

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

NOTED
RICHARD and LINDA SHERMAN on behalf
of themselves and all others similarly situated,

Plaintiffs,

- against -

MERRILL LYNCH & CO., INC, MERILL
LYNCH INTERNET STRATEGIES FUND,
INC., MERRILL LYNCH FUNDS
DISTRIBUTOR, TERRY K. GLENN,
DONALD C. BURKE, CHARLES C.
REILLY, ROSCOE S. SUDDARTH,
RICHARD R. WEST, EDWARD D.
ZINBARG, ARTHUR ZEIKEL, PAUL
G. MEEKS, and HENRY BLODGET,

Defendants.

Civil Action No. **02CV**

Doc # 1
3176

CLASS ACTION COMPLAINT

Jury Trial Demanded

FILED
U.S. DISTRICT COURT
2002 APR 24 PM 4:43
S.D. OF N.Y.

CLASS ACTION

Plaintiffs, individually and on behalf of all other persons similarly situated, by their undersigned counsel, allege, upon personal knowledge as to their own acts, and upon information and belief as to all other matters, as follows:

NATURE OF THE ACTION

1. Plaintiffs bring this action as a class action on behalf of a class consisting of themselves and all other persons and entities (the "Class"), other than defendants and their affiliates, who purchased shares of the Merrill Lynch Internet Strategies Fund, Inc. (the "Internet Strategies Fund" or the "Company") from March 14, 2000 through October 15, 2001, inclusive (the "Class Period"). Plaintiffs seek to recover damages caused to the Class by Defendants' violations of Section 11, Section 12 and Section 15 of the Securities Act of 1933.

2. In March 2000, after watching Merrill Lynch in house financial consultants place at least hundreds of millions of dollars of their clients' money into third party Internet mutual funds, Merrill Lynch launched its own Internet mutual fund. The Merrill Lynch Internet Strategies Fund, Inc. (the "Internet Strategies Fund") was intended to capitalize on the public's insatiable thirst for Internet related securities and mutual funds.

3. Merrill Lynch used the "celebrity" status of Internet Analyst Henry Blodget ("Blodget") to market the Internet Strategies Fund and before the Internet Fund had purchased even a single stock, it had raised at least \$1.1 billion.

4. Although Blodget and the rest of Merrill Lynch's Internet analysts (the "Internet Group") touted Internet related stocks to outside investors, internally they maintained unfavorable opinions about the investment quality of the Internet companies that Merrill Lynch covered (the "Internet Universe"). There were wide conflicts of interests within Merrill Lynch that caused the Internet Group to base ratings on their desire to generate hundreds of millions of dollars in investment banking business rather than basing them on objective valuation methodologies. The Internet Strategies Fund was just another example of Merrill Lynch using the strong reputation of Blodget and the Internet group to generate investment banking and brokerage fees.

5. Merrill Lynch engaged in a scheme that was intended to use Blodget's strong reputation and bullish ratings on the Internet Universe to market the Internet Strategies Fund to unsuspecting investors in order to raise over a billion dollars in assets for the Internet Strategies Fund with the potential to generate hundreds of millions of dollars in fees for Merrill Lynch and its affiliate companies. The Defendants did not disclose that 1) Blodget and the Internet Group held unpublished negative personal views regarding the Internet Universe; 2)

considerable conflicts of interests existed within Merrill Lynch that compromised the objectivity of the Internet Group; and 3) that Blodgett's favorable ratings on Internet Stocks were influenced by his desire to generate investment banking fees.

JURISDICTION AND VENUE

6. This action arises under Section 11, 12(a)(2) and 15 of the Securities Act of 1933 (the "Securities Act"), 15 U.S.C. §§ 77(k), 77(l) and 77(o) and the rules and regulations promulgated thereunder.

7. The jurisdiction of this Court is based on Section 22 of the Securities Act (federal question jurisdiction).

8. Venue is proper in this District as many of the acts, transactions and wrongful conduct alleged herein, including the dissemination to the investing public of the materially misleading statements at issue, occurred in substantial part in this District.

9. In connection with the acts and conduct alleged in this Complaint, the defendants, directly or indirectly, used the mails and instrumentalities of interstate commerce.

THE PARTIES

10. Plaintiff Richard and Linda Sherman purchased shares of the Internet Strategies Fund during the Class Period and was damaged thereby.

11. Defendant Merrill Lynch is an international investment corporation organized and existing under the laws of the State of Delaware, with its principal place of business in the World Financial Center, North Tower, 250 Vesey Street, New York, New York 10281. Merrill Lynch provides investment-banking services to businesses, engages in retail and institutional sales to its customers, and publishes research reports and ratings on stocks.

12. Defendant Internet Strategies Fund, is a non-diversified open-end management investment company organized as a Maryland corporation, with its principal place of business at 800 Scudders Mill Road, Plainsboro, New Jersey 08536. The Fund's stated objective was to provide shareholders with long-term growth of capital through investment primarily in equity securities of issuers that the Investment Advisor, Fund Asset Management, L.P. ("FAM"), believed would use the Internet as a component of their business strategies. The Internet Strategies Fund invested primarily in common stocks of the Internet and Internet related companies that were developing new or innovative products, services or processes that FAM believed would produce earnings growth.

13. Defendant Merrill Lynch Funds Distributor ("MLFD" or "Underwriter Defendant"), a division of Princeton Funds Distributor, Inc. is a corporate affiliate of Merrill Lynch and acted as the principal Underwriter for the Internet Strategy Fund's offering.

14. Defendant Donald C. Burke ("Burke") was Vice President and Treasurer of the Fund. Defendant Burke signed the Registration Statement/Prospectus.

15. Defendant Terry K. Glenn ("Glenn") was President and Director of the Fund. Defendant Glenn signed the Registration Statement/Prospectus.

16. Defendant Charles C. Reilly ("Reilly") was a Director of the Fund. Defendant Reilly signed the Registration Statement/Prospectus.

17. Defendant Roscoe S. Suddarth ("Suddarth") was a Director of the Fund. Defendant Suddarth signed the Registration Statement/Prospectus.

18. Defendant Richard R. West ("West") was a Director of the Fund. Defendant West signed the Registration Statement/Prospectus.

19. Defendant Edward D. Zinbarg ("Zinbarg") was a Director of the Fund. Defendant Zinbarg signed the Registration Statement/Prospectus.

20. Defendant Arthur Zeikel ("Zeikel") was a Director of the Fund. Defendant Zeikel signed the Registration Statement/Prospectus.

21. The individuals named as Defendants in paragraphs 14-20 herein will be collectively referred to as the ("Director Defendants").

22. The Director Defendants were involved in drafting, producing, reviewing and/or disseminating the materially false and misleading statements and information alleged herein, including SEC filings, the Registration Statement/Prospectus, press releases, and other public documents, were aware of or negligently disregarded that materially false and misleading statements were being issued regarding the Fund, and approved or ratified these statements, in violation of the federal securities laws. Each Director Defendant was provided with copies of the documents alleged herein to be misleading prior to their issuance and/or had the ability and/or opportunity to prevent their issuance or cause them to be corrected accordingly, each Director Defendant is responsible for the accuracy of the public reports and releases detailed herein and is therefore primarily liable for the materially false representations contained herein.

23. It is appropriate to treat the Director Defendants as a group for pleading purposes and to presume that the materially false, misleading and incomplete information conveyed in the Company's Registration Statement/Prospectus as alleged herein are the collective actions of the Director Defendants identified above. Each of the Director Defendants, by virtue of their high-level positions with the Internet Strategies Fund, directly or indirectly had the ability to, and participated in, the management of the Internet Strategies Fund, and was directly or indirectly involved in the day-to-day operations of the Internet Fund at its highest

levels. By virtue of such involvement, these Director Defendants were privy to confidential proprietary information concerning the Company, its sales practices, and business objectives.

24. Defendant Paul G. Meeks ("Meeks") was the manager of the Fund and was primarily responsible for the day-to-day management of the Fund at all relevant times herein. Defendant Meeks was also very involved in marketing the Internet Strategies Fund.

25. Defendant Henry Blodget ("Blodget") was managing director and head of the Internet Group at all relevant times herein. Defendant Blodget was also very involved in marketing the Internet Strategies Fund.

CLASS ACTION ALLEGATIONS

26. Plaintiffs bring this action as a class action pursuant to Federal Rules of Civil Procedure 23(a) and (b)(3) on behalf of themselves and all other persons or entities similarly situated in the Class who purchased shares of the Fund during the Class Period and who sustained damages as a result of such transactions. Excluded from the Class are the defendants herein, members of the immediate families of and persons affiliated with each defendant, the legal representatives, heirs, and successors or assigns of any of the defendants.

27. There were over 100 millions shares of the Internet Fund stock publicly outstanding during the Class Period. Thus, the members of the Class are so numerous that joinder of all members is impracticable.

28. The representative plaintiff's claims are typical of the claims of the members of the Class. Plaintiffs and all Class members sustained damages as a result of Defendants' wrongful conduct complained of herein.

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

30. A class action is superior to other available methods for the fair and efficient adjudication of this controversy. Since the damages suffered by individual Class members may be relatively small, the expense and burden of individual litigation make it virtually impossible for the Class members individually to seek redress for the wrongful conduct alleged.

