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THIS CONSTITUTES NOTICE OF ENTRY  
AS REQUIRED BY FRCP, RULE 77(d).

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CENTRAL DISTRICT OF CALIFORNIA  
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UNITED STATES DISTRICT COURT  
CENTRAL DISTRICT OF CALIFORNIA

DARLENE HANEY, *et al.*,

Plaintiffs,

v.

PACIFIC TELESIS GROUP, *et al.*,

Defendants.

CASE NO. CV 00-758 AHM (MANx)

ORDER 1) GRANTING  
DEFENDANTS' MOTION TO  
DISMISS PLAINTIFFS' FIFTH,  
SEVENTH AND EIGHTH CAUSES OF  
ACTION WITHOUT PREJUDICE AND  
2) GRANTING DEFENDANTS'  
MOTION TO DISMISS PLAINTIFFS'  
SIXTH CAUSE OF ACTION WITH  
PREJUDICE

Docketed  
Copies NTC Sent  
Nov 5 / JS 6  
JS - 2 / JS - 3  
LSD

This putative class action arises out of defendants' allegedly improper sale of stock from two 401(k) plans in which plaintiffs were participants. The proposed class consists of past and present employees of defendants. The named plaintiffs are four current or former employees of defendants Pacific Bell Telephone Company ("Pac Bell"), Pacific Telesis Group ("Pacific Telesis") and SBC Communications, Inc. ("SBC"). These three defendants are related: Pac Bell is a subsidiary of Pacific Telesis, which is, in turn, a subsidiary of SBC. The two remaining defendants are the committees for the 401(k) plans.<sup>1</sup> Plaintiffs allege four causes of action under the Employee Retirement Income Security Act ("ERISA") as well as federal and state securities

<sup>1</sup> The "committee defendants" are 1) the Savings Plan Committee of the Pacific Telesis Group Supplemental Retirement and Savings Plan for Salaried Employees, and the Pacific Telesis Group Supplemental Retirement and Savings Plan for Nonsalaried Employees and 2) the Benefit Plan Committee of the SBC Savings Plan and the SBC Savings and Security Plan.

SEP 20 2000 (63)

1 law claims. Currently before the Court is the motion of defendants Pac Bell, Pacific Telesis and  
2 SBC to dismiss plaintiffs' fifth (federal securities law), sixth (California securities law), seventh  
3 (declaratory relief) and eighth (accounting) causes of action pursuant to F.R.Civ.P. 12(b)(6).

4 **SUMMARY OF CONCLUSION**

5 As set forth more fully below, the Court dismisses plaintiffs' fifth cause of action, the  
6 federal securities law "insider trading" claim, without prejudice because plaintiffs have failed to  
7 meet the heightened pleading requirements for scienter established by the Private Securities  
8 Litigation Reform Act of 1995 ("PSLRA").

9 The Court dismisses plaintiffs' sixth cause of action, the state securities law "insider  
10 trading" claim, with prejudice. This claim, like the federal securities law claim, is based on  
11 defendants' alleged misrepresentations and omissions in connection with the sale of stock owned  
12 by plaintiffs. Accordingly, the Securities Litigation Uniform Standards Act of 1998<sup>2</sup> ("SLUSA")  
13 preempts this claim.

14 Finally, the Court dismisses without prejudice plaintiffs' seventh and eighth claims for  
15 declaratory relief and an accounting. These derivative claims are dependent on the existence of a  
16 viable securities cause of action. As such, the dismissal of plaintiffs' fifth and sixth causes of  
17 action mandates dismissal of these claims as well.<sup>2</sup>

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23 <sup>2</sup> Plaintiffs' opposition brief does not comply with the typeface size requirement of Local  
24 Rule 3.4.1. This brief, had it been set in appropriate typeface, clearly would exceed Local Rule  
25 3.10's twenty-five page limit. Because plaintiffs saw fit to cite to no fewer than 143 federal cases,  
26 many in 56 confusing, lengthy, impenetrable footnotes, they clearly intended to find some manner  
27 to disguise their weak arguments with a meaningless, blunderbuss "weight of the authorities"  
28 approach. Such dubious advocacy! The Court will reject any subsequently-filed documents that do  
not comply with Rule 3.4.1. Plaintiffs' counsel should note that the typeface size requirement  
applies to both text and footnotes. If they repeat this flagrant violation again, they will be  
sanctioned.

1 **FACTUAL ALLEGATIONS**

2 **I. Formation of the Plans**

3 On or about January 1, 1984, Pacific Telesis created two "defined contribution" 401(k)  
4 plans: the Pacific Telesis Group Supplemental Retirement and Savings Plan for Salaried  
5 Employees ("Salaried Plan") and the Pacific Telesis Group Supplemental Retirement and  
6 Savings Plan for Nonsalaried Employees ("Nonsalaried Plan"). Second Amended Complaint  
7 ("SAC") ¶ 71. Both Pacific Telesis and the Pacific Telesis Savings Plan Committee served as  
8 fiduciaries for each Plan. *Id.* at ¶ 72. Each plan initially provided five different funds into which  
9 employee participants could direct their Plan contributions: 1) a Company Stock Fund; 2) a  
10 Money Market Fund; 3) a Bond Fund; 4) a Balanced Fund; and 5) an Equity Fund. *Id.*

11 **II. Creation of the AirTouch Fund**

12 On March 31, 1994, the fiduciaries added a sixth fund option for the Plans: the AirTouch  
13 Common Stock Fund ("AirTouch Fund"). *Id.* at ¶ 73. AirTouch was a wireless  
14 telecommunications company, originally called PacTel Corporation, affiliated with Pacific  
15 Telesis. In April 1994, Pacific Telesis spun off the company which became AirTouch. *Id.* As  
16 part of the spin-off, each holder of Pacific Telesis common stock received shares of AirTouch  
17 stock approximately equivalent to the number of Pacific Telesis shares owned by that  
18 shareholder. *Id.* Plaintiffs all received AirTouch shares and elected to retain their shares in the  
19 AirTouch Fund. *Id.* at ¶¶ 73-74. The AirTouch Fund was a "frozen fund," meaning that  
20 participants could not add to their AirTouch stock holdings. *Id.* at ¶ 75.

21 **III. The SBC Merger and the Prospectus**

22 On April 1, 1996, SBC announced that it would purchase Pacific Telesis. *Id.* at ¶ 76.  
23 SBC and Pacific Telesis consummated the merger on April 1, 1997, and on that date all shares of  
24 PTG common stock converted into SBC common stock. *Id.* Also on April 1, 1997, SBC issued  
25 a single Prospectus<sup>3</sup> for both the Salaried and Nonsalaried Plans. *Id.* at ¶ 78; Def. Request for  
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27 <sup>3</sup> The Prospectus was also a Summary Plan Description. For brevity, the Court will refer to  
28 this document simply as a Prospectus.

1 Judicial Notice (“DRJN”), Ex. 1.<sup>4</sup>

2 The Prospectus contained a detailed 59-page description of both Plans. It described the  
3 various funds available to Plan participants, including the AirTouch Fund. Of particular  
4 importance is the information contained in the Prospectus concerning Plan participants’ transfer  
5 and withdrawal rights:

- 6 • Participants could change the way their future Plan contributions would be invested.  
7 DRJN, Ex 1, p. 11-38.
- 8 • Participants could transfer account balances between the Plans’ different funds (subject to  
9 certain restrictions not relevant here). *Id.* at 11-39.
- 10 • Participants could make withdrawals from their Plan account balances. *Id.* at 11-40.  
11 Withdrawals were paid by a cash distribution. *Id.* at 11-44.

11 The SAC also cites the following Prospectus section:

12 Current participants may also have money invested in the Interest Income Fund  
13 and/or the AirTouch Stock Fund; both funds are closed to new investments. If  
14 you have money in the Interest Income Fund or the AirTouch Stock Fund, you  
15 may leave it there or transfer it to other funds.

15 *Id.* at 11-15. The Prospectus also informed participants that Pacific Telesis “reserve[d] the right  
16 to change or terminate the Plans at any time - during your employment or retirement - for any  
17 reason.” *Id.* at 11-52.

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22 <sup>4</sup> The Court grants defendants’ request for judicial notice of the Prospectus for the Salaried  
23 and Nonsalaried Plans. Because the SAC alleges the contents of the Prospectus, the Court may  
24 consider it in ruling on defendants’ motion. *See Branch v. Tunnell*, 14 F.3d 449, 454 (9th Cir. 1994).  
25 The Court also grants defendants’ request for judicial notice of the SBC Savings Plan Prospectus  
26 because the SAC specifically refers to this document. *See* SAC ¶ 150. The Court denies plaintiffs’  
27 motion to strike defendants’ citations to two unpublished district court decisions and the complaint  
28 from another case pending before this Court. Ninth Circuit Rule 36-1, by its plain language, applies  
only to decisions of the Court of Appeals. Rule 36-1 does not preclude citation of unpublished  
district court decisions. Moreover, the Court may take judicial notice of the complaint from another  
case because a complaint is a matter of public record. *See MGIC Indemnity Corp. v. Weisman*, 803  
F.2d 500, 504 (9th Cir. 1986).

