts of the Class Period.

171. The most senior levels of Lucent management were aware that Lucent was attempting to inflate their sales by a practice which involved shipping products which had serious design or reliability problems, were not yet out of the testing phase, to customers. Indeed, that policy was actually discussed at a meeting between Lucent senior management and the Company's directors in Nuremberg, Germany in September 1999.

172. Lucent management was also well aware of the pervasive practice at the Company of recording sales prematurely or falsely at the end of each quarter to assure that the projections given to Wall Street analysts would be met, and of other steps that were taken in this regard, such as "stuffing the channels", and fraudulently recategorizing overdue receivables so that they *would no longer appear to be uncollectible*. Management expressly noted such problems during the early and middle portions of 1999 and engaged in an abortive effort to "clean up" the situation but backed off from that effort and allowed these wrongful practices to proceed when, shortly before the Class Period began, they recognized that such practices were a necessary component of the Company's effort to report revenue growth consistent with Lucent's prior guidance to the Wall Street community. In or about October 1999, several Lucent executives warned Defendant McGinn that the Company's projections were materially inaccurate because its newest products weren't ready yet and sales of older ones were going to decline. In addition, as alleged above, defendants were aware that a number of Lucent's product lines were encountering declining demand in addition to optical networking, including the Company's wireless, international and switching businesses.

173. Defendant McGinn's scienter can also be inferred from the fact that while he was touting the competitiveness of Lucent's products during the Class Period, he was investing his own money in one of Lucent's competitors. According to a October 19, 2000 registration statement filed with the SEC, McGinn is a limited partner of Zhone Investors FF, LLC the primary investors in Zhone Technologies, Inc. ("Zhone") a data networking company which began operations in September 1999. According to Zhone's registration statement, Lucent is one of Zhone's primary competitors.

174. Defendants were motivated to misrepresent the truth concerning Lucent's business and the success of its products in order to artificially inflate the price of Lucent stock so that the Company could finance acquisition. During the Class Period, Lucent acquired Xedia Companies with a total of more than 3.86 million shares of Lucent Stock, a transaction valued at the time of its occurrence at more than \$279,850,000. The higher Lucent's share price, the less Lucent shares would have to be exchanged to acquire target companies. During the Class Period, Lucent also completed the acquisitions of Excel Switching Corp, on November 4, 1999, in a stock for stock transfer valued at \$1.7 billion.

175. Defendants were also motivated to conceal the true state of Lucent's business to enable Lucent insiders to sell their personal holdings of Lucent shares for a profit. Although Lucent's January 6, 2000 disclosure precipitated a decline in the price of Lucent stock, the market price for shares continued to be artificially inflated as a result of some of the deceptions which occurred during the Class Period until, at least, October 10, 2000.

176. According to First Call Insider Research, during the time from the beginning of the Class Period to October 10, 2000:

(A)Defendant Peterson sold 339,870 shares of Lucent stock that he held directly, receiving thereby proceeds of *approximately \$18,328,216*.

(B)Insider William T. O'Shea, the Executive Vice President and CEO of Lucent's Enterprise segment sold 104, 224 shares of Lucent stock that he held directly, receiving thereby proceeds of approximately \$6,543,183.

(C)Insider Arun N. Netravali, the President of Bell Labs sold 234,864 shares of Lucent stock that he held directly, receiving thereby proceeds of approximately \$14,402,107.

(D)Insider John T. Dickson, the Executive Vice President and CEO of the Microelectronics and Communications Technologies segment sold 137, 288 shares of Lucent stock that he held directly, receiving thereby proceeds of approximately \$6,506,677.

(E)Insider Patricia F. Russo, the Executive Vice President and CEO of the Service Provider Networks sold 100,000 shares of Lucent stock that she held directly, receiving thereby proceeds of approximately \$4,655,000.

(F) Insider Richard J. Rawson, Lucent's Senior Vice President and General Counsel sold 100,000 shares of Lucent stock that he held directly, receiving thereby proceeds of approximately \$5,310,000.

(G) Insider James S. Lusk, Lucent's Senior Vice President and Controller sold 44,000 shares of Lucent stock that he held directly, receiving thereby proceeds of approximately \$2,265,840.

177. Thus, between October 26, 1999 and October 10, 2000, the aforementioned individuals sold an aggregate 1,060,246 shares that they held directly receiving thereby aggregated proceeds of approximately \$58 million.

178. Finally, Defendant McGinn was motivated to conceal the truth about Lucent's operations so that he could maintain his position at the Company. In fact, once the true facts were revealed, McGinn was fired.