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

(a) whether defendants violated the federal securities laws, as well as the common law, by making materially misleading statements and omitting to state material facts in the Registration Statement/Prospectus, as well as other SEC filings and press releases during the Class Period;

(b) whether representations made to the investing public and the shareholders of the Fund during the Class Period omitted and/or misrepresented material facts about the risks and investment strategies of the Internet Strategies Fund;

(c) whether defendants failed to timely disclose material facts necessary in order not to mislead the investing public; and

(d) whether the members of the Class have sustained damages and, if so, what is the proper measure of such damages.

SUBSTANTIVE ALLEGATIONS

BACKGROUND

Internet Sector Mutual Funds Raised Hundreds Of Billions of Dollars From The Public

32. The financial markets in the late 1990's experienced a surge in investments in Internet companies that produced extraordinary gains for individual investors. Excitement over Internet stocks led to the development of Internet sector mutual funds that invested in companies that were expected to benefit from the growth of the Internet.

33. 1999 proved to be an exceptional year for the few mutual funds that focused on the Internet sector. For example, a January 24, 2000 article in *Pensions and Investments* titled "TRIPLE-DIGIT SCORES: Mutual funds find 1999 was a very good year indeed" stated in part:

The average U.S. equity mutual fund (excluding sector funds) returned 26.95% in 1999, making it the third best year ever. But Wiesenberger found that the average technology sector mutual fund returned 122% and the average Internet sector fund returned 131%. In fact, all five Internet mutual funds with track records longer than one year made it into the triple-digit club. (Emphasis Added).

34. A June 8, 2000 *Business Week* article titled "Will Net Fund 'Old Timers' Be Wisest?" stated in part:

Four funds were founded in 1996, and the largest, Munder's NetNet, posted a 173% return last year. Kinetics' Internet Fund...had a 216% return, while WWW Internet charted a gain of 167%....Amerindo's Technology Fund, the fourth old-timer, returned 248% last year...Monument Internet, founded in late 1998,...posted huge numbers its first full year, with a 273% return, while Guinness Flight's Wired Index fund, the oldest of the Net index funds, recorded a 68% gain in '99.

35. The astronomical returns by Internet sector mutual funds generated significant new cash inflows into these funds by investors. For example, the Munder Net Net Fund's assets grew from roughly \$320 million to over \$7.2 billion in 1999 alone.

THE DECEPTIVE SCHEME

Merrill Lynch Jumps on The Band Wagon and Markets Its own Internet Mutual Fund

36. Internet mutual funds experienced significant cash inflows during 1999, however, only several choices existed for investors and the Munder Net Net fund dominated the market. Merrill Lynch's Financial Consultants and retail stock brokers were forced to place their clients' assets into third-party Internet mutual funds because Merrill Lynch did not have its own Internet mutual fund. In fact, according to Terry Gardner, Munder Capital's chief financial officer, Merrill Lynch was the biggest distributor of the Munder Net Net fund. Merrill Lynch's failure to offer its own Internet mutual fund represented lost financial opportunities to Merrill Lynch.

37. As a result of the apparently insatiable demand for Internet mutual funds, Merrill Lynch decided to use the strong reputations of Merrill Lynch, its prized analyst Blodget and the Internet Group to market a Merrill Lynch Internet mutual fund. A proprietary Merrill Lynch Internet mutual fund would enable Merrill Lynch to keep clients' Internet mutual fund assets in house and would enable Merrill Lynch to earn management fees on the assets.

38. In March 2000 Merrill Lynch began marketing its Internet mutual fund – the Internet Strategies Fund.

Merrill Lynch's Internet Analyst Henry Blodget Was An Internet "Celebrity" And One Of The Most Respected "Cheerleaders" Of The Internet

39. Prior to and throughout the Class Period, Blodget was repeatedly recognized in the financial and regular media as a prominent analyst of Internet Companies.

Blodget was repeatedly the subject of newspaper and magazine articles and references, and he appeared repeatedly on business-oriented television programs. As demonstrated below, Blodget assumed virtual "celebrity status" which increased the influence and impact of his analyst reports.

40. Blodget's fame and extraordinary influence as an Internet analyst began on December 16, 1998, when he was an analyst at CIBC Oppenheimer. At that time, he set a "target" price for Amazon.com of \$400 per share. An April 2, 2000 article of the *Washington Post* titled "Analyst With a Knack for Shaking up Net Stocks; Henry Blodget Is Wall Street's Link Between Online Firms, Investor," stated in part:

... it ... took his bold move with Amazon to make him a household name in the world of Internet stockholders. The retailer was at its most controversial then, full of swaggering ambition and bleeding red ink. It was also a hot stock, one that had doubled and redoubled. Two months earlier Blodget had put a 12-month price target of \$150 on it. The stock quickly breezed by that to close on Dec. 15 at \$242.

So he set an "outlandish" new target-\$400. "I was trying to say, 'Stop asking me the price target. There's plenty of upside,'" he says. "But it was like I threw gasoline on a bonfire."

"The reason stocks move is not because they're cheap or expensive," Blodget says. "It's because there's an imbalance of supply and demand. Stocks don't move on valuation."

"Our job is not to be stock pickers, but to be correct on trends, and help investors pick stocks," he said. "There's a significant difference."

(Emphasis Added.)

41. Blodget's celebrity status included regular appearances on television programs concerning the financial markets - programs that had significant influence on the financial markets and the prices of stocks. As reported in the March 15, 1999 issue of *The Wall*

Street Journal in an article titled "Abreast of the Market: What Moves Markets: New Forces Are Now Powering Surging Stocks: Ordinary Joes Move Market Toward Dow 10,000 Mark With Aid From TV, Internet":

The pros keep an eye not just on their banks of quote machines, but also on television screens. "In my fixed-income trading room and my stock trading room, CNBC is on all during the day," says Henry Herrmann, chief investment officer at Overland Park, Kan., mutual-fund group Waddell & Reed. He put in televisions two years ago, when he was upgrading the bond trading room. "It is just another tool but it is a tool," he says. When Prudential's Mr. Acampora turned bearish in August and CNBC relayed his warning of a sharp market drop, the prediction proved self-fulfilling and helped push stocks down. The experience indicated that, at the right time, television appearances by any of a variety of market players can hit the market just as hard as a warning from the Fed's Mr. Greenspan. And television can turn once-unknown analysts, such as Merrill's Mr. Blodget, into instant celebrities. (Emphasis Added).

42. In its October 4, 1999 issue, *Time Magazine* named the "Digital 50- The Most Important People Shaping Technology Today" and Blodget was one of the "Digital 50."

The article stated in part:

Henry M. Blodget The Forecaster Merrill Lynch Senior Internet and e-commerce analyst AGE: 32 WEB: www.ml.com

It takes a certain cachet to make financial-market types swoon. Henry Blodget, arguably the most influential voice on Internet stocks in the world, is so hot right now that his late arrival to a recent bigwig luncheon prompted this announcement: "Elvis has entered the building." The 1989 Yale grad was a managing director and senior Internet analyst at CIBC Oppenheimer when he made the call that shot him into the spotlight and one of the most prestigious jobs on Wall Street. Amazon.com's share price was hovering around \$ 200; pundits were proclaiming that the party was over. But Blodget remained bullish on the online bookseller and said the stock would hit \$ 400 in 12 months--and then it hit the stratosphere. By March, he was at Merrill--and he's been getting the kind of attention shown in those old E.F. Hutton ads ever since. (Emphasis Added).

43. In its June 29, 1999 issue, the *Wall Street Journal* named Blodget as one of three all stars in its "All-Star Analysts 1999 Survey: Internet."

44. Blodget was sometimes referred to as "King Henry," appeared frequently on television business news reports, where he would set forth his bullish opinions and predictions regarding the stocks of various Internet companies and Merrill Lynch promoted Blodget's reputation and used it to enhance the reputation of the analysts in its technology group, in general. For example, in the Spring of 2001, Merrill Lynch placed a two-page advertisement in a weekly trade publication headlined "Fechtelligence." In the advertisement, Merrill Lynch touted the capability of Merrill Lynch's technology group, including the 100 analysts who cover 500 companies and the awards its analysts have won, including Merrill Lynch's "Internet Guru" Henry M. Blodget.

45. The extraordinary extent of Blodget's exposure was reported in the June 5, 2000 issue of *The Industry Standard, The News Magazine of the Internet Economy*, in an article titled "Holding Analysts Accountable. Investors following stock recommendations are often in the dark about Wall Street analysts' conflicts of interest. Regulators aren't happy." In that article it was reported that in the preceding year Blodget had been cited in the press on 1,072 occasions -- more than any of the other listed analysts, venture capitalists and Internet chief executive officers surveyed. Blodget was cited in the media 80% more than the two next highest people surveyed -- Meg Whitman, the CEO of Ebay, and Mary Meeker, Morgan Stanley Dean Witter's Internet analyst.