1 **IV. Liquidation of the AirTouch Fund**

2 Plaintiffs allege that, subsequent to SBC's acquisition of Pacific Telesis, defendants  
3 decided to liquidate the AirTouch Fund and replace Plan participants' AirTouch shares with SBC  
4 shares. SAC ¶ 79. Plaintiffs contend that defendants made this decision "for at least two self-  
5 interested reasons:"

6 1. They wanted to create additional demand for SBC shares and hence drive up, or  
7 at least help maintain, SBC's share price; and

8 2. They wanted to aid SBC in creating a group of SBC-friendly shareholders via  
9 the SBC Shares Fund, particularly after the recapitalization of SBC on April 24,  
1998.

10 *Id.* Plaintiffs do not contend that defendants sought to pocket any of the proceeds from the  
11 liquidation of the AirTouch Funds. Rather, the proceeds were used to purchase SBC shares for  
12 participants' Plan accounts. Plaintiffs contend that the replacement of AirTouch stock with SBC  
13 stock was a poor investment decision because AirTouch was a "highly promising investment"  
14 and defendants knew or should have known that a "bidding war" for AirTouch was ongoing and  
15 would drive up the price of AirTouch stock even farther. *Id.* at ¶¶ 81-82. Moreover, participants  
16 already held SBC stock in their Plan portfolios and the replacement of AirTouch stock with  
17 additional SBC stock would reduce the diversification of the portfolios. *Id.* at ¶ 82.

18 **A. The Salaried Plan**

19 Plaintiffs' allegations concerning the Salaried Plan are threadbare. On May 1, 1998,  
20 defendants "froze" the Salaried Plan's AirTouch Fund, meaning participants could no longer  
21 withdraw stock or its cash equivalent from the Fund after that date. *Id.* at ¶ 84. Between May 1  
22 and July 1, 1998, defendants sold off the AirTouch stock held by Salaried Plan participants  
23 (including plaintiffs Weinald, Takashima and Wilson) worth approximately \$275 million.<sup>5</sup> *Id.*  
24 Defendants used the sale proceeds to purchase SBC stock for the participants' Plan accounts,  
25 creating demand for SBC stock that did not otherwise exist. *Id.*

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27 <sup>5</sup> Elsewhere, plaintiffs contend that defendants began selling off the Salaried Plan's AirTouch  
28 Fund in April 1997. *Id.* at ¶ 81. This statement appears to be erroneous.

1 Plaintiffs contend that defendants failed to give the Salaried Plan participants “clear and  
2 timely notice” of the impending sale and also failed to give adequate notice regarding 1) using  
3 the proceeds of the sale to purchase SBC stock and 2) participants’ rights to avoid that  
4 “mapping” (purchase of SBC stock) by exercising their “in-service withdrawal rights” (if still  
5 employed) or rolling over their AirTouch shares into another IRA (if no longer employed). *Id.* at  
6 ¶¶ 85-86. Plaintiffs do not provide any examples of this purportedly insufficient notice. Rather,  
7 they allege that this notice was “similar to the notice provided to participants in the Nonsalaried  
8 Plan.” *Id.*

9 **B. The Nonsalaried Plan**

10 The SAC’s allegations focus on defendants’ liquidation of the AirTouch stock held by  
11 Nonsalaried Plan participants. On November 1, 1998, defendants froze the Nonsalaried Plan’s  
12 AirTouch Fund. *Id.* at ¶ 88. Between that date and January 1, 1999, defendants sold the  
13 AirTouch stock held by the Nonsalaried Plan participants - a total of approximately \$360 million  
14 - and used the proceeds to go into the market and purchase SBC stock for the participants’ Plan  
15 accounts. *Id.*

16 Plaintiffs allege that defendants failed to give Nonsalaried Plan participants “clear and  
17 timely notice of the liquidation process and their rights to avoid such liquidation.” *Id.* at ¶ 90.<sup>6</sup>  
18 Plaintiffs base this allegation on three “Benefit Briefs” and two “Benefit Bulletins” sent to  
19 Nonsalaried Plan participants between June and October 1998.<sup>7</sup> They contend that these Briefs  
20 and Bulletins contained material omissions and were not sent in such a manner as to attract  
21 attention to the importance of their contents, *e.g.*, by overnight mail or with conspicuous  
22 markings. *Id.* at ¶ 92.

23 ///

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25  
26 <sup>6</sup> The rights to avoid liquidation were based on the same provisions described above:  
either in-service withdrawal or rollover into an IRA.

27  
28 <sup>7</sup> These Bulletins are pertinent only to the Nonsalaried Plan participants because by June 1,  
1998 defendants had already sold the Salaried Plan participants’ AirTouch stock. *See id.* at ¶ 84.

1           **1.     June 1998 Benefit Bulletin Entitled “New Bargaining Agreements Enhance**  
2           **Benefits”**

3           This Bulletin stated, in relevant part:

4           On January 1, 1999, or as soon afterward as is administratively feasible, the  
5           [Nonsalaried Plan] . . . will merge into the SBC Savings and Security Plan . . .  
6           Your account will be transferred into SBC fund options that are very similar to the  
7           [Pacific Telesis] fund options you have at th[is] time.

8           Prior to the merger of [Pacific Telesis] plan with the SBC plan, shares from the  
9           AirTouch Stock Fund will be sold and replaced by shares of SBC common stock.  
10          Beginning about two months before the merger, you will not be able to initiate  
11          transfers from the AirTouch Stock Fund.

12          *Id.* at ¶ 94; DRJN, Ex. 3.<sup>8</sup>

13           **2.     August 1998 Benefit Brief Entitled “Savings Plan Merger Will Take Place in**  
14           **January”**

15          This Brief stated, in relevant part:

16          The [Pacific Telesis Nonsalaried Plan] will merge into the SBC Savings and  
17          Security Plan on or shortly after January 1, 1999. If you participate in the [Pacific  
18          Telesis Nonsalaried Plan], your account will be transferred into SBC fund options  
19          that are very similar to the [Pacific Telesis] fund options that you have at the time  
20          of the merger.

21          ...

22           **The AirTouch Stock Fund**

23          Prior to the merger of the [Pacific Telesis Nonsalaried Plan] into the SBC Plan,  
24          shares from the AirTouch Stock Fund will be sold and replaced with shares of  
25          SBC common stock. If you have a balance in the AirTouch Stock Fund, you'll  
26          have until 1:00 p.m. PT (the time the New York Stock Exchange closes) on  
27          October 30, 1998 to transfer any balance you have in the AirTouch Stock Fund  
28          into any other [Pacific Telesis] plan fund (except the PTG plan Interest Income  
29          Fund, which is closed to new investment). You can request a transfer of your  
30          AirTouch fund balance until 1:00 p.m. PT on October 30, 1998 by calling the  
31          SBC Savings Plan Service Center at 1-800-22 ONLY-U (1-800-226-6598). No  
32          transfers will be permitted after that date.

33          SAC ¶ 98; DRJN, Ex. 4. The August 1998 Benefit Brief also contained a summary of the  
34          different features offered by the Pacific Telesis Nonsalaried Plan and the SBC Plan. DRJN, Ex.  
35          4.

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36  
37           <sup>8</sup> The Court grants defendants' request for judicial notice of the five Benefit Bulletins  
38          and Briefs (DRJN Exs. 3-7). *See* n. 3, *supra*.

1           **3. The October 1998 mailings**

2           **a.     First October 1998 Benefit Brief Entitled "Look for Changes in PTG**  
3           **Supplemental Retirement and Savings Plan - Especially AirTouch Stock**  
4           **Fund"**

4           Plaintiffs contend that "defendants sent a final notice to Nonsalaried Plan participants  
5           sometime in October 1998." SAC ¶ 100. The SAC then quotes from an October 1998 Benefit  
6           Brief. That Benefit Brief provides, in relevant part:

7           **It's a Good Time to Review Your Savings Plan Investments**

8           When was the last time you took a good look at your savings plan portfolio? As  
9           you know, the PTG [Nonsalaried Plan] will merge into the SBC Savings and  
10           Security Plan beginning January 1, 1999, and your assets will be transferred into  
11           fund options similar to those you currently have in your PTG Plan. Right now is  
12           a good time to review your savings plan investments and think about whether they  
13           reflect your investment strategy.

14           If you decide you're satisfied with your savings plan portfolio the way it is, you  
15           don't have to do anything. Your account will be transferred into SBC fund  
16           options that are similar to those you have now. If you decide you do want to  
17           make changes prior to the merger, you can do so through December 31 - except in  
18           the case of the AirTouch Stock Fund - as long as it has been three months since  
19           your last fund transfer.