Applicability Of Presumption Of Reliance: *Fraud-On-The-Market Doctrine*

179. At all relevant times, the market for Lucent's stock was an efficient market for the following reasons, among others:

(a) Lucent's stock met the requirements for listing, and was listed and actively traded on the New York Stock Exchange, a highly efficient and automated market;

(b) As a regulated issuer, Lucent filed periodic public reports with the SEC and the NYSE;

(c) Lucent regularly communicated with public investors via established market communication mechanisms, including through regular disseminations of press releases on the national circuits of major newswire services and through other wide-ranging public disclosures, such as communications with the financial press and other similar reporting services; and

(d) Lucent was followed by several securities analysts employed by major brokerage firms who wrote reports which were *distributed to the sales force and certain customers of their* respective brokerage firms. Each of these reports was publicly available and entered the public marketplace.

180. As a result of the foregoing, the market for Lucent's stock promptly digested current information regarding Lucent from all publicly available sources and reflected such information in Lucent's stock price. Under these circumstances, all purchasers of Lucent's common stock during the Class Period suffered similar injury through their purchase of Lucent's common stock at artificially inflated prices and a presumption of reliance therefore applies.

NO SAFE HARBOR

181. The statutory safe harbor provided for forward-looking statements under certain circumstances does not apply to any of the allegedly false statements pleaded in this complaint. Many of the specific statements pleaded herein were not identified as “forward-looking statements” when made. To the extent there were any forward-looking statements, there were no meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the purportedly forward-looking statements. Alternatively, to the extent that the statutory safe harbor does apply to any forward-looking statements pleaded herein, Defendants are liable for those false forward-looking statements because at the time each of those forward-looking statements was made, the particular speaker knew that the particular forward-looking statement was false, and/or the forward-looking statement was authorized and/or approved by an executive officer of Lucent who knew that those statements were false when made.

FIRST CLAIM

Violation Of Section 10(b) Of The Exchange Act Against And Rule 10b-5 Promulgated Thereunder Against All Defendants

182. Plaintiff repeats and realleges each and every allegation contained above as if fully set forth herein.

183. During the Class Period, Lucent and the Individual Defendants, and each of them, carried out a plan, scheme and course of conduct which was intended to and, throughout the Class Period, did: (i) deceive the investing public, including plaintiff and other Class members, as alleged herein; (ii) artificially inflate and maintain the market price of Lucent's common stock; and (iii) cause plaintiff and other members of the Class to purchase Lucent's common stock at artificially inflated prices. In furtherance of this unlawful scheme, plan and course of conduct, Defendants, and each of them, took the actions set forth herein.

184. Defendants (a) employed devices, schemes, and artifices to defraud; (b) made untrue statements of material fact and/or omitted to state material facts necessary to make the statements not misleading; and (c) engaged in acts, practices, and a course of business which operated as a fraud and deceit upon the purchasers of the Company's securities in an effort to maintain artificially high *market prices for Lucent's securities in violation of Section 10(b) of the Exchange Act and Rule 10b-5*. All Defendants are sued either as primary participants in the wrongful and illegal conduct charged herein or as controlling persons as alleged below.

185. In addition to the duties of full disclosure imposed on Defendants as a result of their making of affirmative statements and reports, or participation in the making of

affirmative statements and reports to the investing public, Defendants had a duty to promptly disseminate truthful information that would be material to investors in compliance with the integrated disclosure provisions of the SEC as embodied in SEC Regulation S-X (17 C.F.R. Sections 210.01 et seq.) and Regulation S-K ([17 C.F.R. Sections 229.10](#) et seq.) and other SEC regulations, including accurate and truthful information with respect to the Company's operations, financial condition and earnings so that the market price of the Company's securities would be based on truthful, complete and accurate information.

186. Lucent and the Individual Defendants, individually and in concert, directly and indirectly, by the use, means or instrumentalities of interstate commerce and/or of the mails, engaged and participated in a continuous course of conduct to conceal adverse material information about the business, operations and future prospects of Lucent as specified herein.

187. These Defendants employed devices, schemes and artifices to defraud, while in possession of material adverse non-public information and engaged in acts, practices, and a course of conduct as alleged herein in an effort to assure investors of Lucent's value and performance and continued substantial growth, which included the making of, or the participation in the making of, untrue statements of material facts and omitting to state material facts necessary in order to make the statements made about Lucent and its business operations and future prospects in the light of the circumstances under which they were made, not misleading, as set forth more particularly herein, and engaged in transactions, practices and a course of business which operated as a fraud and deceit upon the purchasers of Lucent's common stock during the Class Period.

188. Each of the Individual Defendants' primary liability, and controlling person liability, arises from the following facts: (i) the Individual Defendants were high-level executives and/or directors at the Company during the Class Period and members of the Company's management team or had control thereof; (ii) each of these Defendants, by virtue of his or her responsibilities and activities as a senior officer and/or director of the Company was privy to and participated in the creation, development and reporting of the Company's internal budgets, plans, projections and/or reports; (iii) each of these Defendants enjoyed significant personal contact and familiarity with the other Defendants and was advised of and had access to other members of the Company's management team, internal reports and other data and information about the Company's finances, operations, and sales at all relevant times; and (iv) each of these Defendants was aware of the Company's dissemination of information to the investing public which they knew or recklessly disregarded was materially false and misleading.

