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United States District Court
Southern District of New York

IN RE WINSTAR COMMUNICATIONS SECURITIES LITIGATION	:	Master File No. 01 Civ. 3014 (GBD)
This Document Relates	:	
To:All Actions	:	SECOND CONSOLIDATED AMENDED COMPLAINT

Lead Plaintiffs and the additional listed plaintiffs identified below (collectively, "Plaintiffs") allege the following based upon the investigation conducted by and through their undersigned attorneys, except as to those paragraphs relating to Plaintiffs, their purchases of the securities of Winstar Communications, Inc. ("Winstar" or the "Company") or their suitability to serve as class representatives. Those allegations are alleged upon Plaintiffs' personal knowledge. The investigation of Plaintiffs' counsel has included, but has not been limited to, the following: (a) the review and analysis of the filings made by Winstar with the United States Securities and Exchange Commission ("SEC"); (b) the review and analysis of the press releases identified in this Amended Complaint (the "Complaint"); (c) the review and analysis of the analyst reports, newspaper, magazine and other periodical articles identified in the Complaint; (d) the review and analysis of the filings made by Winstar, its employees and others in Winstar's Chapter 11 bankruptcy proceeding in the United States District Court for the District of Delaware (the "Winstar Bankruptcy") that are identified in this Complaint; and (e) interviews of former Winstar employees, customers, institutional investors and other witnesses conducted by Plaintiffs' counsel.

I. SUMMARY OF CLAIMS

1. This is a class action brought by Plaintiffs on behalf of a class consisting of all persons who purchased the common stock or publicly-traded bonds of Winstar during the period from March 10, 2000 until April 2, 2001(the "Class Period").

2. The defendants (collectively, "Defendants") include: William Rouhana, who was the Company's Chief Executive Officer ("CEO") and Chairman of the Board at all material times; Nathan Kantor, who was Winstar's President and Chief Operating Officer ("COO") throughout the Class Period; Richard J. Uhl, who was the Company's Chief Financial Officer ("CFO") throughout the Class Period; Grant Thornton LLP ("Grant Thornton"), the accounting firm that served as Winstar's outside auditor throughout the Class Period; and Lucent Technologies Inc. ("Lucent"), a designer, maker and seller of communications systems, software and products that engaged in a fraudulent scheme throughout the Class Period that had the effect of inflating the market prices of Winstar's publicly-traded securities. Defendants Rouhana, Kantor and Uhl are collectively referred to herein as the "Winstar Defendants." While Winstar's misconduct was co-extensive with that of the Winstar Defendants, the Company is not named as a defendant in this Complaint because it has filed a bankruptcy petition in the United States District Court for the District of Delaware.

3. As alleged herein, Defendants engaged in a variety of manipulative and deceptive schemes that served to vastly overstate Winstar's business success, sales and earnings and to facilitate a massive fraud on public investors. Among other things, Winstar engaged in numerous highly suspicious and unusual "end-of-quarter" transactions with Lucent - Winstar's largest supplier and single largest source of financing - and with other parties that served to falsely and artificially inflate the Company's reported sales and earnings. Most of these transactions lacked economic substance and could not properly serve as the basis for reported sales and revenues. As a result, much of the Company's reported revenues and earnings during the Class Period were fictitious in nature.

4. Winstar's transactions with Lucent were only vaguely disclosed to investors, and investors were never told that a significant portion of Winstar's revenue came from Lucent pursuant to unusual revenue-swapping transactions. Moreover, Defendants never disclosed that these improper transactions were the primary driver of the Company's seemingly positive growth trend, and that the Company's continued appearance of success necessarily depended on the participation of Lucent in these highly improper and secret revenue-swapping transactions.

5. In addition to transactions with Lucent, the Winstar Defendants engaged in similar unusual and improper end-of-quarter "revenue-swapping" transactions with various other customers.

6. As a result of these practices, as well as a virtually non-existent system of internal controls that allowed and encouraged gross misreporting of financial data, Winstar's financial results were materially misstated at all relevant times, including in both audited and unaudited financial results disseminated to public investors during the Class Period.

7. The Winstar Defendants also repeatedly made statements to the investing public during the Class Period that the Company's fundamental business position was strong and that the Company was well-funded at least through 2002. Remarkably, the Winstar Defendants continued to make such statements until only a few days before the Company filed the Winstar Bankruptcy in April 2001.