20           ....  
21           **If You Have a Balance in the AirTouch Stock Fund**

22           If you have a balance in the AirTouch Stock Fund of your PTG Nonsalaried  
23           Savings Plan, you should be aware that, as of October 30, the AirTouch Stock  
24           Fund will be renamed the SBC Shares Transition Fund, and the AirTouch shares  
25           remaining in the Fund will be sold and replaced with SBC shares.

26           If you wish, you may transfer any balance held in the AirTouch Stock Fund to  
27           another PTG plan fund option before the close of the stock market on October 30  
28           (except the PTG plan Interest Income Fund, which is closed to new investment).  
29           You can transfer AirTouch funds once until 1:00 p.m. Pacific Time on October 30  
30           by calling the Service Center. If you decide not to transfer your AirTouch Stock  
31           Fund balance by October 30, your balance will be in the SBC Shares Transition  
32           Fund. You cannot transfer assets out of the SBC Shares Transition Fund. By  
33           December 31, all the AirTouch Stock will be sold and the proceeds invested in  
34           SBC shares.

35           If you request a withdrawal or distribution from the PTG plan in November or  
36           December and part of your PTG plan account is invested in the SBC Shares  
37           Transition Fund, you may ask for that portion of your withdrawal or distribution  
38           to be made in shares, rather than in cash, and you will receive SBC shares.  
39           AirTouch shares will not be distributed for withdrawals or distributions requested  
40           after October.

41           DRJN, Ex. 7.

42           ///

43           ///

1           **b. Second October 1998 Benefit Brief**

2           Although the narrative section of the SAC refers only to the first October 1998 mailing,  
3 plaintiffs later allege that defendants sent two additional mailings to Nonsalaried Plan  
4 participants in October 1998.<sup>9</sup> One of these mailings was another Benefit Brief. This Brief  
5 contained an advisory on the pending sale of the AirTouch Fund identical to the advisory in the  
6 August 1998 Benefit Brief:

7           **The AirTouch Stock Fund**

8           Prior to the merger of the [Pacific Telesis Nonsalaried Plan] into the SBC Plan,  
9 shares from the AirTouch Stock Fund will be sold and replaced with shares of  
10 SBC common stock. If you have a balance in the AirTouch Stock Fund, you'll  
11 have until 1:00 p.m. PT (the time the New York Stock Exchange closes) on  
12 October 30, 1998 to transfer any balance you have in the AirTouch Stock Fund  
into any other [Pacific Telesis] plan fund (except the PTG plan Interest Income  
Fund, which is closed to new investment). You can request a transfer of your  
AirTouch fund balance until 1:00 p.m. PT on October 30, 1998 by calling the  
SBC Savings Plan Service Center at 1-800-22 ONLY-U (1-800-226-6598). No  
transfers will be permitted after that date.

13 SAC ¶ 153(e); DRJN, Ex. 6.

14 This Benefit Brief also contained a summary of the different features offered by the Pacific  
15 Telesis Nonsalaried Plan and the SBC Plan similar to that contained in the August 1998 Benefit  
16 Brief.

17           **c. Third October 1998 Benefit Brief**

18           This undated Benefit Brief states, in relevant part:

19           **AirTouch Stock Fund Reminder**

20           The PTG [Nonsalaried Plan] will merge into the SBC Savings and Security Plan  
21 at the beginning of 1999. Prior to the merger, shares from the AirTouch Stock  
22 Fund will be sold and replaced with shares of SBC common stock.

23           If you participate in the AirTouch Stock Fund, remember that there will be a  
24 period of approximately two months before the merger when you will not be able  
25 to initiate transfers from the AirTouch Stock Fund. You'll receive more  
26 information about the merger and the AirTouch Stock Fund when the exact dates  
27 have been determined.

28 SAC ¶ 153(a); DRJN, Ex. 5.

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<sup>9</sup> Plaintiffs do not allege the order in which defendants sent the three October 1998 mailings  
or the precise dates on which Nonsalaried Plan participants received them.

1 Between November 1, 1998 and January 1, 1999, defendants sold off the Nonsalaried  
2 Plan participants' AirTouch holdings. SAC ¶ 88. The SAC does not allege what percentage of  
3 Nonsalaried Plan participants with shares in the AirTouch Fund elected to transfer or withdraw  
4 their shares from that fund. However, plaintiff Haney and other putative Nonsalaried Plan class  
5 members did not transfer or withdraw their AirTouch shares, so the shares were sold and  
6 replaced with SBC common stock.

#### 7 **V. The AirTouch-Vodafone Merger**

8 Between September 1998 and January 1999, the time period during which Nonsalaried  
9 Plan participants had to elect to retain their AirTouch stock, AirTouch was engaged in merger  
10 negotiations with Vodafone Global. *Id.* at ¶ 154. It is undisputed that none of the notices sent to  
11 Plan participants regarding the AirTouch Fund liquidation mentioned these merger discussions or  
12 the possibility of a merger. Plaintiffs contend that the possibility of AirTouch-Vodafone merger  
13 was material information because a merger would cause the value of AirTouch stock to increase.  
14 *Id.* at ¶¶ 153(e), 154.

15 In mid-January 1999, AirTouch and Vodafone publicly announced their merger.<sup>10</sup> *Id.*  
16 Due in large part to the merger, the value of AirTouch stock (now Vodafone AirTouch) "has  
17 essentially tripled in value since SBC liquidated the Salaried and Nonsalaried AirTouch Stock  
18 Funds in the Spring and late Fall of 1998." *Id.* at ¶ 104. Plaintiffs contend that the cumulative  
19 loss suffered by participants in the Salaried and Nonsalaried Plans who allowed defendants to  
20 sell their AirTouch shares is approximately \$1.15 billion, an average of \$28,750 for each of the  
21 estimated 40,000 class members. *Id.*

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26 <sup>10</sup> Defendants request that the Court take judicial notice of Vodafone's January 5,  
27 1999 news release stating that it might merge with AirTouch and AirTouch's January 15, 1999 news  
28 release announcing the merger. DRJN, Exs. 8-9. The Court grants that request for the limited  
purpose of confirming that the SAC accurately alleges that dates on which the merger was publicly  
announced. *See* n. 3, *supra*.

1 **VI. SBC's April 2000 Statement**

2 In April 2000, after plaintiffs initiated this action, SBC stated that "[n]o SBC savings plan  
3 includes direct stock ownership in any other company that is not related to SBC." *Id.* at ¶ 155(a).  
4 As discussed below, plaintiffs contend that this statement is materially inconsistent with  
5 defendants' representation in the April 1997 Prospectus that Plan participants who held AirTouch  
6 stock in the AirTouch Fund could "leave it there or transfer it to other funds," and this  
7 inconsistency reveals defendants' intent not to allow participants to retain their AirTouch shares.  
8 *Id.*

9 **LEGAL STANDARDS**

10 On a motion to dismiss pursuant to Rule 12(b)(6) for failure to state a claim, the  
11 allegations of the complaint must be accepted as true and are to be construed in the light most  
12 favorable to the nonmoving party. *Wylar Summit Partnership v. Turner Broadcasting System, Inc.*,  
13 135 F.3d 658, 661 (9th Cir. 1998). "[A] complaint should not be dismissed unless it  
14 appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which  
15 would entitle him to relief." *Id.* Where a motion to dismiss is granted, a district court should  
16 provide leave to amend unless it is clear that the complaint could not be saved by any  
17 amendment. *Chang v. Chen*, 80 F.3d 1293, 1296 (9th Cir. 1996).

18 **DISCUSSION**

19 **Part I**

20 **The Federal Securities Fraud Claim - Fifth Cause of Action**

21 Virtually all of the SAC's factual allegations concern defendants' sale of the AirTouch  
22 stock held by participants in the Nonsalaried Plan. Accordingly, in Subpart A, the Court  
23 analyzes the SAC's allegations with respect to the Nonsalaried Plan.<sup>11</sup> In Subpart B, the Court  
24 analyzes the Salaried Plan participants' federal securities fraud claim.

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27 \_\_\_\_\_  
28 <sup>11</sup> Of the named plaintiffs, only Darlene Haney was a participant in the Nonsalaried Plan.

**Subpart A**  
**The Nonsalaried Plan**

**I. Background**

The SAC's fifth cause of action alleges, upon information and belief, that defendants' sale of plaintiffs' AirTouch stock violated § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and Rule 10b-5. Section 10(b) provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange-

...  
(b) to employ, in connection with the purchase or sale of any security registered on a national securities exchange or any securities not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary and appropriate in the public interest or for the protection of investors.

Rule 10b-5 provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5.

"[T]o prove violation of either Section 10(b) or Rule 10b-5, the private plaintiff must demonstrate that the alleged fraud occurred 'in connection with the purchase or sale of a security.'" *Ambassador Hotel Co, Ltd. v. Wei-Chuan Investment*, 189 F.3d 1017, 1025 (9th Cir. 1999). The plaintiff must then prove five elements:

- 1) misrepresentation (or omission, where there exists some duty to disclose);
- 2) materiality;
- 3) scienter (intent to defraud or deceive);
- 4) reliance; and

1 5) causation (both actual and proximate).