46. Another example of Blodget's exposure was reported in a March 12, 2001 *Washington Post* article titled "Who Blew the .com Bubble?; The Cautionary Tale of Henry Blodget." That article stated in part:

Henry Blodget, Wall Street's loudest cheerleaders for Internet stocks, made it to the front page of the New York Times last week. And thereby hangs a tale about the media and the bubble.

The Merrill Lynch analyst rode a tidal wave of publicity as the Net stocks he was touting soared toward the stratosphere.

From the day he burst into the headlines in December 1998, Blodget has been mentioned 95 times in the Wall Street Journal, 66 times in the New York Times, 53 times in The Washington Post (which ran a 3,800-word profile of him last year) and 27 times in Business Week. Just since the beginning of last year, he has been mentioned (or interviewed) on television 816 times, a Nexis database search finds.
(Emphasis Added)

47. It was generally recognized in the financial media that Blodget's recommendations substantially impacted the price of Internet stocks. For example, a August 19, 1999 article in the *New York Times* titled "Stocks Slump as Investors Take Profits" stated in part:

A surprisingly strong earnings report by Dell Computer and a recommendation of eight Internet stocks by Merrill Lynch's influential analyst, Henry Blodget, helped keep the Nasdaq average in positive territory most of the day before it, too, slipped and ended down 13.49 points, or five-tenths of 1 percent, to 2,657.73.

Mr. Blodget, the Merrill Lynch analyst, recommended eight Internet stocks he saw as benefiting from this year's holiday shopping season, perhaps tripling revenue from on-line sales and advertising. He predicted the shares, which "offer a sound way to play the fundamental strength and renewed investor enthusiasm" expected in coming months, would surge 50 percent to 100 percent by year-end.

All his picks rose. Amazon.com jumped 3 7/8, to 113 1/8; America Online 1 11/16, to 99 3/16, and Yahoo 6 3/16, to 145 1/16. His other picks were Etoys, Excite@Home, Lycos, Inktomi and Barnesandnoble.com.

48. Blodget resigned from Merrill Lynch on November 14, 2001 and news coverage of Blodget's resignation reflected that Merrill Lynch hired Blodget as an Internet analyst because his high profile, bullish reports on Internet stocks would help Merrill Lynch obtain investment banking and underwriting business in the Internet sector. For example, on the CNBC television program "Squawk Box" on November 15, 2001, David Faber said in part:

Merrill had always been looking for real strength in technology, banking especially, where they had a weakness to a certain extent. They felt that by hiring Blodget, such a cheerleader for the Internet sector, they would position themselves well with many companies. They did get some underwriting business out of it. Unfortunately, many of those issues did not do much of anything. (Emphasis Added).

49. Similarly, a November 16, 2001 article in the *Financial Post* titled "King Henry begins new chapter: Merrill's faded dot-com guru resigns to write book" stated in part:

Henry Blodget, the technology analyst who epitomized the irrationality of dot-com mania, has walked away from Wall Street, accepting a buy-out package worth about US\$2 million from Merrill Lynch & Co.

Mr. Blodget's decision marks the end of a short but spectacular career that saw him go from an anonymous analyst to one of the Internet's most influential market gurus. At the height of dot-com bonanza, Mr. Blodget -- once dubbed 'King Henry' in industry circles-- had the ability to send stocks soaring or sinking by simply speculating about their prospects. (Emphasis Added).

Merrill Lynch Capitalized On Blodget's Status When Marketing The Internet Fund

50. Blodget was synonymous with the unlimited potential upside of investing in the Internet and Merrill Lynch used Blodget's fame alongside Merrill Lynch's reputation to market the Internet Strategies Fund to unsuspecting investors.

51. The Merrill Lynch Internet Strategies Fund was an extraordinary success and raised approximately \$1.1 billion in its initial public offering of shares to investors. In fact, the Internet Strategies Fund was one of Merrill Lynch's biggest fund openings ever. The success

of the initial offering was directly attributable to Merrill Lynch and Blodget's strong reputations which Merrill Lynch used to feed its client's frenzy for Internet stocks.

52. On March 1, 2000, the Internet Strategies Fund kicked off its marketing push at the AMG Technology Summit - ".com and Beyond" - San Francisco. Presentations made by the fund's managers such as Meeks and several guest speakers including Blodget, were simulcast to the workstations of Merrill Lynch's more than 14,000 financial consultants around the country. A two-week "virtual roadshow" followed, in which interactive video and audio conferences, CD-roms and other communications avenues were used to deliver information about the new fund to Merrill Lynch financial consultants.

53. In an internal Merrill Lynch marketing piece "Mutual Interest" dated February 2000, Merrill Lynch Financial Consultants were informed about the Internet Strategies Fund. It stated that at the Merrill Lynch Financial Consultants would be able to gain insight into how the Internet Strategies Fund is prepared to capitalize on the growth of the technology sector by listening to key industry leaders and Merrill Lynch technology experts including Blodget and Meeks.

54. A Merrill Lynch press release issued on March 27, 2000 titled "Merrill Lynch Launches Internet Strategies Fund; Fund Raises \$1.1 Billion In Initial Public Offering" stated in part:

Merrill Lynch today said its Merrill Lynch Internet Strategies Fund raised \$1.1 billion in its two-week initial offering period, marking the second time this year a Merrill Lynch equity fund has topped the \$1 billion plateau during its subscription period.

The ML Internet Strategies Fund (MBNTX) will be managed by Paul Meeks, Robert Zidar and Dawn Simon. Mr. Meeks, who will serve as senior portfolio manager for the fund,

also serves as senior portfolio manager on the Merrill Lynch Global Technology Fund (MBGTX).

"Through the Merrill Lynch Internet Strategies Fund, clients will be able to invest in one of the most exciting sectors of the New Economy backed by the resources of Merrill Lynch," said Bob Doll, co-head and chief investment officer of Merrill Lynch Asset Management Group (AMG) Americas. "Our new Internet-specific fund is designed to complement the Merrill Lynch Global Technology Fund, which gives investors broader exposure to the technology sector."

...But the raging interest in this sector, coupled with the instant access to our financial consultants that technology afforded us, helped us raise \$1 billion just weeks after we brought in a similar amount for our two new aggressive growth funds."

The Merrill Lynch Internet Strategies Fund seeks long-term capital appreciation by investing primarily in stocks of companies that the fund's managers believe will use the Internet as a component of their business strategy. The fund will invest primarily in the common stocks of Internet companies that engage in the many aspects of products and services that facilitate the use of the Internet, including: online consumer and business commerce; data transport, distribution and transmission; network infrastructure; optimization and utilization technologies; and applications used in connection with the World Wide Web.

The fund is closed to new investors for an indeterminate period of time.

Merrill Lynch is one of the world's leading financial management and advisory companies with offices in 43 countries and total client assets exceeding \$1.7 trillion. Through the Merrill Lynch Asset Management Group, the firm is one of the world's largest managers of financial assets, with more than \$550 billion under management.

(Emphasis Added)

55. A June 8, 2000 *Business Week* article titled "Will Net Fund 'Old Timers'"

Be Wisest:" commenting on the success of the Internet Strategies Fund added that Merrill

Lynch's "success is largely due to [it's] marketing muscle, name recognition, and vast brokerage network."

56. A July 2000 article in *Red Herring* titled "Late to the game; Fund companies are trying to cash in on the Internet frenzy. It's probably too late" described the growth of Internet mutual funds and stated in part:

Of course, Wall Street is in the business of giving people what they want, and what many investors want these days is the opportunity to double their money in months rather than years.

From a pure marketing standpoint, Merrill Lynch's Internet Strategies has been the most successful new fund. It collected over \$1 billion from Merrill Lynch clients and is now the third-largest Internet fund, behind Munder NetNet and Kinetics Internet. Terry Gardner, Munder Capital's chief financial officer, is not surprised by Merrill Lynch's success... [and said that] Internet Strategies is "probably getting some of the money that might have come our way[.]"

The Internet Strategies Fund Went Bust

57. Although the Merrill Lynch Internet Strategies Fund was very successful in raising assets in its initial offering, that success did not materialize into strong investment results for investors.

58. Merely several weeks after the launch of the Internet Strategies Fund, on April 14, 2000 the Nasdaq Composite Index endured its biggest point drop ever. Investors in the Internet Strategies Fund's initial public offering would never realize a gain from their initial investment by selling shares of the Internet Strategies Fund.

59. Within one year of its offering, by the end of the first quarter of 2001, the Internet Strategies Fund lost 74% of its value and was down roughly 43.1% in the first quarter 2001 alone. By February 28, 2001, assets had dropped more than 75% to \$280.8 million.

Commenting on the Merrill Lynch Internet Strategies Fund, Chris Traulsen, a senior analyst at Morningstar Inc., a Chicago-based mutual fund information provider, stated "Gosh, you kind of wonder about these companies coming out with these funds...It seems that they had their eye on whether it would be popular and be able to pull in fees for them, rather than whether they would be good for investors."

60. The Internet Strategies Fund, only 13 months after its initial public offering, filed a proxy requesting that shareholders approve a merger of the fund into Merrill's Global Technology Fund. Shareholders approved the merger and on or about October 15, 2001 the Internet Strategies fund was merged into the Global Technology Fund.