8. Defendant Lucent actively and substantially participated in the fraudulent scheme alleged herein. In particular, Lucent's fraudulent end-of-quarter transactions with Winstar were a principal source of the overstatements reflected on the Company's financial statements that had the effect of inflating the trading prices of Winstar's securities. Furthermore, while Winstar has specifically acknowledged that the Company was severely disappointed at all material times with Lucent's ability to provide the engineering services and components necessary to complete Winstar's broadband network, both the Winstar Defendants and Lucent concealed those material facts from investors throughout the Class Period.

9. Following the gradual and belated public revelation of Winstar's extreme financial distress, the prices of Winstar's securities collapsed.

10. As a result, Plaintiffs assert the claims alleged herein to recover damages and other appropriate relief on behalf of themselves and the members of the Class.

II. JURISDICTION AND VENUE

11. This Court has jurisdiction over the subject matter of this action pursuant to Section 27 of the Securities Exchange Act of 1934 (the "Exchange Act"), 15 U.S.C. § 78aa.

12. The claims asserted herein arise under Sections 10(b) and 20(a) of the Exchange Act (15 U.S.C. §§ 78j(b) and 78t(a)), and Rule 10b-5 promulgated thereunder by the SEC (17 C.F.R. § 240.10b-5).

13. Venue is proper in this District pursuant to Section 27 of the Exchange Act because Winstar maintains executive offices in this district. Furthermore, many of the alleged acts and transactions, and much of the conduct constituting violations of law, including the preparation, issuance, and dissemination to the investing public of materially false and misleading information, occurred, at least in part, in this District.

14. In connection with the acts alleged in this Complaint, Defendants, directly and indirectly, used the means and instrumentalities of interstate commerce, including the mails, telephone communications, and the facilities of the national securities exchanges.

III. THE PARTIES AND WINSTAR

A. Plaintiffs

15. By Order dated July 30, 2001, the Court appointed the "BIM Group" as Lead Plaintiffs in this action. As a group, the BIM Group plaintiffs have suffered aggregate losses estimated to be $6,487,781.48. The BIM Group's members are:

BIM Intermobiliare SGR (a wholly-owned subsidiary of Banca Intermobiliare di Investimenti E Gestioni SpA) - with losses of $4,595,040.20. BIM is an Italian asset management firm, and a wholly-owned subsidiary of an Italian bank, that made purchases primarily for the benefit of asset-management clients over whose accounts it enjoys discretion, as well as for its own account. BIM purchased both Winstar common stock and Winstar's 12¾% Bonds due in 2010;

Robert Ahearn - a Boston-based businessman, whose losses include those suffered individually as well as in his capacity as administrator of a corporate profit sharing plan - with losses of $878,983.28; and

DRYE Custom Pallets (a corporate investment account by its authorized representative Michael A. Kostrzewa) - a Michigan company with losses estimated to be $404,652.00.

16. In addition to the Lead Plaintiffs, plaintiffs Sanford Gould, David Rich, Richard Sulentic, and Andres Rios purchased shares of

Winstar common stock during the Class Period and have expressed their willingness to serve as class representatives in this action.

17. As a direct and proximate result of their purchases of Winstar securities during the Class Period, the Lead Plaintiffs, the additional plaintiffs identified herein and all of the members of the Class have suffered significant damages. All of those persons purchased Winstar securities at prices that were materially inflated as a result of the misrepresentations and omissions alleged herein. Moreover, all of those persons suffered economic losses when the market prices of those securities collapsed following the gradual and belated revelation that Winstar could not fund its operations and could not produce the progressively improving financial results referred to by Defendants during the Class Period.

B. Winstar

18. Non-party Winstar is a Delaware corporation with its principal executive offices located at 685 Third Avenue, New York, New York. Winstar is not named as a defendant in this case because it filed for bankruptcy protection in April 2001.

19. Winstar is a broadband services company. During the Class Period, Winstar claimed that it was building one of the world's most widely available, end-to-end broadband networks in order to provide telecommunications services to businesses. According to Winstar's filings with the SEC and other public representations, Winstar provided its customers with the following services and products: high-speed Internet connections and data transfer; Web hosting and design; telephone services; Web-based applications; and professional services. Winstar also operated Office.com, an online business service for small and medium-sized businesses.