2 *Id.*

3 On this motion to dismiss, defendants do not challenge that the alleged fraud took place  
4 in connection with the sale of a security, *i.e.*, the AirTouch stock. However, defendants contend  
5 that plaintiffs have failed to adequately plead any of the remaining five elements. The Court now  
6 turns to these elements.

7 **II. Material Misrepresentation/Omission**

8 The PSLRA modified the pleadings requirements for both the misrepresentation and  
9 scienter elements of a federal securities fraud claim. With respect to the misrepresentation  
10 element, the PSLRA provides:

11 **Misleading statements and omissions**

12 In any private action arising under this chapter in which the plaintiff alleges that  
the defendant-

- 13 (A) made an untrue statement of a material fact; or  
14 (B) omitted to state a material fact necessary in order to make the  
statements made, in light of the circumstances in which they were  
15 made, not misleading:

16 the complaint shall specify each statement alleged to have been misleading, the  
reason or reasons why the statement is misleading, and, if an allegation regarding  
17 the statement or omission is made on information and belief, the complaint shall  
state with particularity all facts on which that belief is formed.

18 15 U.S.C. § 78u-4(b)(1). This subsection requires a plaintiff relying on information and belief,  
19 as is the case here, *see* SAC ¶ 150, to plead the facts underlying her belief “in great detail.” *In re*  
20 *Silicon Graphics Sec. Litig.*, 183 F.3d 970, 985 (9th Cir. 1999) (“*Silicon Graphics*”). As such,  
21 plaintiffs must satisfy the PSLRA’s particularity requirement.<sup>12</sup>

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26 <sup>12</sup> Plaintiffs cite *In re Petsmart, Inc. Sec. Litig.*, 61 F. Supp.2d 982 (D. Ariz. 1999) for the  
27 proposition that “the pleading standards are ‘relaxed’” where a plaintiff pleads on information and  
28 belief. *Opp.* at 5. However, plaintiffs must nevertheless satisfy the PSLRA’s standard for  
information and belief pleadings.

1 The SAC alleges that the five Benefit Briefs and Bulletins sent by defendants to  
2 Nonsalaried Plan participants between June and October 1998 contained misleading statements  
3 and omissions regarding the sale of the participants' stock in the AirTouch Fund. Plaintiffs  
4 contend that the Briefs and Bulletins were misleading because:

- 5 1) defendants did not disclose the possibility of an AirTouch-Vodafone  
6 merger;
- 7 2) defendants did not disclose that plaintiffs had a right to withdraw their  
8 shares from the AirTouch Fund pursuant to their "in service withdrawal  
9 rights;"
- 10 3) defendants did not disclose that plaintiffs had a right to roll their AirTouch  
11 shares out of the Pacific Telesis Plan and into another qualified plan or a  
12 rollover IRA;
- 13 4) defendants presented the sale of plaintiffs' AirTouch shares as a "fait  
14 accompli;" and
- 15 5) the June 1998 Benefit Brief informed plaintiffs that their assets in the  
16 Pacific Telesis plans would be transferred into the SBC Plan funds "very  
17 similar to those you currently have in your PTG Plan" but did not inform  
18 plaintiffs that the replacement of their AirTouch shares with SBC shares  
19 would reduce the diversification of each account that already held SBC  
20 shares.

21 The Court considers each of these alleged misrepresentations and omissions in turn to determine  
22 whether they satisfy the particularity requirement of § 78u-4(b)(1).

#### 23 **A. The AirTouch-Vodafone Merger**

24 Defendants do not challenge plaintiffs' contention that AirTouch and Vodafone were  
25 engaged in merger discussions during the latter part of 1998. Defendants also do not contest that  
26 none of the Benefit Bulletins and Briefs sent between June and October 1998 disclosed these  
27 merger negotiations to Plan participants. However, defendants contend that plaintiffs have failed  
28 to adequately plead 1) that defendants knew of the merger discussions before the discussions  
became public knowledge and 2) even assuming defendants knew of the merger discussions, that  
by November 1998 the discussions were material.

In the scienter section of this Order(Section III.B.), the Court discusses plaintiffs'  
allegations that defendants knew of the non-public merger discussions. In this section, the Court  
discusses the materiality of any omission assuming that plaintiffs could adequately plead that

1 defendants did possess such knowledge.

2 “[A]n omitted fact is material if there is a substantial likelihood that a reasonable  
3 shareholder would consider it important in deciding how to vote.” *Basic, Inc. v. Levinson*, 485  
4 U.S. 224, 231, 108 S.Ct. 978, 983, 99 L.Ed.2d 194 (1988) (citing *TSC Indus., Inc. v. Northway,*  
5 *Inc.*, 426 U.S. 438, 449, 96 S.Ct. 2126, 2132, 48 L.Ed.2d 757 (1976)). Stated otherwise, “there  
6 must be a substantial likelihood that the disclosure of the omitted fact would have been viewed  
7 by the reasonable investor as having significantly altered the ‘total mix’ of information made  
8 available.” *Id.* at 231-232, 108 S.Ct. at 983 (citing *TSC Indus., Inc.*, 426 U.S. at 449, 96 S.Ct. at  
9 2132). Whether merger negotiations are material is a fact-specific determination based on the  
10 both the probability that the merger will occur and the magnitude of the merger. *Id.* at 239, 108  
11 S.Ct. at 987. In order to assess the probability of the merger, the factfinder generally should look  
12 to the “indicia of interest in the transaction at the highest corporate levels” including board  
13 resolutions, instructions to investment bankers, and actual negotiations. *Id.* However, “[n]o  
14 particular event or factor short of closing the transaction need be either necessary or sufficient by  
15 itself to render merger discussions material.” *Id.*

16 Here, defendants contend that plaintiffs have failed to plead with the requisite “great  
17 detail” any facts suggesting that the merger negotiations between AirTouch and Vodafone were  
18 material at the time defendants froze the AirTouch Fund in the Salaried and Nonsalaried Plans.  
19 The Court agrees. In any amended pleading, plaintiffs shall specify precisely how the AirTouch-  
20 Vodafone merger negotiations were material.<sup>13</sup>

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21  
22 <sup>13</sup> Plaintiffs also contend that between September 1998 and January 1999 defendants knew  
23 of the ongoing merger discussions because “[t]he existence of these merger discussions was reported  
24 in the press at that time.” SAC ¶ 155(b). As discussed below, an omission may be material where  
25 the omitted information is not already part of the “total mix” of information available to the public.  
26 The “total mix” of information may include “information already in public domain and facts known  
27 or reasonably available to shareholders.” *United Paperworkers Int’l v. Int’l Paper*, 985 F.2d 1190,  
28 1199 (2d Cir. 1993) (citing *Rodman v. Grant Foundation*, 608 F.2d 64, 70 (2d Cir. 1979)).  
Therefore, if the press was reporting the possibility of an AirTouch-Vodafone merger, then this  
information was likely part of the “total mix” of information reasonable available to plaintiffs. If  
so, then even assuming that defendants knew of the possible merger, their failure to disclose such  
information would not be material.

1           **B.     Plaintiffs' Withdrawal and Rollover Rights**

2           The Benefit Briefs and Bulletins informed each plaintiff that her AirTouch shares would  
3 be liquidated and replaced with SBC stock unless she elected to transfer her AirTouch Fund  
4 balance to another Plan fund. DRJN, Exs. 3-7. The Briefs and Bulletins did not inform Plan  
5 participants that they could also avoid the liquidation by withdrawing their AirTouch shares from  
6 the Plan or rolling the shares over into an IRA. Plaintiffs do not dispute that the 1997 Prospectus  
7 did inform Plan participants about their withdrawal and rollover rights. However, they contend  
8 that this "kernel of information" was inadequate to inform plaintiffs of their rights over a year  
9 later when plaintiffs were faced with the decision of what to do with their AirTouch shares. Opp.  
10 at 7.

11           Defendants argue that the 1997 Prospectus informed plaintiffs of their withdrawal and  
12 rollover rights. Defendants couch the issue as whether they had a "duty to reiterate" plaintiffs'  
13 withdrawal and rollover rights in the Benefit Briefs and Bulletins given that plaintiffs already  
14 possessed this information. The Court views this as a question of materiality. On this Rule 12  
15 motion, the Court's inquiry is limited to the issue of whether defendants' failure to recite  
16 plaintiffs' withdrawal and rollover rights in the Benefit Briefs and Bulletins was immaterial as a  
17 matter of law. Materiality is generally an issue for the trier of fact. *Fecht v. Price Co.*, 70 F.3d  
18 1078, 1080 (9th Cir. 1995), *cert. denied*, 517 U.S. 1136, 116 S.Ct. 1422, 134 L.Ed.2d 547  
19 (1996). However, materiality may be resolved as a matter of law "if the adequacy of the  
20 disclosure or the materiality of the statement is so obvious that reasonable minds could not differ  
21 ... ." *Id.* at 1081 (citations omitted).