Merrill Lynch Analysts Maintained Artificially Strong Ratings on Internet Stocks in order to Generate Hundreds of Millions of Dollars in Investment Banking Fees

The Merrill Lynch Rating System: Theory Versus Reality

61. Until June 15, 2001, Merrill Lynch had a five-category stock rating system:

1	Buy	(20% or more price growth expected)
2	Accumulate	(10% or 20% price growth expected)
3	Neutral	(10% price growth to 10% price drop expected of price)
4	Reduce	(10% to 20% price drop expected)
5	Sell	(20% or more price drop expected)

62. Each covered stock was rated for both the intermediate-term (through the next twelve months) and long-term (beyond twelve months), and assigned an investment risk ranging from "A" (least risky) through "D" (most risky).¹ The ratings assigned to covered companies were represented to the investing public to be independent, objective and on the merits as stated in the Merrill Lynch Global Securities Research and Economics Group Policy and Procedures Manual:

¹ All of the stocks discussed herein were assigned a "D" rating by the Merrill Lynch internet group.

Objectivity of Opinions. Opinions expressed by Analysts must be objective. Any indication that a Research opinion is less than totally objective, or that it may have been influenced by a business relationship of the Firm, could seriously damage the Firm's reputation and lead to potential legal liability.

63. This simply was not the case with respect to ratings published by the internet group.

64. Although Merrill Lynch's published rating system provided for 4s (reduce) and 5s (sell), the Internet Group never used 4s or 5s. A listing of covered internet stocks titled *Internet/eCommerce Q2 2000 coverage*, lists 24 stocks, none of which was rated less favorably than a 2. Merrill Lynch never published a single reduce or sell rating on any stock covered by the internet group.

65. Thus, although represented to be a five-point system, internally it became a three-point system. On April 23, 2001, in lieu of assigning reduce or sell recommendations to stocks they no longer favored, the internet group instead merely quietly stopped covering the stock without any announcement of meaningful explanation to the retail public.

66. Thus, as previously covered stocks such as Pets.com, Mypoints.com, Quokka Sports, Webvan, iVillage, Buy.com, 24/7 Media, E-Toys, Internet Capital Group, and InfoSpace plummeted, sometimes all the way to zero, retail customers and the investing public were never advised to sell. The reason for this failure is at least in part the substantial unrevealed conflict of interest discussed below.

The Ratings Assigned To Stocks Did Not Comport With Their Definitions

67. The de facto three-point system not surprisingly wreaked havoc amongst the various constituencies called upon to interpret and utilize the ratings, especially the retail

public. While sophisticated institutional investors and equities traders may have recognized the de facto three-point scale, the public and retail investors did not have such insight.

68. Thus, the public was unaware that while the internet group was contemplating a 3 (neutral) rating on selected stocks, internally the Internet Group said amongst themselves that the stock was "going a lot lower," that the company was "crap," or a "dog". Nor was the public told that while the internet group was contemplating a 2 (accumulate) rating on a variety of stocks internally - - and to selected institutional investors - - the analysts were saying that there was "[n]o reason to own" the stock, or that the group expected the stock to be "flat" over the next six months without "any real catalysts [for change]". The public also was not told that the group internally disparaged other stocks rated 2 as a "piece of shit," and "such a piece of crap".

69. The electronic communications of the Internet group feature many such exchanges. For example, on August 30, 1999, the group initiated coverage on the stock of Internet Capital Group (ICGE), an investment banking client, with a 2-1 rating. The stock closed on October 4, 2000 at \$15.69, down from a high of \$212 on December 22, 1999. But even with these prognostications, the public rating remained 2-1 and, when eventually downgraded on November 9, 2000, was changed only to a 2-2. The result was a continued recommendation to the investing public to purchase a stock about which the head of the Internet group was obviously exceptionally and accurately pessimistic, and for which he anticipated a drop of an additional 60 percent. Despite this pessimistic outlook, ICGE was on Merrill Lynch's list of the top ten technology stocks ("Top Ten Tech" list), as late as September 12, 2000.

70. Merrill Lynch maintained a list of its highest recommended stocks, selected from all of the stocks Merrill Lynch covered - - not just internet stocks. To be selected

for this list (the "Favored 15"), to which retail brokers and the public had access, a stock had to have a 1-1 rating. InfoSpace was on the "Favored 15" List from at least August 2000 until December 5, 2000, even though Blodget had acknowledged as early as July 2000 that the stock was a "powder keg" and that "many institutions" had raised "bad smell comments" about it, and in October had referred to it as a "piece of junk." Oddly enough, Blodget was unaware that the stock he had been covering for months carried the imprimatur of the "Favored 15." InfoSpace, was not removed from the "Favored 15" until December 5, 2000 and was not downgraded until December 11, 2000.

71. Below is a chart of examples demonstrating discrepancies between the numerical investment ratings assigned by the internet group and the group's contemporaneous internal analysis or opinions.

Company	Date	Contemporaneous Analyst Comments	Published Rating
Aether System (AETH)	03/15/01	On March 15, 2001 in a e-mail correspondence regarding AETH the following was stated: "might have announcement next week ... which could pop stock. . .but fundamentals horrible"	3-1
Excite @home (ATHM)	12/27/99 12/29/99	On December 27, 1999, Virginia Syer wrote an e-mail to Henry Blodget stating, "we are neutral on the stock" On December 29, 1999 Henry Blodget responded to an e-mail from Steve Feldsher and commented, Six month outlook is "flat", without any "real catalysts" for improvement seen	2-1
Excite @home (ATHM)	06/03/00	On June 3, 2000, in a e-mail correspondence between Virginia Syer and Henry Blodget, Blodget replied that ATHM is "such a piece of crap"	2-1
GoTo.Com	1/11/01	On January 11, 2001, John Faig sent	3-1

Company	Date	Contemporaneous Analyst Comments	Published Rating
(GOTO)		an e-mail to Henry Blodget with the subject: "What's so interesting about GOTO except banking fees???" Blodget replied "Nothing"	
InfoSpace (INSP)	7/13/00	On July 13, 2000 Henry Blodget replied to Sofia Ghachem and stated "this stock is a powder keg, given how aggressive we were on it earlier this year and given the "bad smell" comments that so many institutions are bringing up"	1-1
InfoSpace (INSP)	10/20/00	On October 20, 2000, Henry Blodget replied to an e-mail from Jeff Sexton remarking that INSP was a "piece of junk"	1-1
Internet Capital Group Inc. (ICGE)	10/06/00	On October 6, 2000 Henry Blodget wrote an e-mail in regard to ICGE stating, "No hopeful news to relate.... We see nothing that will turn this around near-term. The company needs to restructure its operations and raise additional cash, and until it does that, there is nothing positive to say."	2-1
Lifeminders (LFMN)	12/04/00	On December 4, 2000, Henry Blodget replied to Eve Glatt and called LFMN a "POS" (piece of shit)	2-1
24/7 Media (TFSM)	10/10/00	On October 10, 2000 Henry Blodget responded to an e-mail from Eve Glatt and commented on TFSM, by stating that it was a "piece of shit"	2-2

The Internet Research Group Was Not Independent Of Investment Banking

72. The evidence establishes that the Internet research analysts were far from independent of their investment banking colleagues, and that their tortured relationship helped drive both the selection of covered stocks and the ratings ultimately assigned.

73. Tension between the various departments in a single firm is nothing new. At a securities firm, this tension is usually addressed by the establishment of a "Chinese Wall" – an internal relationship barrier by which investment bankers are prevented from sharing with other firm employees material, non-public information received by the bankers from their publicly traded company clients. Thus, a banker generally should be barred from discussing such inside information with a research analyst who is disseminating to the public a research report on the same company. Another form of "Chinese Wall" attempts to prevent investment bankers from influencing analysts' ratings for the stock of existing or potential investment banking clients.

74. The compensation structure of a securities firm can exacerbate the potential for an analyst to be conflicted. Where analysts' compensation is affected, directly or indirectly, by the analysts' contribution to investment banking, analysts' objectivity and independence can be seriously eroded.

75. Research analysts at Merrill Lynch were actively involved in evaluating and effectuating investment banking transactions. Moreover, analysts' compensation was tied to the success of their efforts in this regard.

76. The analysts in the Internet group at Merrill Lynch knew very well that investment banking business translated into compensation for them personally and the firm generally, and that their research played a role in attracting and keeping that investment banking business. On April 26, 2000, an analyst and investment banker discussed through an e-mail exchange how to attract investment banking business of a company from a competitor. The banker proposed a formula that had apparently worked in the past with another banking client: "we should aggressively link coverage with banking – that is what we did with Go2Net (Henry

[Blodget] was involved)...[I]f you are very bullish (b/c they will love you), they are not happy with GS [Goldman Sachs] and are going to be active, we can probably get by on a 'handshake.'" This e-mail lays bare the understanding that Merrill Lynch intended the prospect of affirmative research to attract investment banking clients.