C. Defendants

20. At all relevant times, defendant Rouhana was the Company's CEO and Chairman of the Board.

21. At all relevant times, defendant Kantor was the Company's President and COO.

22. At all relevant times, defendant Uhl was the Company's CFO.

23. By virtue of their roles as three of the Company's highest-ranking executives, defendants Rouhana, Kantor and Uhl were "control persons" of Winstar as that term is utilized in § 20(a) of the Exchange Act.

24. Rouhana was able to exercise control over Winstar's operations because he was the Company's highest-ranking executive. As a result, Rouhana served as the Company's primary voice in all press releases and interviews and actively participated in the day-to-day management of Winstar's affairs.

25. Kantor was able to exercise control over Winstar's operations because he was Winstar's second-highest ranking executive throughout the Class Period. In that role, Kantor was closely involved in all aspects of the day-to-day management of Winstar's affairs, including the misconduct alleged herein. Kantor also frequently served as the Company's voice in press releases and other public statements.

26. Uhl was able to exercise control over Winstar's operations because he was the Company's highest-ranking financial officer throughout the Class Period. As a result, he was intimately involved in all aspects of the day-to-day management of Winstar's operations, including the misrepresentations and omissions concerning Winstar's operations, financial results and prospects that are the subject of Plaintiffs' claims. Uhl also prepared the Company's false and misleading financial statements, participated in the drafting of the Company's financial releases, supervised and drafted material portions of the Company's SEC filings, and signed certain of the SEC filings described herein.

27. It is appropriate to presume that the issuance of the false, misleading and incomplete information concerning Winstar conveyed to Plaintiffs, the members of the Class and other investors during the Class Period resulted from the collective actions of the Winstar Defendants. The Winstar Defendants served as the Company's public spokespersons, participated in drafting, reviewing and disseminating the false and misleading statements and information alleged herein, and were aware of the material adverse facts that rendered those statements false and misleading.

28. Defendant Grant Thornton is a worldwide firm of certified public accountants, auditors and consultants. Throughout the Class Period, and for several years prior to that time, Grant Thornton, through its New York City office, served as Winstar's auditor and principal accounting firm.

29. Defendant Lucent is a designer, maker and seller of communications systems, software and products. Lucent maintains its principal executive offices at 600 Mountain Avenue, Murray Hill, New Jersey 07974. Lucent engages in significant business activities throughout the world, including New York City.

IV. PLAINTIFFS' CLASS ACTION ALLEGATIONS

30. Plaintiffs bring this action as a class action pursuant to Federal Rule of Civil Procedure 23. The "Class" consists of all persons and entities who were damaged as a result of their purchases of Winstar common stock on the open market during the Class Period, or who were damaged as a result of their purchases of Winstar's publicly traded bonds during the Class Period. The following persons are excluded from the Class: Defendants; the officers and directors of the Company; the members of those persons' immediate families;

those persons' legal representatives, heirs, successors and assigns; and any entity in which any Defendant has or had a controlling interest.

31. The Class is so numerous that joinder of all Class members is impracticable. While the exact number of Class members is unknown to Plaintiffs at this time and can only be ascertained from the records maintained by Winstar or its agents, as of November 9, 2000, there were 92,224,263 shares of Winstar common stock outstanding. Those shares were held by what Plaintiffs believe were thousands of shareholders who were located throughout the world.

32. Furthermore, during the Class Period, Winstar had more than $2 billion of publicly traded bonds which were sold to members of the Class and actively traded by investors. Those bonds were purchased by hundreds if not thousands of investors located throughout the world. As a result, it is reasonable to believe that there are thousands of members of the Class. v 33. Plaintiffs' claims are typical of the claims of the members of the Class because all members of the Class purchased Winstar securities during the Class Period and sustained damages as a result of the same misconduct, as alleged herein.

34. Plaintiffs will fairly and adequately protect the interests of the members of the Class. Plaintiffs have retained counsel competent and experienced in class action and securities litigation and Plaintiffs have no interests antagonistic to or in conflict with the other members of the Class. Furthermore, as is set forth in the attached certifications, all of the Plaintiffs have suffered substantial economic losses as a result of Defendants' misconduct and, therefore, have significant incentive to prosecute this action diligently.

35. A class action is superior to other available methods for the fair and efficient adjudication of this controversy. Because there are many Class members and those persons are located throughout the world, joinder of all Class members is impracticable. Moreover, individual Class members are foreclosed from prosecuting separate claims because the damages suffered by most Class members are far smaller than the expenses associated with individual actions. Thus, it is desirable for all concerned to conduct this litigation on behalf of all Class members in a single forum. No unusual difficulties are likely to be encountered in the management of this class action.