22           Case law does provide some support for the proposition that where information has been  
23 made available to shareholders, a defendant's failure to disclose that information later on may be  
24 immaterial as a matter of law. In *Berkowitz v. Conrail, Inc.*, 1997 WL 611606 (E.D. Pa. Sept.  
25 25, 1997), the district court dismissed the plaintiff's claim that the defendant fraudulently failed  
26 to disclose that it had been approached by another company regarding a possible merger. The  
27 district court based its ruling, in part, on the fact that a newspaper article relied upon by the  
28 plaintiff revealed that very information:

1 [T]here can be no liability under the securities laws because of an alleged failure  
2 to disclose information that is already available to the public. This is because  
such information is already part of the “total mix.”

3 *Id.* at \* 11 (citation omitted).<sup>14</sup> See also *Pacheco v. Cambridge Technology Partners (Mass.),*  
4 *Inc.*, 85 F. Supp.2d 69, 78-79 (D. Mass. 2000) (citing *Berkowitz* for proposition that “allegedly  
5 undisclosed information which the market has already perceived is immaterial as matter of law”);  
6 *Frigitemp Corp. v. Financial Dynamics Fund*, 524 F.2d 275, 282 (2d Cir. 1975) (affirming  
7 dismissal of securities fraud claim based on the defendants’ alleged failure to disclose purchases  
8 of shares because a party’s “reasonable belief that the other party already has access to the facts  
9 should excuse him from new disclosures which reasonably appear to be repetitive” and plaintiffs  
10 had access to transfer sheets describing defendants’ purchases).<sup>15</sup>

11 At the hearing on this motion, defense counsel argued that plaintiffs had no “duty to  
12 speak” because the information contained in the Prospectus concerning plaintiffs’ withdrawal  
13 and rollover rights remained accurate through 1998 when defendants sent the Benefit Bulletins  
14 and Briefs. Defense counsel further contended, also for the first time, that any omission was  
15 immaterial because defendants complied with applicable disclosure requirements under ERISA  
16 and the Internal Revenue Code, citing *Press v. Quick & Reilly, Inc.*, 218 F.3d 121 (2d Cir. 2000).

17 On this motion, the Court need not make a definitive ruling as to whether defendants’  
18 failure to recite participants’ withdrawal and rollover rights in the Benefit Bulletins and Briefs  
19 could constitute a material omission under the securities laws. Plaintiffs will be permitted to file  
20 an amended complaint. If the amended complaint contains allegations concerning a failure to  
21 disclose withdrawal and rollover rights and defendants believe that such allegations are deficient,  
22 then defendants may brief these arguments in a motion to dismiss following good faith  
23 compliance with Local Rule 7.4.1.

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24  
25 <sup>14</sup> Defendants also cite *Villers v. Board of Trustees, Sheet Metal Workers’ National Pension*  
26 *Fund*, 901 F. Supp. 1011 (S.D.W.Va. 1995) for the proposition that “there is no legal duty to  
reiterate things already disclosed.” However, *Villers* is an ERISA case and does not assist the Court  
27 in analyzing defendants’ duty to disclose in the context of an alleged securities law violation.

28 <sup>15</sup> The same standard of materiality applies to misleading proxy statements under Rule 14a-9  
and fraud in connection with the sale of securities under Rule 10b-5. See *Basic, supra*.

1           **C. The “Fait Accompli”**

2           Plaintiffs contend that the Benefit Briefs and Bulletins misled Nonsalaried Plan  
3 participants by presenting the sale of their AirTouch shares as a “fait accompli.” This contention  
4 might contain some merit if the Briefs and Bulletins had failed to present participants with any  
5 option other than allowing defendants to sell their AirTouch shares. But such was not the case.  
6 Each of the five Briefs and Bulletins references the participants’ ability to transfer their account  
7 balances out of the AirTouch Fund before the Fund’s liquidation. In August 1998, over two  
8 months prior to the “freezing” of the Fund, defendants provided participants with specific and  
9 detailed information on transferring their account balances out of the AirTouch Fund, DRJN, Ex.  
10 4, and defendants repeated this specific information on two occasions in October 1998. *Id.* at  
11 Exs. 6-7. It is true that in the Briefs and Bulletins defendants did not provide plaintiffs with  
12 information regarding their withdrawal and rollover rights; however, that omission cannot  
13 reasonably lead to, much less compel, the conclusion that defendants presented the liquidation of  
14 the AirTouch Fund as a “fait accompli.” By providing participants with information regarding  
15 their transfer rights, defendants gave them clear notice that they could avoid the liquidation if  
16 they so desired. As such, plaintiffs’ allegations fail to show how defendants presented the  
17 liquidation as a “fait accompli.” This allegation fails as a matter of law, and plaintiffs shall not  
18 renew it in any amended complaint.

19           **D. Reduction of Diversification**

20           Plaintiffs also contend that defendants’ representations that the SBC Plan funds were  
21 “similar” to the Pacific Telesis Nonsalaried Plan options were misleading. SAC ¶ 153(b),(e).  
22 This is so, plaintiffs argue, because defendants did not inform participants holding AirTouch  
23 stock that the replacement that stock with SBC stock (which they already held in their  
24 Nonsalaried Plan accounts) would reduce the diversification of their accounts.

25           Plaintiffs’ contention borders on frivolous. Suppose that A owns a basket that contains  
26 apples, oranges and grapes and B owns a basket that contains apples and oranges. If A and B  
27 each know what fruits are in his basket and in the other’s basket and they agree to trade baskets,  
28 must B inform A that A’s new basket will be less diverse than his original basket? Defendants’

1 alleged failure to inform plaintiffs that their portfolios would lose diversity was immaterial as a  
2 matter of law. This contention also shall not be renewed in any amended complaint.

### 3 **E. Summary of Conclusion**

4 Should plaintiffs elect to amend, they may renew their allegations regarding defendants'  
5 purported knowledge of the AirTouch-Vodafone merger and defendants' failure to recite  
6 participants' withdrawal and rollover rights in the Benefit Briefs and Bulletins. However, any  
7 amended complaint shall not renew plaintiffs' allegations concerning either the "fait accompli"  
8 or the reduction of diversification.

## 9 **III. Scienter**

### 10 **A. The PSLRA's Heightened Pleading Requirement**

11 In the context of § 10(b), scienter is a "mental state embracing intent to deceive,  
12 manipulate, or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193-94 n. 12, 96 S.Ct.  
13 1375, 1381 n. 12, 47 L.Ed.2d 668 (1976). Prior to enactment of the PSLRA, a securities fraud  
14 plaintiff could plead scienter under F.R.Civ.P. 9(b) "simply by saying that scienter existed." *In*  
15 *re Glenfed Sec. Litig.*, 42 F.3d 1541, 1547 (9<sup>th</sup> Cir. 1994) (en banc). However, the PSLRA  
16 heightened this pleading requirement:

17 In any private action arising under this chapter in which the plaintiff may recover  
18 money damages only on proof that the defendant acted with a particular state of  
19 mind, the complaint shall, with respect to each act or omission alleged to violate  
20 this chapter, *state with particularity facts giving rise to a strong inference that the*  
21 *defendant acted with the required state of mind.*

22 15 U.S.C. § 78u-4(b)(2) (emphasis added).

23 The Ninth Circuit has adopted a stringent interpretation of the PSLRA's requirement that  
24 a plaintiff plead facts giving rise to a "strong inference" of scienter:

25 We hold that a private securities plaintiff proceeding under the PSLRA must  
26 plead, in great detail, facts that constitute *strong circumstantial evidence of*  
27 *deliberately reckless or conscious misconduct.*

28 *Silicon Graphics*, 183 F.3d at 974 (emphasis added). Significantly, a plaintiff cannot meet this  
burden by pleading facts showing "mere recklessness or a motive to commit fraud and  
opportunity to do so." *Id.*

///

1           The plaintiffs in *Silicon Graphics* made two primary allegations concerning the  
2 defendants' scienter: 1) internal company reports contradicted the individual defendants' positive  
3 public statements regarding the company's financial status and 2) while making these positive  
4 statements, the individual defendants sold large amounts of their own stock in the company. The  
5 Ninth Circuit held that these allegations, both individually and collectively, did not constitute  
6 strong evidence of deliberate recklessness or conscious misconduct. First, the plaintiffs did not  
7 plead specific information regarding the alleged internal reports, *i.e.*, who wrote them, their  
8 contents, which defendants read them and how the plaintiffs learned of them. Second, the *Silicon*  
9 *Graphics* Court found that even the corporate insiders' sales of their company stock did not  
10 suggest deliberate recklessness because, *inter alia*, only two of the insiders sold a significant  
11 percentage of their holdings.