77. One way Blodget prioritized research coverage for stocks was whether the company had an investment banking relationship with Merrill Lynch. Consistent with this agenda, Blodget, within weeks of joining Merrill Lynch as head of the internet research group, distributed a memorandum entitled, "Managing the Banking Calendar for Internet Research," which he sent to the Co-Heads of U.S. Equity Research, and senior investment bankers. The memorandum unapologetically described Blodget's expectation that at least 50 percent of his and his team's time would be allocated to investment banking matters. In addition to discussing "banking transactions [] in the pipeline" and "promising deals," the memorandum described Blodget's work schedule for one week as being divided "85% banking, 15% research." Blodget's own time allocation reveals that Merrill Lynch viewed research as a sales tool for investment banking.

78. From December 1999 to November 2000, the internet group was involved in investment banking deals that -- on its own estimate -- produced approximately \$115 million of revenue to Merrill Lynch. The list of the group's activities for that year included participating in the bankers' sales pitch to potential clients, marketing transactions to institutional investors once the bankers had obtained the assignment, and then initiating and doing "follow-on" research coverage.

79. The evidence examined to date confirms that the analysts' decisions about whether a stock should get coverage and what type of coverage it should receive were made

neither objectively nor independent of the investment banking group. In one instance on October 4, 2000, an analyst stated that "part of the reason we didn't highlight [a risk] is because we wanted to protect ICG's banking business." In another communication on June 16, 2000, an analyst worried about the impact of a particular rating on the relationship with investment banking or its venture capitalists. So pervasive was the tie between investment banking and research coverage, that when a competitor unexpectedly initiated coverage on the stock of a potential investment banking client, it prompted one Merrill Lynch analyst to respond, "they are angling for the M&A business too!"

80. Analysts conveyed to one another that they would "win brownie points" from investment banking if the investment bankers could assure a company that the analysts would cover its stock. Implicit in this was that "coverage" would always be favorable. Bankers, in turn, attempted to use the analysts to move the price of a stock to a level where research could be initiated, and so fulfill the promise of research coverage in exchange for banking work. One banker, who was frustrated by a stock's failure to reach the requisite price level of \$10 before coverage could commence, implored the Internet group to let the company speak at the group's upcoming conference that would be attended by many institutional investors - - to promote Merrill Lynch's "active banking agenda" with the company and alleviate the company's unhappiness with the "research tie up" at Merrill Lynch.

81. Investment banking also was involved in criticizing and editing the Internet Group's reports for client companies, opining on whether a particular rating would be acceptable and, in at least one instance, apparently opposing a proposed rating because "[there is no] interest in seeing initiation [of research coverage] at 3-2 [rating]". On November 16, 2000

analysts openly discussed the conflict in e-mails, stating "the whole idea that we are independent from banking is a big lie -- without banking this would be [rate] a 3-2."

82. On October 9, 2000, research management itself acknowledged that "we are off base on how we rate stocks and how much we bend backwards to accommodate banking etc."

83. Merrill Lynch has never publicly acknowledged that improper influence of investment banking on research. To the contrary, the public was specifically told on April 6, 2001 that the internet group analysts were independent, objective and unbiased. Knowing that such conflicts existed, and that members of the research group routinely acted as quasi-investment bankers, Merrill Lynch pretended there was a clear division, thereby enhancing the analysts' credibility.

The Analysts' Compensation Was Linked To Their Investment Banking Work

84. The research analysts' objectivity and independence was further eroded by the fact that their compensation depended in part on their efforts made on behalf of investment banking. In the Fall of 2000, Merrill Lynch's Deepak Raj, then co-head of global equity research, in an email to all equity analysts requested:

We are once again surveying your contributions to investment banking during the year.... Please provide complete details on your involvement in the transaction, paying particular attention the degree that you research coverage played a role in origination, execution and follow-up. Please note, as well, your involvement in advisory work on mergers or acquisition, especially where your coverage played a role in securing the assignment and your follow-up marketing to clients. Please indicate where your research coverage was pivotal in securing participation in high yield offering.

85. On November 2, 2000, Blodget and the internet research group responded to the above request. In a detailed memorandum with schedules, entitled "IBK Contributions:

Internet Team." Blodget stated that: (a) his group had been involved in over 52 completed or potential investment banking transactions; (b) the completed transactions had earned \$115 million for the firm; and (c) more transactions would have been completed had not the "market window for most internet companies closed in June." He also identified the services his analysts typically performed for investment banking, including pitching the client, marketing the offering and, notably, initiation and follow-on research coverage. Shortly after documenting these contributions, Blodget's salary contract -- which contained a guaranteed minimum -- was cancelled and replaced with a substantially larger compensation package. Overall, Blodget's agreed-annual compensation, including "guaranteed" minimum cash bonus, increased from \$3 million for 1999 to \$12 million for 2001.

The Analysts Were Not Independent From The Companies They Covered

86. The Internet Group at times appeared more concerned with acting as consultants to the companies they covered than as objective analysts. For example, as the stock of InfoSpace plummeted, losing almost 90 percent of its value in a year, the internet group counseled a senior officer of the company on how to handle himself and whether certain decisions were good business moves. When the company's officer confided a plan to invest in a particular venture, the analyst gave the investment banker advice:

We need to talk about this. While I understand your genuine enthusiasm for the company and trust your "killer deal instinct", I am concerned that the market will not react favorably to any news that [InfoSpace] fund US Search. My BEST advice to you is to let Yahoo and Lycos win this one -- there will be plenty of deals for you to do and [InfoSpace] cannot afford this kind of scrutiny right now -- the stock is under a lot of pressure.

87. Thus, as Merrill Lynch was supposedly providing the public with its objective opinion about a company's stock, it did not reveal that it was simultaneously advising that company how to keep the stock stable.

88. Merrill Lynch did not disclose to the public that the Internet Group shared -- and at times appeared even to negotiate -- proposed ratings with the bankers and companies at issue, in clear violation of Merrill Lynch's policy that analysts "may not disclose proposed investment conclusions" to company management.

Infospace – An Example of the Internet Group's Treatment of a Stock

89. Merrill Lynch initiated coverage of InfoSpace in December 1999 with a rating of 2-1 (accumulate-buy) and a price objective of \$160. The stock then traded at \$152.20. Shortly thereafter, Merrill Lynch upgraded the rating to 1-1. As of March 2, 2000, the price had reached \$261, but thereafter the stock steadily dropped. Yet Merrill Lynch's internet group maintained a 1-1 rating on the stock to December 10, 2000, when the price was \$13.69.² No sell rating was ever issued.

90. Throughout 2000, Merrill Lynch strongly supported InfoSpace. By March 21, 2000, it had upgraded its rating to a 1-1 (buy-buy), even though the stock was down considerably from its high, and concerns about the company's accounting practices had surfaced. The price objective nevertheless was then at \$200.

91. Around this time, Merrill Lynch was courting investment banking business from Go2Net, a technology company. On an April 5, 2000 conference call, Blodget and Mazzucco gave Go2Net a "presentation" about Merrill Lynch's investment banking and research abilities. In written materials, Blodget was promoted with a photograph and InfoSpace was listed as one of Merrill Lynch's covered stocks.

92. While the Internet Group continued to promote InfoSpace stock with buy/buy ratings, Merrill Lynch brokers began to raise numerous and serious questions about Merrill Lynch's support of the stock in e-mails to Blodget and Sofia Ghacehm between April 27,

² From December 1999 to December 2000, the stock split twice, each time at two for one.

2000 and June 15, 2000: "What is the deal with InfoSpace... [I] felt reluctant to push it these days," "should we be concerned about this... InfoSpace reported a loss of 38 cents a share, compared to a loss of 3 cents per share a year ago...." and "the stock continues to under perform and... few mutual fund managers are buying this stock... maybe we should re-evaluate our stance, I am really concerned for our clients." Ghachem also was questioned about InfoSpace's management selling their shares of the stock.

93. By June 1, 2000, the stock price had fallen to \$43, but Merrill Lynch continued its buy/buy ratings. On June 15, 2000, Blodget e-mailed Ghachem, confessing "enormous skepticism" about the stock. On June 20, 2000 Ghachem e-mailed Blodget to inform him that investment banking was meeting with InfoSpace on June 27th and the bankers had promised InfoSpace that Blodget would appear.

94. Merrill Lynch's buy ratings continued into early July 2000. On July 10, 2000, Go2Net went on Merrill Lynch's Grey Scan list, because Go2Net had asked Merrill Lynch to undertake a sale of Go2Net to InfoSpace. The next day, Merrill Lynch issued a "company update" – commonly referred to as a "booster shot" – on InfoSpace reiterating its buy rating. Unlike several other company updates on InfoSpace, no discernable reason was given for the update. In mid-July, Blodget complained to Ghachem, "I'm getting killed on this thing," yet his buy ratings for InfoSpace continued, even as the stock dropped further in price.

95. On October 26, 2000, Merrill Lynch completed the sale of Go2Net to InfoSpace. On December 11, 2000, Merrill Lynch finally reduced its rating to accumulate; the price had hit \$13. On December 20, 2000, Merrill Lynch issued a research bulletin indicating that InfoSpace's Vice-President had filed a lawsuit against InfoSpace's CEO, alleging multiple securities violations and racketeering.