36. There are numerous questions of law and fact common to the members of the Class that predominate over any questions affecting only individual Class members. These common questions of law and fact include, among others:

a. whether Defendants violated Sections 10(b) and 20(a) of the Exchange Act and SEC Rule 10b-5;
b. whether Defendants participated in the common course of conduct complained of herein;
c. whether documents, releases, reports, and statements disseminated to the investing public during the Class Period failed to disclose or misrepresented material facts concerning the Company's financial condition and operations;
d. whether Defendants acted with knowledge or with reckless disregard for the truth in omitting and/or misrepresenting material facts concerning the Company's revenues, net income, operations, financial status and prospects;v e. whether, during the Class Period, the market prices of Winstar common stock and bonds were artificially inflated due to the non-disclosures and/or material misrepresentations complained of herein; and
f. whether the members of the Class have sustained damages, and, if so, the proper measure thereof.

V. THE FACTS AND CIRCUMSTANCES THAT DEMONSTRATE THAT DEFENDANTS' CLASS PERIOD REPRESENTATIONS WERE MATERIALLY FALSE AND MISLEADING

37. Throughout the Class Period, Defendants made a series of misrepresentations and omissions concerning Winstar that had the effect of inflating the prices at which the Company's securities traded or of maintaining the prices of those securities at artificially high levels. As is alleged in detail below, the misrepresentations and omissions made by Defendants can be categorized as concerning: (a) the Company's financial results, particularly its revenue, margins, EBITDA and net income; (b) the sources of the Company's revenues, particularly the Company's heavy reliance upon transactions with Lucent to generate substantial revenue; (c) the status of the Company's relationship with Lucent, which was Winstar's principal supplier and financier; (d) the Company's liquidity and ability to fund its continuing operations and the ambitious expansion plan heralded by the Winstar Defendants throughout the Class Period; and (e) the Company's grossly deficient system of internal controls and the abusive business practices allowed and encouraged by this environment.

A. Defendants' Material Misrepresentations And Omissions Concerning The Company's Financial Results

38. As is specifically alleged below, throughout the Class Period, Defendants made repeated misrepresentations in which they overstated the Company's revenue, gross margins, EBITDA, and net income in order to portray the Company as a growing concern that was successfully adding customers as it built the nationwide broadband network that the Winstar Defendants claimed would enable the Company to achieve profitable operations.

39. The Winstar Defendants and Lucent inflated the Company's financial results principally by engaging in large, end-of-quarter transactions that lacked economic substance, but which enabled the Company to report the growing revenues that the Winstar Defendants repeatedly told investors to expect from the Company. The Winstar Defendants made those promises of improved revenues, and authorized the fraudulent transactions with Lucent, in order to attract the investment capital necessary to fund the build-out of the Company's broadband network.

40. Creating the impression that Winstar was a rapidly-growing enterprise was a necessary condition to the Winstar Defendants' expansion plans because the Company suffered staggering losses throughout the Class Period as the Winstar Defendants made billions of

dollars in capital expenditures in an effort to build-out the Company's broadband network before investors lost interest in funding Winstar's operations.

41. Lucent was willing to participate in the Winstar Defendants' fraudulent efforts to inflate Winstar's revenues because, as a quid pro quo for the large payments made to Winstar for engineering and design services for Winstar's broadband network during the Class Period, Winstar agreed to "purchase" large volumes of Lucent products that Winstar did not need.

42. In that way, both Lucent and Winstar benefitted from the fraudulent transactions because both companies were able to report the large revenue gains that they had promised investors they could expect. Demonstrating substantial revenue growth was of extraordinary importance to Winstar because, throughout the Class Period, investors focused heavily upon revenue growth in valuing telecommunications concerns such as Winstar.

43. The large, end-of-quarter Winstar-Lucent transactions lacked economic substance because those transactions were not driven by the legitimate economic self-interests of the two companies. Rather, they were conducted solely to create the impression that the two companies were producing substantial revenue growth.