#### 12           **B. Application to This Case**

13           The SAC alleges that the following facts constitute strong evidence of deliberate  
14 recklessness or conscious misconduct by defendants:

- 15           1)     Although defendants informed plaintiffs in 1997 that they could leave  
16 their money invested in the AirTouch Fund, after this lawsuit was filed,  
17 defendants stated in April 2000 that "[n]o SBC savings plan includes  
18 direct stock ownership in any other company that is not related to SBC."  
SAC ¶ 155(a). Plaintiffs contend that this inconsistency shows that  
defendants did not intend to allow Plan participants to retain their  
AirTouch holdings.
- 19           2)     Between September 1998 and January 1999, defendants had access to  
20 nonpublic information regarding a possible AirTouch-Vodafone merger  
and "knew" that the merger was "imminent." *Id.* at ¶ 155(b).
- 21           3)     Defendants were fiduciaries of the Plans but nevertheless a) did not  
22 disclose plaintiffs' withdrawal or rollover rights; b) presented the  
liquidation of plaintiffs' AirTouch shares as a "fait accompli;" c) did not  
23 disclose that an AirTouch-Vodafone merger would make plaintiffs'  
AirTouch shares more valuable than SBC shares; d) did not disclose that  
24 the AirTouch shares added diversity to plaintiffs' Plan accounts; e) mailed  
one Benefits Bulletin and two Briefs in October 1998, "only weeks,  
25 possibly even days" prior to the October 30, 1998 deadline and did not  
send these mailings via certified or overnight mail, which would have  
26 distinguished them from other routine Benefit Bulletins and Briefs. *Id.* at  
¶ 155(c).
- 27           4)     Defendants froze the Nonsalaried Plan's AirTouch fund after October 30,  
28 1998. *Id.* at ¶ 155(d).

- 1           5) Defendants had motive and opportunity to replace plaintiffs' AirTouch  
2 shares with SBC shares because defendants knew that the AirTouch shares  
3 had a higher value than the price at which they were trading and replacing  
the AirTouch shares with SBC shares would create an artificial demand  
for SBC stock. *Id.* at ¶ 155(e).

4 In addition, plaintiffs' opposition brief argues that the following factual allegations also evidence  
5 the requisite degree of scienter:

- 6           6) Defendants did not announce their decision to merge the Pacific Telesis  
and SBC plans until mid-1998. *Opp.* at 15.  
7  
8           7) There was no reason why the Pacific Telesis and SBC plans needed to  
merge. *Id.* at 16.  
9           8) Defendants' misstatements and omissions were material and the  
importance and size of the plans' merger is evidence of scienter. *Id.*  
10           9) Defendants knew plaintiffs wanted to retain their AirTouch shares. *Id.*  
11           10) Defendants' violation of their fiduciary duties under ERISA suggests  
12 deliberate recklessness. *Id.* at 17.

13 The Court concludes that these factual allegations, both individually and collectively, do not  
14 constitute "strong circumstantial evidence of deliberately reckless or conscious misconduct" as  
15 required by *Silicon Graphics*.

16           **1. SBC's April 2000 Statement**

17           In April 2000, SBC stated that "[n]o SBC savings plan includes direct stock ownership in  
18 any other company that is not related to SBC."<sup>16</sup> Plaintiffs contend that this statement is  
19 "fundamentally inconsistent" with the April 1997 Prospectus, which informed participants that  
20 "if you have money in the [AirTouch Fund], you may leave it there or transfer it to other funds,"  
21 SAC ¶ 155(a). According to plaintiffs, the April 2000 statement "unequivocally reveals that  
22 SBC did not want any employees to hold AirTouch stock," and thus suggests that defendants'  
23 failure to disclose participants' withdrawal and rollover rights amounted to conscious  
24 misconduct. *Opp.* at 15.

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27           <sup>16</sup> Neither party has provided the Court with a copy of the document that contains this  
28 statement.

1           The April 2000 statement does not, as plaintiffs contend, suggest that defendants  
2 possessed any fraudulent intent. First, plaintiffs' opposition mischaracterizes the statement.  
3 SBC did not, as plaintiffs assert, state "that it has always been SBC's policy that no SBC  
4 employees may hold direct ownership in any other company." Opp. at 14. The April 2000  
5 statement appears to be nothing more than a statement of the SBC plans' then-current status. It  
6 therefore is not inconsistent with the 1997 Prospectus and cannot be evidence of a concealed  
7 nefarious intent as of 1997. The statement sheds no meaningful light on why SBC may have  
8 chosen to liquidate the AirTouch Fund or whether SBC attempted to mislead participants into  
9 acquiescing in the replacement of their AirTouch shares with SBC shares. Indeed, the  
10 Prospectus explicitly informed participants that the Plans could be changed or terminated at any  
11 time and for any reason. DRJN, Ex. 1, p. 11-52. Defendants' decision to eliminate the AirTouch  
12 Fund and eliminate Plan options that included direct ownership in other companies does not  
13 suggest either conscious misconduct or deliberate recklessness.

14           **2. Defendants Had Access to Nonpublic Information and Knew of the Merger**

15           The Court concludes that plaintiffs have failed to adequately plead that defendants knew  
16 of a possible AirTouch-Vodafone merger. As such, plaintiffs cannot base their allegations on  
17 defendants' purported omission of the pending merger regardless whether the merger discussions  
18 could be considered material as discussed above.

19           This is not the usual case where corporate insiders of Company A are accused of failing  
20 to disclose material information with respect to the merger of Company A and Company B. *See,*  
21 *e.g., Heliotrope General, Inc. v. Ford Motor Co.*, 189 F.3d 971 (9th Cir. 1999) ("*Heliotrope*").  
22 Rather, this case presents the situation where the defendants are entities unrelated to either  
23 Company A or Company B but are accused of failing to disclose material information regarding  
24 the A-B merger. As such, whether defendants possessed material non-public information  
25 regarding the possible merger is a genuine issue.

26           Plaintiffs' allegations with respect to defendants' knowledge of the potential AirTouch-  
27 Vodafone merger do not satisfy the PSLRA's particularity requirement. The SAC alleges:

28 ///

1 At all times mentioned in this complaint, defendants were plan sponsors,  
2 administrators, and fiduciaries of plaintiff's [sic] 401(k) plan which held  
3 AirTouch stock. As a result of this relationship - as well as the relationship  
4 between [Pacific Telesis] and Pac Bell (on the one hand) and AirTouch (on the  
5 other hand) that existed after Pac Bell spun off AirTouch (from the time that  
6 AirTouch was spun off from Pac Bell through the time AirTouch was merged  
7 with Vodafone, Sam Ginn was the CEO of AirTouch and, prior to the spin-off,  
8 CEO of Pac Bell) - [sic] had access to material information about the merger  
9 discussions between AirTouch and Bell Atlantic Communications Corporation  
10 ("Bell Atlantic") and the merger discussions between AirTouch and Vodafone  
11 PLC ("Vodafone"). This information would have significantly affected the  
12 market price of AirTouch securities if it was generally available to the public, and,  
13 as defendants knew, was not intended to be available to the public and was not  
14 generally available to the public. As a result, from at least September 1998 until  
15 the public announcement of the AirTouch and Vodafone merger in January 1999,  
16 defendants knew that the AirTouch and Vodafone merger was imminent and that  
17 such merger would substantially increase the value of AirTouch stock.  
18 Additionally, from at least September 1998 until the public announcement of the  
19 AirTouch and Vodafone merger in January 1999, defendants knew that AirTouch  
20 was in merger discussions with Bell Atlantic and that AirTouch was also in  
21 merger discussions with Vodafone. The existence of these merger discussions  
22 was reported in the press at that time.

23 SAC ¶ 155(b). These allegations fail to provide the "great detail" that the PSLRA requires. *See*  
24 *Silicon Graphics*, 183 F.3d at 985 (plaintiff's contention that company's "internal reports"  
25 established fraudulent scheme held insufficient to satisfy particularity requirement because  
26 plaintiff did not allege adequate "corroborating details" such as her sources of information  
27 regarding the reports, who drafted them, their contents and which corporate officers received  
28 them).

Here, plaintiffs contend that defendants possessed non-public information about the  
possible merger because 1) defendants were fiduciaries of the Nonsalaried Plan and 2) the CEO  
of AirTouch was formerly the CEO of Pac Bell. Plaintiffs' first contention lacks merit. An  
ERISA plan fiduciary does not possess material nonpublic information about any stock held by  
the ERISA plan merely by virtue of that fiduciary status. Plaintiffs' second argument is equally  
unavailing. Simply because Sam Ginn, the CEO of AirTouch at the time of the 1999 AirTouch-  
Vodafone merger, was the CEO of Pac Bell before the 1994 AirTouch spin-off does not, without  
more, suggest that Ginn fed defendants nonpublic information after he became CEO of  
AirTouch. *See Heliotrope, supra* (complaint properly dismissed where plaintiff failed to identify  
particular information that defendants allegedly possessed concerning likelihood of merger and

1 specific manner in which they allegedly acquired such information). Plaintiffs fail to allege the  
2 existence of any documents, statements or other communications showing that defendants  
3 actually possessed such inside information. Given this lack of specificity, plaintiffs' conclusory  
4 allegations that defendants "knew" of an "imminent" AirTouch-Vodafone merger are inadequate  
5 and plaintiffs cannot rely on these allegations to satisfy their pleading obligation for the  
6 misrepresentation/omission element. Indeed, defendants were not even insiders of either  
7 AirTouch or Vodafone; they were competitors. As such, these factual allegations also are  
8 insufficient to establish any fraudulent intent.