96. From July 2000 through April 2001, e-mails reflect tremendous doubts by the Merrill Lynch analysts as to the future of InfoSpace and the ethics of its CEO. While Merrill Lynch's rating sat at 1-1 with a price objective of \$100, its analysts graphically observed that the stock "is a piece of junk" and "toast" if the CEO leaves. When a Merrill Lynch broker wrote to Blodget commenting on InfoSpace's poorly written 1999 annual report. Blodget responded, to Ghachem that he "would love to reset the price target to \$30 or something." Even after Merrill Lynch finally downgraded the stock to 2-1 in December of 2000, the stock still enjoyed an "accumulate" rating, despite the internet group's frank internal comments about "what a sleazebag" the CEO was and how Blodget was "officially not comfortable" with the CEO being associated with the company.

97. The evidence suggests that business considerations influenced the internet group in maintaining its buy rating for InfoSpace as long as it did. The group regarded InfoSpace important to Merrill Lynch's banking business, as evidenced by a May 17, 2000 e-mail to a member of the Merrill Lynch retail staff:

This company [InfoSpace] is very important to us from a banking perspective, in addition to our institutional franchise....

(adding that "non-deal roadshows" for companies such as InfoSpace "have a tremendous effect on our banking efforts).

98. Contrary to the image of objectivity that Merrill Lynch has sought to cultivate for its research arm, the evidence shows that analysts knowingly compromised their honestly held beliefs regarding the merits of particular stocks and skewed the ratings they issued in order to promote the interests of Merrill Lynch's investment banking business, and that the analysts' involvement in that business netted them substantial monetary rewards. The investing

public, of course, knew nothing of the inherent conflict of interest underlying the Merrill Lynch rating system, and was deprived of the analysts' honest opinions.

**THE FALSE AND MISLEADING STATEMENTS
CONTAINED IN THE REGISTRATION STATEMENT/PROSPECTUS**

99. On or about March 14, 2000, the Director Defendants and the Underwriter Defendant caused Internet Strategies Fund to file the materially false and misleading Registration Statement/Prospectus with the SEC in connection with the Internet Strategies Fund's IPO.

100. The Registration Statement/Prospectus contained numerous materially false and misleading statements and omitted to disclose numerous material facts that were required to be disclosed in order to render the statements made therein not materially misleading at the time it was declared effective. In particular, the sections of this document entitled: (i) "Key Facts"; (ii) "Details About the Fund"; and (iii) "Statement of Additional Information: Investment Objectives and Policies"; each omitted and/or misrepresented material facts concerning the Internet Fund.

The Material Omissions and/or Misrepresentations In The "Key Facts" Section Of The Prospectus

101. Under the "Merrill Lynch Internet Strategies Fund At A Glance" subheading, p. 3, the Registration Statement/Prospectus stated in relevant part:

What are the Fund's main investment strategies?

The Fund will invest primarily in common stocks of Internet and Internet related companies that are developing new or innovative products, services or processes that the Investment Advisor believes are likely to produce earnings growth.

102. The statements set forth in the foregoing paragraph were materially false and misleading at the times they were made based on the fact that it omitted to state that:

a. the Investment Advisor would also be willing to invest in companies that Blodgett and the Internet Group believed were not likely to produce earnings growth;

b. the Internet Strategies Fund was being marketed at a time when the Internet Group at Merrill Lynch published strong investment ratings on all Internet companies followed by Merrill Lynch even though internally, Merrill Lynch held negative views of those same stocks;

c. the Merrill Lynch Investment Group published strong ratings on Internet stocks in order to secure investment banking business;

d. substantial conflicts of interests existed within Merrill Lynch that broke through all "Chinese Walls" that were established to ensure the objectivity of Merrill Lynch's analysts and the Internet Group.

103. Under the "Merrill Lynch Internet Strategies Fund At A Glance" subheading, p. 3, the Registration Statement/Prospectus stated in relevant part:

What are the main risks of investing in the Fund?

As with any mutual fund, the value of the Fund's investments – and therefore the value of Fund shares – may fluctuate. These changes may occur because a particular stock market in which the Fund invests is rising or falling. At other times, there are specific factors that may affect the value of a particular investment. If the value of the Fund's investments goes down, you may lose money. We cannot guarantee that the Fund will achieve its investment objective.

Although Internet and Internet and related companies comprise a relatively new industry, equity securities issued by these companies historically have been extremely volatile. Volatility may increase the risk that the securities may lose value. Because the Fund invests primarily in securities issued by Internet and Internet related companies, there is a risk that the Fund will perform poorly during a downturn in either market sector. An

investment in the Fund is subject to the risk associated with equity securities issued by Internet and Internet related companies. These risks include rapidly changing technology, the continuous introduction into the marketplace of increasingly diverse and innovative applications of that technology, the relatively high risk of obsolescence of both hardware and software and extensive existing and proposed government regulation. In addition, an Internet or Internet related company in which the Fund invests may perform poorly due to factors affecting the particular company that may be unrelated to the Internet industry as a whole. These factors make the Fund more vulnerable to price changes of stocks of Internet and Internet related companies, which are extremely volatile, than a more broadly diversified mutual fund.

The Fund may invest in smaller companies that the Investment Adviser believes have potential for capital appreciation. The securities of such companies share the risks common to small capitalization emerging growth securities, including limited product lines or markets. Smaller companies may be less financially secure than larger, more established companies, may depend on a smaller number of key personnel and may trade in lower volumes than larger, more established companies.

Who should invest?

The Fund may be an appropriate investment for you if you:

- Are looking to invest in a portfolio comprised primarily of equity securities of Internet and Internet related companies and are willing to accept the risks associated with investment in those industries

104. The statements set forth in the foregoing paragraphs were materially false and misleading at the times they were made because:

- a. the section fails to state that Merrill Lynch's analysts including Blodget and the Internet Group were aware of specific factors that they believed would affect many of the companies in the Merrill Lynch Internet Universe;
- b. it omits to state that the Internet Strategy Fund plans to invest in an industry filled with companies that Merrill Lynch analysts including Blodget and the Internet

Group privately believed were poor investments at the time of the Internet Strategies Fund's offering;

c. the statement is too general and omits to state that Merrill Lynch analysts, including Blodget and the Internet Group privately believed that many of the stocks in the Internet Universe were poor investments and that specific factors existed at the time of the offering that would cause individual stocks that the Internet Strategy Fund would invest in to decline;

d. it omits to state that the Internet Strategies Fund would be open to investing in companies that Blodget and the Internet Group did not personally believe would have potential for capital appreciation;

e. Merrill Lynch analysts including Blodget and the Investment Group held personal views that there were considerable risks to the Internet Universe;

f. it omitted to state that the Internet Strategies Fund was being marketed at a time when the Internet Group published strong investment ratings on all Internet companies followed by Merrill Lynch even though those analysts, including Blodget, held negative personal views of those same stocks;

g. it omitted to state that Blodget and the Internet Group published strong ratings on Internet stocks in order to secure investment banking business;

h. it omitted to state that substantial conflicts of interests existed within Merrill Lynch that broke through the "Chinese Walls" that were established to ensure the objectivity of Henry Blodget and the Internet Group.

The Material Omissions and/or Misrepresentations In The "Details About The Fund" Section Of The Prospectus

105. Under the "How The Fund Invests" subheading, p. 7, the Registration Statement/Prospectus stated in relevant part:

The Fund also will invest in Internet related companies that currently use or are developing various other Internet applications – such as electronic commerce, e-mail and Intranet communications – as an integral part of their business strategies. For example:

- Many wholesale and retail companies are making increasing use of the Internet to sell their products and services....

The Fund may invest in Internet and Internet related companies that are not yet profitable but that the Investment Adviser believes are likely to produce earnings or revenue growth or operating efficiencies through the development of new or innovative products, services or processes.

106. The statements set forth in the foregoing paragraphs were materially false and misleading at the times they were made because:

- a. it omits to state that the Investment Advisor would also be willing to invest in companies that Blodget and the Internet Group believed were not likely to produce earnings growth;
- b. the Internet Strategies Fund was being marketed at a time when the Internet Group published strong investment ratings on all Internet companies followed by Merrill Lynch even though those analysts, including Blodget, held negative personal views of those same stocks;
- c. Merrill Lynch analysts including Blodget and the Internet Group published strong ratings on Internet stocks in order to secure investment banking business; and

d. substantial conflicts of interests existed within Merrill Lynch that broke through any "Chinese Walls" that were established to ensure the objectivity of Blodget and the Internet Group.

107. Under the "Investment Risks" subheading, p. 10, the Registration Statement/Prospectus stated in relevant part:

The Fund's principal risks include:

Sector Risk — Sector risk is the risk that the Fund's focus on the securities of Internet and Internet related companies will expose the Fund to the price movements in one industry more than a more broadly diversified mutual fund. Because the Fund invests primarily in a limited number of market sectors, there is a risk that the Fund will perform poorly during a downturn in either market sector. An investment in the Fund is subject to the risks associated with equity securities issued by Internet and Internet related companies, as noted. The Fund should not be considered a balanced investment program by itself.