189. Defendants had actual knowledge of the misrepresentations and omissions of material facts set forth herein, or acted with reckless disregard for the truth in that they failed to ascertain and to disclose such facts, even though such facts were available to them. Such Defendants' material misrepresentations and/or omissions were done knowingly or recklessly and for the purpose and effect of concealing Lucent's operating condition and future business prospects from the investing public and supporting the

artificially inflated price of its securities. As demonstrated by Defendants' overstatements and misstatements of the Company's business, operations and earnings throughout the Class Period, Defendants, if they did not have actual knowledge of the misrepresentations and omissions alleged, were reckless in failing to obtain such knowledge by deliberately refraining from taking those steps necessary to discover whether those statements were false or misleading.

190. As a result of the dissemination of the materially false and misleading information and failure to disclose material facts, as set forth above, the market price of Lucent's common stock was artificially inflated during the Class Period. In ignorance of the fact that market prices of Lucent's publicly-traded securities were *artificially inflated, and relying directly or indirectly on the* false and misleading statements made by Defendants, or upon the integrity of the market in which the securities trade, and/or on the absence of material adverse information that was known to or recklessly disregarded by Defendants but not disclosed in public statements by Defendants during the Class Period, Plaintiff and the other members of the Class acquired Lucent common stock during the Class Period at artificially high prices and were damaged thereby.

191. At the time of said misrepresentations and omissions, Plaintiff and other members of the Class were ignorant of their falsity, and believed them to be true. Had Plaintiff and the other members of the Class and the marketplace known of the true financial condition and business prospects of Lucent, which were not disclosed by Defendants, Plaintiff and other members of the Class would not have purchased or otherwise acquired their Lucent common stock, or, if they had acquired such common stock during the Class Period, they would not have done so at the artificially inflated prices which they paid. 192. By virtue of the foregoing, Defendants have violated Section 10(b) of the Exchange Act, and Rule 10b-5 promulgated thereunder.

193. As a direct and proximate result of Defendants' wrongful conduct, Plaintiff and the other members of the Class suffered damages in connection with their respective purchases and sales of *the Company's common stock during the Class Period*.

SECOND CLAIM

Violation Of Section 20(a) Of *The Exchange Act Against Individuals Defendants*

194. Plaintiff repeats and realleges each and every allegation contained above as if fully set forth herein.

195. The Individual Defendants acted as controlling persons of Lucent within the meaning of Section 20(a) of the Exchange Act as alleged herein. By virtue of their high-level positions, and their ownership and contractual rights, participation in and/or awareness of the Company's operations and/or intimate knowledge of the Company's financial position and its foreseeable growth and earnings prospects, the Individual

Defendants had the power to influence and control and did influence and control, directly or indirectly, the decision-making of the Company, including the content and dissemination of the various statements which plaintiff contends are false and misleading. The Individual Defendants were provided with or had unlimited access to copies of the Company's reports, press releases, public filings and other statements alleged by Plaintiff to be misleading prior to and/or shortly after these statements were issued and had the ability to prevent the issuance of the statements or cause the statements to be corrected.

196. In particular, each of these Defendants had direct and supervisory involvement in the day-to-day operations of the Company and, therefore, is presumed to have had the power to control or *influence the particular transactions giving rise to the securities violations as alleged herein, and exercised the same.*

197. As set forth above, Lucent and the Individual Defendants each violated Section 10(b) and Rule 10b-5 by their acts and omissions as alleged in this Complaint. By virtue of their positions as controlling persons, the Individual Defendants are liable pursuant to Section 20(a) of the Exchange Act. As a direct and proximate result of Defendants' wrongful conduct, Plaintiff and other members of the Class suffered damages in connection with their purchases of the Company's common stock during the Class Period.

WHEREFORE, Plaintiff prays for relief and judgment, as follows:

(a) Determining that this action is a proper class action and certifying Plaintiff as a class representative under [Rule 23 of the Federal Rules of Civil Procedure](#);

(b) Awarding compensatory damages in favor of Plaintiff and the other Class members against all Defendants, jointly and severally, for all damages sustained as a result of Defendants' wrongdoing, in an amount to be proven at trial, including interest thereon;

(c) Awarding Plaintiff and the Class their reasonable costs and expenses incurred in this action, including counsel fees and expert fees; and

(d) Such other *and further relief as the Court may deem just and proper.*

JURY TRIAL DEMANDED

Plaintiff hereby demands a trial by jury.