44. The unusual nature of the end of quarter Lucent-Winstar transactions is reflected in a December 20, 1999 e-mail from Chuck Naylor of Lucent to Allan Zendle of Winstar. In that e-mail, Naylor described an "EOQ Letter," i.e., an End of Quarter Letter, that he expected to receive from Zendle of Winstar. The text of the e-mail states: As part of our mutual [end of quarter] activities, one of the things that we need on our end is a letter from Winstar that allows us to recognize revenues for the Optical products you're purchasing. I've kept this as simple as possible by using the same letter from last quarter with changes noted in red (see attached). Note, the change has to do with the risk of loss upon shipment (a.k.a. insurance). I'm happy to address any incremental changes you may incur as a result of the change. Our plan is to cover these topics more broadly when we close on the addendum to the Supply Agreement.

Your support of this request is appreciated!

45. Thus, the Naylor e-mail demonstrates that large end-of-quarter transactions between Lucent and Winstar were commonplace. Furthermore, the e-mail strongly suggests that Winstar was intimately involved in Lucent's efforts to inflate its own revenue through those transactions.

46. The mechanics of the transactions worked as follows. Towards the end of each quarter of 1999 and the Class Period, Lucent would request that the Company make substantial purchases of Lucent telecommunications equipment in order to enable Lucent to meet the revenue objectives that it had promised investors they could expect.

47. Although Winstar never needed all of the equipment that Lucent desired to sell to the Company, the Winstar Defendants recognized that they were beholden to Lucent. That was the case because, in October 1998, Lucent and Winstar signed a "Supply Agreement" whereby Winstar obligated itself to purchase most of the telecommunications equipment for the Company's broadband network from Lucent. Furthermore, in connection with that transaction and a 1998 "Credit Agreement" between Lucent and Winstar, Lucent agreed to provide the Company with $2 billion of "vendor financing" to fund Winstar's operations.

48. The terms of those agreements were highly unorthodox. The typical vendor financing agreement provides a customer only with sufficient funds to make purchases of equipment from the vendor. In exchange for Winstar's agreement to work closely with Lucent to maximize Lucent's revenues, however, Lucent agreed to provide Winstar with financing equal to 30% more than the amount of the products purchased by the Company from Lucent. In addition, Lucent agreed to permit Winstar to utilize the proceeds of the loans received from Lucent to finance the purchases of other companies' products.

49. Thus, throughout the Class Period, Winstar was highly dependent upon Lucent for the equipment necessary to build the Winstar broadband network, and, even more importantly, for the financing provided to the Company, which was perpetually short of capital to finance the Winstar Defendants' expansion plans.

50. As a result, Winstar generally agreed each quarter to make substantial purchases of equipment from Lucent at Lucent's behest although the Company frequently did not need the equipment provided by Lucent. On each such occasion, Lucent loaned Winstar the funds necessary to purchase that equipment pursuant to the terms of the Supply Agreement and the Credit Agreement.

51. Accordingly, Winstar did not actually need to raise the cash necessary to purchase the Lucent equipment. Rather, it merely had to make interest payments on the debt associated with the equipment purchases pursuant to the terms of the Supply Agreement and the Credit Agreement.

52. One such transaction is described by Lucent in a Memorandum of Law filed by Lucent in connection with its motion to obtain relief from the automatic stay in the Winstar Bankruptcy. According to that document:

Pursuant to a "bill and hold" letter from Winstar, Lucent delivered [$8.6 million in telecommunications equipment] to the Pilot Warehouse in Phoenix, Arizona, between October 4, 2000 and January 1, 2001. The Pilot Warehouse is a third party storage facility for which Lucent pays rent. Lucent has paid all storage charges associated with storing the Phoenix Warehouse Collateral at the Pilot Warehouse. The Winstar bill and hold letter indicated that a large inventory of Stinger LS DSLAMs and cabinets was necessary for planned hub site deployments and that Winstar did not have the capacity to store the equipment. Winstar requested that Lucent provide interim warehousing for the equipment. [Winstar] did not take possession of the [equipment] before the Petition Date, but instead left that equipment in the Pilot Warehouse for storage at Lucent's expense. On May 10, 2001, three weeks after the petition date, [Winstar] first asked Lucent to remove the [equipment] from the warehouse.

53. Those motion papers also emphasized that Winstar "made no efforts to obtain possession of the [equipment] for over five months."

54. Thus, the Pilot Warehouse transaction resulted in Winstar purchasing a large inventory of telecommunications equipment from Lucent for which Winstar had no immediate use as its financial status rapidly deteriorated towards bankruptcy. The Pilot Warehouse transaction is therefore a prime example of Winstar's efforts to inflate Lucent's revenues as a quid pro quo for Lucent's decision to permit Winstar to bill Lucent for engineering and construction fees related to the work performed by Winstar to build-out its own broadband network.