Internet and Internet Related Company Risk — Although Internet and Internet related companies comprise a relatively new industry, equity securities issued by these companies historically have been extremely volatile. Volatility increases the risk that the securities may lose value. Many factors may affect the value of an Internet or Internet related company. These factors include the ability of a company to keep pace with rapidly changing technology and a geometrically expanding consumer base. Competition among Internet and Internet related companies is intense, and profit margins can be small or nonexistent. In fact, many Internet and Internet related companies operate at substantial losses with no prospect for profit in the foreseeable future. For these reasons, the Fund and its investments may be considered speculative.

The Fund may invest in smaller companies that the Investment Adviser believes have potential for capital appreciation. These companies may have short operating histories, may not be publicly traded and may not yet be profitable. The securities of such companies share the characteristics common to small cap and emerging growth securities including limited product lines or markets. Such securities may be less financially secure than larger or more established companies, may depend on

a small number of key personnel and, if publicly traded, may trade in lower volumes than larger or more established companies. Internet related companies that establish a presence on the World Wide Web often face the challenge of maintaining personnel and systems adequate to respond efficiently to Internet demand. As a result, Internet and Internet related companies may be subject to more abrupt and erratic price movements than the stock market as a whole.

Internet and Internet related companies are strongly affected by worldwide scientific or technological developments. As a result, their products may rapidly become obsolete. Such companies are often subject to governmental regulation and may therefore be adversely affected by government policies.

Small Cap and Emerging Growth Securities Risk — In addition to the risks listed above with respect to Internet and Internet related companies, small cap or emerging growth companies are subject to the risk that if a product fails, or if management changes, or there are other adverse developments, the Fund's investment in a small cap or emerging growth company may lose substantial value. Investing in small cap and emerging growth securities requires a long term view.

Market and Selection Risk — Market risk is the risk that the stock market in one or more countries in which the Fund invests will go down in value, including the possibility that the market will go down sharply and unpredictably. Selection risk is the risk that the investments that the Investment Adviser selects will under perform the stock market or other funds with similar investment objectives and investment strategies.

108. The statements set forth in the foregoing paragraphs were materially false and misleading at the times they were made because:

a. it omitted to state that the Investment Advisor would also be willing to invest in companies that Merrill Lynch analysts including Blodget and the Internet Group believed were not likely to produce earnings growth;

b. it omitted to state the Internet Strategies Fund was being marketed at a time when the Internet Group published strong investment ratings on all Internet companies

followed by Merrill Lynch even though those analysts, including Blodget, held negative personal views of those same stocks;

c. it omitted to state that Merrill Lynch analysts including Blodget and the Internet Group published strong ratings on Internet stocks in order to secure investment banking business; and

d. it omitted to state that substantial conflicts of interests existed within Merrill Lynch that broke through any "Chinese Walls" that were established to ensure the objectivity of Blodget and the Internet Group.

The Material Omissions and/or Misrepresentations In The "Additional Information: Investment Objective and Policies" Section Of The Prospectus

109. Under the "Investment Objective and Policies" heading, p. 2, the Registration Statement/Prospectus stated in relevant part:

The investment objective of the Fund is to seek long term growth of capital through investment primarily in equity securities of issuers that the Investment Adviser believes will use the Internet as a component of their business strategies. The Fund seeks to achieve its investment objective by identifying issuers that engage in research, design, development, manufacturing or distribution of products or services used to facilitate use of the Internet, including issuers focusing on applications to be used in connection with the World Wide Web ("Internet companies") and issuers that use or are developing an internet strategy that the Investment Adviser believes will significantly benefit the issuers by improving its customer base, cost efficiencies, competitive advantage, and/or business prospects ("Internet related companies"). The Fund may invest in Internet companies and Internet related companies that are not yet profitable but that the Investment Adviser believes are likely to produce earnings or revenue growth or operating efficiencies through the development of new or innovative products, services or processes.

As described in the Prospectus, when selecting investments for the Fund, the Investment Adviser seeks to identify Internet and Internet related companies that are developing new or innovative products, services or processes that the Investment Adviser

believes are likely to produce earnings or revenue growth or operating efficiencies. Specifically, Internet companies may produce, market or distribute products or services designed to secure, enhance, store, process, record, reproduce, retrieve or distribute information over the Internet. Many of these issuers focus on applications that utilize the World Wide Web (the "Web"). The Web is a widely used graphical interface publishing medium that may contain text, graphics, interactive feedback mechanisms and cross linking functions. The Fund also invests in Internet related companies that currently use or intend to use various other Internet applications—such as electronic commerce, e-mail and Intranet communications systems (systems that use Internet technology to share information within a company's internal computer network)—as integral parts of their business strategies.

The Fund's focus on the securities of Internet and Internet related companies heightens its exposure to price movements in one industry more significantly than a more broadly diversified mutual fund. Because the Fund invests primarily in one industry, there is a risk that the Fund will perform poorly during a downturn in that industry. Internet and Internet related companies are also strongly affected by worldwide scientific or technological developments. As a result, their products may rapidly become obsolete.

110. The statements set forth in the foregoing paragraphs were materially false and misleading at the times they were made because:

- a. it omitted to state that the Investment Advisor would also be willing to invest in companies that Blodget and the Internet Group believed were not likely to produce earnings growth;
- b. it omitted to state the Internet Strategies Fund was being marketed at a time when the Internet Group published strong investment ratings on all Internet companies followed by Merrill Lynch even though those analysts, including Blodget, held negative personal views on those same stocks;
- c. it omitted to state that Blodget and the Internet Group published strong ratings on Internet stocks in order to secure investment banking business; and

d. it omitted to state that substantial conflicts of interests existed within Merrill Lynch that broke through any "Chinese Walls" that were established to ensure the objectivity of Blodget and the Internet Group.

111. Under the "Description of Certain Investments" subheading, p. 3-4, the Registration Statement/Prospectus stated in relevant part:

... The Investment Adviser believes that properly selected companies of this type have the potential to increase their earnings or market valuation at a rate substantially in excess of the general growth of the economy. Full development of these companies and trends frequently takes time and, for this reason, the Fund should be considered as a long-term investment and not as a vehicle for seeking short-term profits.

While the process of selection and continuous supervision by the Investment Adviser does not, of course, guarantee successful investment results, it does provide access to an asset class not available to the average individual due to the time and cost involved. Careful initial selection is particularly important in this area as many new Internet and Internet related companies have promise but lack certain of the fundamental factors necessary to prosper. Investing in these companies requires specialized research and analysis. In addition, many investors cannot invest sufficient assets in such companies to provide wide diversification.

Small companies are generally little known to most individual investors although some may be dominant in their respective industries. The Investment Adviser believes that relatively small Internet and Internet related companies will continue to have the opportunity to develop into significant business enterprises. The Fund may invest in securities of small issuers in the relatively early stages of business development which have a new technology, a unique or proprietary product or service or a favorable market position. Such companies may not be counted upon to develop into major industrial companies, but management believes that eventual recognition of their special value characteristics by the investment community can provide above-average long-term growth to the Fund.

Equity securities of specific Internet and Internet related companies may present different opportunities for long-term capital appreciation during varying portions of economic or

securities markets cycles, as well as during varying stages of their business development. The market valuation of small cap issuers tends to fluctuate during economic or market cycles, presenting attractive investment opportunities at various points during these cycles.

112. The statements set forth in the foregoing paragraphs were materially false and misleading at the times they were made because:

a. it omitted to state that the Investment Advisor would also be willing to invest in companies that Blodget and the Internet Group believed were not likely to produce earnings growth;

b. it omitted to state the Internet Strategies Fund was being marketed at a time when the Internet Group published strong investment ratings on all Internet companies followed by Merrill Lynch even though those analysts, including Blodget, held negative personal views on those same stocks;

c. it omitted to state that Blodget and the Internet Group published strong ratings on Internet stocks in order to secure investment banking business; and

d. it omitted to state that substantial conflicts of interests existed within Merrill Lynch that broke through any "Chinese Walls" that were established to ensure the objectivity of Blodget and the Internet Group.

THE TRUTH EMERGES

113. On April 8, 2002 it was reported in the New York Times that Eliot L. Spitzer, the Attorney General of New York, obtained a court order forcing Merrill Lynch to make immediate changes to its stock reports. Spitzer called the investment advice of Merrill Lynch "tainted." The Order, by a New York State Supreme Court judge, directed Merrill Lynch to disclose in its published research whether a company is an investment banking client or a prospective client.

114. On April 18, 2002, Merrill Lynch agreed to alter its disclosure policy and issued a press release that stated in part:

Merrill Lynch has reached agreement with the New York State Attorney General on additional disclosures in securities research reports.

The added disclosure provisions are as follows:

- By April 24, 2002, Merrill Lynch will implement a website that will disclose, for companies covered in research reports, those companies which have engaged in publicly announced equity underwritings and merger and acquisition transactions over the prior 12 months, for which Merrill Lynch has received, or is entitled to receive, compensation. Language directing readers to the website will be included in research reports.
- By June 3, 2002, Merrill Lynch will replace this website disclosure by stating in equity research reports whether it has received, or is entitled to receive from the covered company, compensation from publicly announced equity underwriting and merger and acquisition transactions over the prior 12 months.
- By June 3, 2002, Merrill Lynch will include language on the first page of equity research reports stating that investors should assume that Merrill Lynch is seeking, or will seek, investment banking and other business from the covered company.
- By June 3, 2002, Merrill Lynch will include in equity research reports specific disclosure, on a percentage basis, for the intermediate-term "strong buy," "buy," "neutral" and "reduce/sell" ratings for stocks in the following categories:
 1. All stocks in the sector or industry group applicable to the covered company.
 2. All stocks in the applicable sector or industry group from which Merrill Lynch has received or is entitled to receive compensation for publicly announced equity underwriting and merger and acquisition transactions over the prior 12 months.
 3. All stocks covered by Merrill Lynch Global Equity Research.
 4. All stocks covered by Merrill Lynch Global Equity Research from which Merrill Lynch has received or

is entitled to receive compensation for publicly announced equity underwriting and merger and acquisition transactions over the prior 12 months.