9 **3. Defendants' Nondisclosures of Withdrawal and Rollover Rights**

10 The Court has concluded that defendants' failures to reiterate participants' withdrawal  
11 and rollover rights cannot be deemed immaterial as a matter of law. But that does not also  
12 establish scienter. Misrepresentation and scienter are two separate elements; that plaintiffs have  
13 adequately pled the former does not automatically satisfy their burden to adequately plead  
14 scienter.

15 It is undisputed that the Briefs and Bulletins provided participants with detailed  
16 instructions on how to avoid the replacement of their AirTouch shares with SBC shares by  
17 transferring their AirTouch account balances to another Plan fund. If defendants intended to  
18 fraudulently induce plaintiffs into accepting SBC shares, it would be counterproductive to inform  
19 plaintiffs how to avoid the AirTouch Fund liquidation. But defendants did just that. Their  
20 failures to disclose participants' withdrawal and rollover rights do not give rise to a strong  
21 inference of deliberate recklessness.

22 **4. Defendants froze the Nonsalaried Plan's AirTouch Fund after**  
23 **October 30, 1998**

24 Before the October 30, 1998 deadline, defendants informed participants on at least five  
25 occasions that the Fund would be frozen and provided participants with detailed information on  
26 how to transfer their assets out of the Fund. That defendants actually carried out their plan to  
27 liquidate the Fund does not suggest deliberate recklessness or conscious misconduct.

28 ///

1           **5. Motive and Opportunity to Replace AirTouch Shares with SBC**  
2           **Shares**

3           “[A]lthough facts showing . . . motive to commit fraud and opportunity to do so may  
4 provide some reasonable inference of intent, they are not longer sufficient to establish a *strong*  
5 inference of deliberate recklessness.” *Silicon Graphics*, 183 F.3d at 970 (emphasis in original).  
6 Thus, plaintiffs must allege facts over and above mere motive and opportunity to adequately  
7 plead scienter. However, even considering plaintiffs’ scienter allegations collectively, the Court  
8 concludes that plaintiffs have not provided a strong inference of deliberate recklessness.

9           **6. Defendants did not announce their decision to merge the Pacific Telesis and**  
10           **SBC plans until mid-1998**

11           Defendants assert in their moving papers that SBC decided to merge its plan with the  
12 Pacific Telesis plans in 1997. Mem. at 6 n. 4. Plaintiffs’ opposition questions why defendants  
13 waited until mid-1998 to announce this decision, Opp. at 15, even though the SAC does not  
14 assert this delay as a basis for establishing scienter. Plaintiffs argue that this delay creates a  
15 “strong inference” that “SBC decided to recapture the AirTouch stock upon the high possibility  
16 of an AirTouch merger.” *Id.* Assuming that defendants knew of a possible AirTouch merger,  
17 their decision to recapture participants’ AirTouch shares might hint of fraud if defendants  
18 obtained the shares and held them until the stock’s price rose following public announcement of  
19 the merger. However, plaintiffs allege that defendants sold the AirTouch shares between  
20 November 1, 1998 and January 1, 1999, *i.e.*, before public announcement of the merger. Thus,  
21 after the announcement of the merger of the SBC and Pacific Telesis plans, defendants did not  
22 take advantage of the increase in the price of AirTouch stock. Moreover, plaintiffs do not  
23 contend that part of defendants’ alleged scheme was to pocket any proceeds from the liquidation  
24 of the AirTouch portfolio. *See* SAC ¶ 79. The SAC fails to allege how defendants could have  
25 had a motive to keep secret their decision to merge the SBC and Pacific Telesis plans until  
26 defendants gained nonpublic information regarding the AirTouch merger. Plaintiffs’ allegations  
27 regarding the timing of the announcement do not create any inference of deliberate recklessness.

28       ///

1           **7.       There was no reason why the Pacific Telesis and SBC plans needed to merge**  
2           Plaintiffs contend that because SBC did not merge its plan with the Pacific Telesis plans  
3 immediately upon acquiring Pacific Telesis in 1997, “there appears to be no reason why the SBC  
4 and PTG plans needed to merge” in January 1999. Opp. at 16. But the SAC alleges no facts  
5 which would establish that the merger lacked any justification or that it was a bad business  
6 decision.

7           **8.       The importance and size of the plans’ merger**

8           Plaintiffs cite *Schlagel v. Learning Tree Int’l*, 1998 WL 1144581 (C.D. Cal. Dec. 23,  
9 1998) and *In re Tel-Save Sec. Litig.*, 1999 WL 999427 (E.D. Pa. Oct. 19, 1999) (“*Tel-Save*”) in  
10 support of their contention that the size and importance of the SBC and Pacific Telesis plans’  
11 merger is evidence of scienter. However, neither case stands for this proposition. The plaintiffs  
12 in *Schlagel* alleged that individual defendant officers and directors of the corporate defendant  
13 falsified the corporation’s financial statements and made false and misleading statements about  
14 the corporation’s financial health while selling their own shares in the corporation. The district  
15 court found that the plaintiffs had adequately alleged scienter based on the timing of the  
16 individual defendants’ stock sales, violations of GAAP (Generally Accepted Accounting  
17 Principles) and allegations that the individual defendants knew of the corporation’s financial  
18 troubles through internal corporate documents and attendance at board meetings.

19           *Tel-Save* involved allegations of a scheme hatched by a corporation’s officers and  
20 directors to artificially inflate the price of the corporation’s stock through concealment of the  
21 corporation’s actual marketing costs and other expenses. The corporation’s CEO moved to  
22 dismiss. The district court found that the plaintiffs had adequately alleged the CEO’s scienter in  
23 part because “knowledge concerning a company’s key businesses or transactions may be  
24 attributable to the company, its officers and directors” and that the CEO knew or should have  
25 known of the alleged misstatements. *Tel-Save*, 1999 WL 999427 at \*5. In sum, neither of these  
26 cases stands for the proposition that the size or importance of a merger suggests fraudulent intent.

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1           **9. Defendants knew plaintiffs wanted to retain their AirTouch shares**

2           Plaintiffs contend that defendants knew they wanted to retain their AirTouch shares  
3 because 1) in 1994, most Plan participants, including plaintiffs, elected to retain their AirTouch  
4 shares and 2) between 1994 and 1998, “relatively few participants voluntarily sold their  
5 AirTouch stock to invest in the [Pacific Telesis] Plans’ other options.” SAC ¶¶ 74-75.

6           These allegations do not provide the “great detail” required by the PSLRA. Moreover,  
7 neither *AUSA Life Ins. Co. v. Ernst & Young*, 206 F.3d 202 (2d Cir. 2000), nor *Ventimiglia v.*  
8 *Gruntal & Co.*, 1989 WL 251402 (S.D.N.Y. Nov. 1. 1989), the cases cited by plaintiffs in  
9 support of this contention, apply the Ninth Circuit’s stringent scienter pleading requirement.

10           **10. Defendants’ violation of their fiduciary duties under ERISA suggests**  
11           **deliberate recklessness**

12           Plaintiffs cite several cases in which the defendants’ violation of GAAP was found  
13 probative of fraudulent intent. *See, e.g., Provenz v. Miller*, 102 F.3d 1478 (9<sup>th</sup> Cir. 1996).  
14 Plaintiffs contend that because their allegation that defendants breached ERISA fiduciary duties  
15 must be presumed to be true, defendants’ “extreme departure from the standards of fiduciary  
16 care” supports a finding of deliberate recklessness.

17           None of the authorities cited by plaintiffs stands for the proposition that an alleged  
18 violation of ERISA fiduciary duties creates a strong inference of deliberate recklessness.  
19 Plaintiffs’ allegations, if proven, may well establish that defendants violated ERISA. But a  
20 breach of fiduciary duty does not, in and of itself, establish a violation of § 10(b) or Rule 10b-5.  
21 *See Santa Fe Indus. Inc. v. Green*, 430 U.S. 462, 477, 97 S.Ct. 1292, 1303, 51 L.Ed.2d 480  
22 (1977) (finding that Congress did not intend “to bring within the scope of § 10(b) instances of  
23 corporate mismanagement such as this, in which the essence of the complaint is that shareholders  
24 were treated unfairly by a fiduciary”). Here, plaintiffs’ allegations that defendants breached their  
25 fiduciary duties under ERISA do not provide a basis for finding that defendants acted with  
26 deliberate recklessness as required by *Silicon Graphics*.