55. The fact that Winstar made large purchases of equipment from Lucent although the Company had no use for that equipment is also demonstrated by a September 18, 2000 e-mail from Deborah Harris, the Vice President of Lucent's Customer Team, to Nina Aversano, Lucent's former President, North America - Service Provider Networks. In that e-mail, Harris stated that Winstar was "vehement that [it was] out of money and [did] not want to spend money on product that [it] cannot immediately utilize. The deals of the past are haunting us . . . there's $87M [of inventory] in their warehouse."

56. The fact that Lucent and Winstar were engaging in fraudulent transactions designed to inflate Winstar's revenue was well known at Lucent and Winstar, was ongoing since before Grant Thornton conducted its fiscal year 1999 auditing activities, and, accordingly, should have been easily identified by Defendants.

57. In an anonymous letter sent to Deborah C. Hopkins, Lucent's Chief Financial Officer, on August 8, 2000, an obviously knowledgeable Lucent employee described a pattern of fraudulent transactions designed to inflate Winstar's revenue. The letter did not specifically identify Winstar as the company referred to in the letter. Nevertheless, in a September 7, 2000 e-mail from Aversano to Hopkins and Richard McGinn, Lucent's President, CEO and Chairman, Aversano identifies the company as Winstar. The anonymous letter states:

Dear Ms. Hopkins:

I am writing to inform you of some Lucent accounting irregularities that I suspect are illegal. Please excuse me for writing anonymously.

About a year ago, I started hearing rumors of completely fabricated revenue, for both Lucent and its customer. Now I have friends (at very low levels of management) that complain of being forced to take part in such schemes.

Here's the way it works: a small customer (non-RBOC) contracts for a network to be provided (EF&I) by Lucent. As the quarter comes to a close, the customer adds $35M to the purchases for some special professional services. Lucent decides to outsource the services, so it hires the customer as its sub-contractor, for the price of $35M. The customer and Lucent exchange invoices and payments a day or so before the quarter ends, so both can recognize revenue immediately. No additional services are actually provided by either party. The purpose of the exchange, according to those involved, is to help the customer cook its books, though it obviously also inflates Lucent's revenues.

In a case I personally know of, the $35M of over-stated revenue represents over a third of the customer's quarterly revenue publicly reported. How will it look when this company fails and the SEC finds out that Lucent conspired to inflate its numbers?

58. The financial results announced by the Winstar Defendants during the Class Period also understated Winstar's expenses as a result of the Company's fraudulent transactions with Lucent.

59. Frequently, Lucent and Winstar would engage in end-of-quarter transactions for which Lucent would record revenue but agree to refrain from billing Winstar for a few days to allow Winstar to avoid recording the expense on the Company's quarterly financial statements.

60. That practice is described in a September 22, 2000 e-mail concerning the "Winstar/Lucent 2000 Partnership Deal" from Deborah Harris, the Vice President of Lucent's Customer Team. In that e-mail, Harris states that, in exchange for Winstar's commitment to purchase $187.8 million of Lucent products and services, Lucent would defer $63.4 million of billing properly made during the quarter ended December 31, 2000 until January 2, 2001.

61 The large, end-of-quarter deals between Lucent and Winstar were so prevalent that Lucent created a summary document entitled "Lucent/Winstar End of Quarter Deals, Fiscal Year 2000." In that document, Lucent states that it recognized $358.9 million of revenue in the period between October 1, 1999 and September 30, 2000 (Lucent's fiscal 2000) as a result of the end-of-quarter deals with Winstar, including $113.9 million in the fourth calendar quarter of 1999, $115 million in the first calendar quarter of 2000, and $113 million in the second calendar quarter of 2000.

62 The fact that Lucent's agreement to permit Winstar to bill Lucent for engineering fees related to the construction of Winstar's network was a quid pro quo for Winstar's agreement to purchase unneeded equipment from Lucent is made clear by a September 18, 2000 e-mail from Deborah Harris to Aversano. In that e-mail, Harris states that Lucent "pass[ed] through around $67M/Q of [revenue to] Winstar Services." She also noted, "We have been told to stop this practice. We will be communicating our position to Winstar the week of 9/18. . . . We may want to delay this move for a quarter based on this EOQ [end-of-quarter] deal."