CLAIM FOR RELIEF

**Against Internet Strategies Fund, Director Defendants And MLFD
For Violation of Section 11 of the Securities Act and Against Director
Defendants Under Section 15 of the Securities Act for Violation of Section 11**

Count I

115. Plaintiffs incorporate each of the foregoing paragraphs as if fully set forth herein. This Count is asserted against Internet Strategies Fund, Director Defendants and MLFD for violations of Section 11 of the Securities Act, 15 U.S.C. § 77(k), and against the Director Defendants for liability under Section 15 of the Securities Act, 15 U.S.C. § 77(o) for violations of Section 11 of the Securities Act.

116. The Internet Strategies Fund is the issuer of the shares sold via the Registration Statement/Prospectus. The Director Defendants are signatories of the Registration Statement/Prospectus and were Directors and/or officers of the Company at the time of the Offering. MFLD was one of the underwriters of the Internet Strategies Fund's stock offering.

117. Internet Strategies Fund, Director Defendants and MLFD participated in the preparation of, issued, caused to be issued and participated in the issuance of the materially false and misleading Registration Statement/Prospectus, which was inaccurate and misrepresented or failed to disclose, inter alia, the material facts concerning the Internet Strategy Fund's business and prospects, as set forth herein. None of these defendants made a reasonable investigation or possessed reasonable grounds for the belief that the statements contained in the Registration Statement/Prospectus were true, without omissions of any material facts and were not misleading.

118. MFLD assisted in the preparation of the Registration Statement/Prospectus, and was required to investigate with due diligence the representations contained therein to confirm that they did not contain materially misleading statements or omit to state material facts. MFLD did not perform this investigation with due diligence and, indeed, had a substantial direct interest in the success of the Offering, as detailed above and, thus, is liable under Section 11 of the Securities Act.

119. Director Defendants as directors and/or officers of the Internet Strategies Fund and as signatories of the Registration Statement/Prospectus that was filed with the SEC were responsible for the preparation of the Registration Statement/Prospectus and failed to make a reasonable investigation or possess reasonable grounds for believing that the representations contained in the Registration Statement/Prospectus were true and that they disclosed all material facts. Director Defendants are primarily liable under Section 11 of the Securities Act and are also secondarily liable as controlling persons of the Internet Strategies Fund under Section 15 of the Securities Act.

120. As a direct and proximate result of the false and misleading statements in the Registration Statement/Prospectus, roughly 100 million shares of the Internet Strategies Fund common stock was sold in the Offering for approximately \$1.1 billion and by October 2001 when the Internet Strategies Fund ceased to exist as a standalone fund, the Internet Strategies Fund had lost more than 75% of its value and was worth approximately \$280.8 million.

121. Plaintiffs and other members of the Class purchased their Internet Strategy Fund shares in or traceable to the Offering without knowledge of the untruths or omissions alleged herein.

122. The action was brought within one year after the discovery of the untrue statements and omission and within three years after the Internet Strategies Fund was offered to the public.

Count II

**Against Merrill Lynch, Blodget, Meeks, Internet Strategies
Fund, MLFD and Director Defendants for Violation of Section 12
Of the Securities Act and Against the Director Defendants
Under Section 15 of the Securities Act for Violation of Section 11**

123. Plaintiffs incorporate each of the foregoing allegations as if fully set forth herein. This count is asserted against Merrill Lynch, Blodget, Meeks, Internet Strategies Fund, MLFD and the Director Defendants, for violation of Section 12(a)(2) of the Securities Act, 15 U.S.C. § 771, and against the Director Defendants for liability under Section 15 of the Securities Act, 15 U.S.C. § 77(o), for violation of Section 12(a)(2) of the Securities Act.

124. Merrill Lynch, Blodget, Meeks, Internet Strategies Fund, MLFD and the Director Defendants were sellers, offerors, and/or solicitors of sales of the Internet Strategy Fund common stock for their financial benefit pursuant to the Registration Statement/Prospectus in connection with the Offering. None of the defendants named in this Count made a reasonable investigation or possessed reasonable grounds for the belief that the statements contained in the Registration Statement were true, without omissions of any material facts and were not misleading.

125. The Registration Statement/Prospectus contained misstatements of material facts, omitted to state other facts necessary to make the statements made not misleading, and concealed and failed to disclose material facts. Merrill Lynch, Blodget, Meeks, and MLFD's actions of solicitation included participating in "road shows" to promote the sale of the Internet

Fund common stock as well as the preparation of the false and misleading Registration Statement/Prospectus disseminated to public investors.

126. The Director Defendants, as Directors and/or officers of the Internet Strategies Fund at the time of the Offering and as signatories of the Registration Statement/Prospectus that was filed with the SEC, were responsible for the preparation of the Registration Statement/Prospectus and failed to make a reasonable investigation or possess reasonable grounds for believing that the representations contained in the Registration Statement/Prospectus were true and that they disclosed all material facts. The Director Defendants are primarily liable under Section 12 of the Securities Act and are also secondarily liable as controlling persons of the Internet Fund under Section 15 of the Securities Act.

127. Plaintiffs and other members of the Class purchased the Internet Strategies Fund common stock issued pursuant to the false and misleading Registration Statement/Prospectus. Plaintiff did not know, or in the exercise of due diligence could not have known, of the untruths and omissions contained in the Registration Statement/Prospectus.

128. By reason of the conduct alleged herein, the MLFD violated, and/or controlled a person who violated Section 12(a)(2) of the Securities Act.

129. Plaintiffs, individually and representatively, hereby elects to rescind and tender to the Underwriter Defendant those securities that plaintiff and the other members of the Class continue to own, in return for the consideration paid for those securities together with interest thereon. Plaintiff and members of the Class who have sold their Internet Strategies Fund common stock are entitled to rescissory damages.

130. The action was brought within one year after the discovery of the untrue statements and omission and within three years after the common stock was offered to the public.

PRAYER FOR RELIEF

WHEREFORE, plaintiffs, on behalf of themselves and the Class, pray for Judgment as follows:

a. declaring this action to be a plaintiff class action properly maintained pursuant to Rule 23(a) and (b)(3) of the Federal Rules of Civil Procedure and declaring plaintiff to be proper Class representative;

b. finding that the Defendants violated Section 11, Section 12 and Section 15 of the Securities Act of 1933 promulgated thereunder by their acts and omissions as alleged in this Complaint;

c. awarding plaintiffs and the members of the Class damages, together with interest thereon;

d. awarding plaintiffs and other members of the Class their costs and expenses of this litigation, including reasonable attorneys' fees and experts' fees and other costs and disbursements; and

e. awarding plaintiffs and other members of the Class such other and further relief as may be just and proper under the circumstances.

Jury Demand

Plaintiffs demands a trial by jury.

Dated: April 24, 2002

Respectfully submitted,

ABBHEY GARDY, LLP

By: 

Mark C. Gardy (MG-0338)
212 East 39th Street
New York, NY 10016
(212) 889-3700

02

CERTIFICATION OF LEAD PLAINTIFF
PURSUANT TO FEDERAL SECURITIES LAWS

1. Richard & Linda Sherman, certify that:

1. I have reviewed a copy of the complaint filed in this action.
2. I did not purchase the Merrill Lynch Internet Strategies Fund that is the subject of this action at the direction of plaintiff's counsel, or in order to participate in any private action arising under the Private Securities Litigation Reform Act (the "PSLRA").
3. I am willing to serve as a representative party on behalf of a class and will testify at deposition and trial, if necessary.
4. My transactions in the security that is the subject of this litigation during the class period set forth in the complaint are as follows:

<u>No. of Shares</u>	<u>Stock Symbol</u>	<u>Buy/Sell Date</u>	<u>Price Per Share</u>	
<u>2,381</u>	<u>MDNTX</u>	<u>3/17/2000</u>	<u>\$10.4990</u>	<u>still own</u>
_____	_____	_____	_____	_____
_____	_____	_____	_____	_____
_____	_____	_____	_____	_____

*List additional transactions on a separate sheet of paper, if necessary.

5. I have not served as or sought to serve as a representative party on behalf of a class under this statute during the last three years.
6. I will not accept any payment for serving as a representative party, except to receive my pro rata share of any recovery or as ordered or approved by the court or any award to me by the Court of reasonable costs and expenses (including lost wages) directly relating to my representation of the class.

The foregoing are, to the best of my knowledge and belief, true and correct statements.

Dated: 4/24/02

Signed: 