27 ///

28 ///

1           **C. Summary of Conclusion**

2           For all the reasons set forth above, the Court finds that the SAC's factual allegations do  
3 not constitute strong circumstantial evidence of deliberately reckless or conscious misconduct on  
4 the part of defendants.

5           **IV. Reliance**

6           When a securities fraud plaintiff primarily pleads omissions, the plaintiff is entitled to a  
7 presumption of reliance. *Blinder v. Gillespie*, 184 F.3d 1059 (9<sup>th</sup> Cir. 1999), *cert. denied*,  
8 --U.S.--, 120 S.Ct. 1158, 145 L.Ed.2d 1070 (2000). Here, the SAC primarily pleads omissions,  
9 e.g., defendants' failure to inform plaintiffs of their withdrawal and rollover rights. Plaintiffs are  
10 therefore entitled to a presumption of reliance.

11           **V. Causation**

12           Defendants contend that plaintiffs have failed to adequately plead causation because  
13 plaintiffs allege that they were "'forced' to sell their AirTouch stock 'without [their] consent' . . ."  
14 Reply at 14. Thus, according to defendants, their allegedly coercive actions would have required  
15 plaintiffs to acquiesce in the sale of the AirTouch stock irrespective of any alleged  
16 misrepresentations or omissions.

17           This is not a fair reading of the SAC. Plaintiffs clearly allege that they would not have  
18 allowed defendants to sell their AirTouch shares and replace those shares with SBC stock had  
19 defendants not made the alleged misrepresentations and omissions. SAC ¶ 157. Plaintiffs have  
20 adequately pled causation.

21           **VI. Conclusion**

22           Based on the foregoing discussion, the Court dismisses plaintiffs' federal securities fraud  
23 claim for failure to adequately plead scienter. The Court considers it unlikely that plaintiffs will  
24 be able to amend to allege additional facts that will satisfy the scienter pleading requirement.  
25 However, given that this is the first dismissal of this claim, the Court will nevertheless allow  
26 plaintiffs an opportunity to amend. The dismissal is therefore without prejudice. However, as  
27 stated above, any amended complaint shall not renew plaintiffs' deficient allegations concerning  
28 the "fait accompli" and reduction of diversification.



1 Congress enacted the SLUSA to “prevent plaintiffs from seeking to evade the protections  
2 that Federal law provides against abusive litigation by filing suit in State court rather than  
3 Federal court.” *Derdiger v. Tallman*, 75 F. Supp.2d 322, 324 (D. Del. 1999) (citing H.R.Rep.  
4 No. 105-803 (1998)). The SLUSA provides, in relevant part:

5 No covered class action based upon the statutory or common law of any State or  
6 subdivision thereof may be maintained in any State or Federal court by any  
private party alleging--

7 (A) a misrepresentation or omission of a material fact in connection with  
the purchase or sale of a covered security; or

8 (B) that the defendant used or employed any manipulative or deceptive  
9 device or contrivance in connection with the purchase or sale of a covered  
security.

10 15 U.S.C. § 78bb(f)(1). This subsection preempts a claim if four conditions are met: 1) the  
11 underlying suit is a “covered class action;” 2) the claim is based on state law; 3) the claim  
12 concerns a “covered security;” and 4) the plaintiff alleges “untrue, manipulative, or deceptive  
13 statements or omissions in connection with the sale or purchase of the security.” *Hines v. ESC*  
14 *Strategic Funds, Inc.*, 1999 WL 1705503 at \*3 (M.D. Tenn. Sept, 17, 1999). “It appears that  
15 Congress’s intention then, with the exception of certain ‘preserved’ actions, was to completely  
16 preempt state securities class actions alleging fraud or manipulation relating to covered securities  
17 when it enacted the [SLUSA].” *Abada v. Charles Schwab & Co., Inc.*, 68 F.Supp.2d 1160, 1165  
18 (S.D. Cal. 1999).

19 Here, plaintiffs do not dispute that their § 25402 claim satisfies the first three conditions  
20 for preemption, *i.e.*, this lawsuit is a covered class action, § 25402 is a state law claim and the  
21 AirTouch stock is a covered security.<sup>18</sup> Thus, the only issue is whether plaintiffs’ § 25402 claim

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22  
23 <sup>18</sup> A “covered class action” includes “any single lawsuit in which . . . damages are sought on  
24 behalf of more than 50 persons or prospective class members, and questions of law or fact common  
25 to those persons or members of the prospective class, without reference to issues of individualized  
26 reliance on an alleged misstatement or omission, predominate over any questions affecting only  
individual persons or members . . .” 15 U.S.C. § 78bb(f)(5)(B). The SAC falls within this  
definition. See SAC ¶¶ 63-65.

27 A “covered security” is a security listed, or authorized for listing, on the New York Stock Exchange,  
28 the American Stock Exchange or the Nasdaq National Market. 15 U.S.C. § 78bb(f)(5)(E) (adopting  
definition of “covered security” from 15 U.S.C. § 77r(b)). Defendants contend, and plaintiffs do not

1 alleges either a “misrepresentation or omission of a material fact” or a “manipulative or  
2 deceptive device or contrivance” in connection with the purchase or sale of plaintiffs’ AirTouch  
3 stock.

4 Plaintiffs contend that their § 25402 claim does not fall within the SLUSA’s preemptive  
5 scope because it is a claim for “trading while possessing information not disclosed to the public”  
6 and neither a misrepresentation/omission or a manipulative device is an essential element of  
7 § 25402. Opp. at 21. The SAC’s allegations with respect to the § 25402 “insider trading” cause  
8 of action are substantially similar to their federal “insider trading” cause of action.<sup>19</sup> The § 25402  
9 cause of action relies extensively on the same alleged misrepresentations and omissions that form  
10 the basis for the federal securities fraud claim, *i.e.*, defendants’ failures to disclose the possibility  
11 of an AirTouch-Vodafone merger, plaintiffs’ withdrawal and rollover rights, and the reduction in  
12 diversity of plaintiffs’ account that would result from replacement of their AirTouch shares with  
13 SBC shares. See SAC ¶ 162. Finally, the SAC alleges that “[b]ut for the above-described  
14 device/scheme/artifice, misrepresentations and omissions, plaintiffs would not have sold their  
15 shares.” *Id.* at ¶ 164 (emphasis added).

16 These allegations reveal that plaintiffs’ § 25402 cause of action, like the § 10(b)/Rule  
17 10b-5 cause of action, arises in connection with alleged misrepresentations and omissions by  
18 defendants. That plaintiffs have chosen to place another label on these allegations does not save  
19 them from preemption. See, *e.g.*, *Hines*, 1999 WL 1705503 (SLUSA preempts claim for  
20 securities fraud under Tennessee law where plaintiff alleged that “defendants employed devices,  
21 schemes, and artifices to defraud, [and] made material misrepresentations and omitted to state  
22 material facts” in connection with the offer and sale of securities). Accordingly, the Court  
23 concludes that the SLUSA preempts plaintiffs’ sixth cause of action.

24  
25 \_\_\_\_\_  
26 dispute, that AirTouch stock was traded on the New York Stock Exchange during the time period  
at issue here. Mem. at 21.

27 <sup>19</sup> Plaintiffs’ § 25402 allegations regarding defendants’ knowledge of a possible AirTouch-  
28 Vodafone merger are a verbatim recitation of the their allegations concerning defendants’ scienter  
for the federal securities fraud claim. See SAC ¶¶ 155(a-e), 162(a-e).

1 **Part III**  
2 **Declaratory Relief and Accounting - Seventh and Eighth Causes of Action**

3 The parties agree that these causes of action are not independent grounds for liability but  
4 are "theories of recovery for violations of securities laws." Opp. at 23. The viability of these  
5 claims therefore depends on the existence of a securities law claim. The dismissal of plaintiffs'  
6 federal and state insider trading claims requires dismissal of these claims as well.<sup>20</sup>

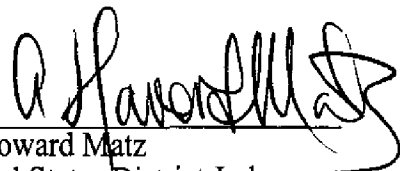
7 **CONCLUSION**

8 For the foregoing reasons, and good cause appearing therefor, the Court ORDERS as  
9 follows:

- 10 1. The Court GRANTS defendants' motion to dismiss plaintiffs' fifth (federal securities law),  
11 seventh (declaratory relief) and eighth (accounting) causes of action without prejudice.  
12 2. The Court GRANTS defendants' motion to dismiss plaintiffs' sixth cause of action (state  
13 securities law) with prejudice.  
14 3. Plaintiffs shall file any amended complaint by not later than October 10, 2000.

15  
16 IT IS SO ORDERED.

17  
18 DATE: September 19, 2000

  
A. Howard Matz  
United States District Judge

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28 <sup>20</sup> The Court need not consider defendants' other arguments for dismissal of these claims.