63 It is also evident that the highest levels of Winstar management were aware of the efforts undertaken by Winstar and Lucent to inflate each other's reported revenue. In a September 22, 2000 letter to defendant Kantor, Harris informed Kantor that Lucent would no longer participate in the end-of-quarter deals designed to inflate the companies' revenues.

64 In response, Kantor sent a September 24, 2000 e-mail to Aversano. In that e-mail, Kantor stated that, if Lucent followed through on its proposal to stop permitting Winstar to bill Lucent tens of millions of dollars per quarter to build its own network, Winstar would no longer provide Lucent with its customary assistance in inflating Lucent's own revenue at quarter end. Kantor stated: I am very surprised and disappointed with this - we've only discussed and agreed on this a million times. This doesn't sit well with me and will have a major impact on our ability to help you this quarter.

You've got to get this fixed.

65 Eventually, Lucent relented in its efforts to extricate itself from the accounting scheme. In a September 27, 2000 letter from Aversano to Kantor, Lucent agreed to continue the fraudulent revenue "pass through" to Winstar.

66 Winstar also inflated its reported revenues and net income by improperly recognizing revenue in connection with transactions where Winstar's customers were provided with rights of return. For example, a December 30, 1999 e-mail from Bill Standish of Anixter International, Inc., a large distributor of telecommunications equipment, described one significant transaction in which Winstar granted Anixter a right of return.

67 The e-mail states:

3. Winstar -

$10 mil of radio[s] to be sold to Wannet [actually Wam!net] (sp)? at a margin of 7% if sold within 90 days 2% per month additional beyond 90 days. We will return after 6 months. 90 day payment terms. If little or no sales after 90 days we will not pay Winstar and have the option to return the product. Lucent will guarantee that we will collect and they will guarantee return of the product.

68 While GAAP prohibits vendors from recognizing revenue in connection with transactions involving a right of return until the product is actually sold to an end user, Plaintiffs believe that Winstar immediately recognized revenue at the time it shipped the radios to Anixter.

69 Similarly, Winstar engaged in numerous end-of-quarter revenue swapping schemes with other large customers, such as Angstrom, one of its Internet Service Provider business partners. For example, on April 6, 2001, amidst the fiscal crisis at the Company, Robert McGuire (a senior member of the Company's management team), with the direct approval of defendants Kantor and Uhl, arranged a $1,797,664 revenue swap with Angstrom, in which Winstar would wire transfer that amount to Angstrom at the beginning of the day, and Angstrom would wire the same amount back later in the day. In that regard, an e-mail from Les Ricalde at Winstar to Nate Kantor dated April 6, 2001, stated:

Nate,

At Bob's [McGuire's] direction, we seek your approval to exchange payments of equal amounts (1,797,664) with Angstrom on Monday, April 9. We remit the amount first and Angstrom has agreed to wire us back the money the same day.

Les Ricalde

No legitimate business reason existed for this transaction. Defendant Kantor provided approval for the transaction by e-mail on April 10, 2001, and the transfer took place on April 11, 2001. After Winstar made the transfer, Angstrom refused to return the money to Winstar.

70 As a result of the foregoing facts, Defendants misled investors concerning the financial performance of the Company during the Class Period in at least the following respects:

a0 The Company's revenue and income were overstated by at least $25 million per quarter;
b0 The Company's inventories, assets, shareholders' equity, gross profits and earnings per share were likewise each materially overstated;
c0 The Company's financial statements did not present, in all material respects, the Company's true financial condition, and did not reflect all adjustments which were necessary for a fair statement of the interim and full year periods presented;
d0 The Company's internal controls were grossly inadequate and, as a result, the Company's ability to record, process, summarize, and report financial data in its financial statements was significantly deficient;
e0 The Company's audited financial statements for the fiscal year 1999 (ending December 31, 1999) were not presented in conformity with GAAP or principles of fair reporting; and
f0 The Company's interim financial statements for each quarterly period during the Class Period were not presented in conformity with GAAP or principles of fair reporting.

71 In addition, the Winstar Defendants falsely and materially overstated the Company's net income and earnings per share for each of the Company's quarterly periods during the Class Period and for fiscal 1999. Moreover, by failing to file financial statements with the SEC which conformed to the requirements of GAAP, the Winstar Defendants and Grant Thornton violated the disclosure requirements of Regulation S-X, 17 CFR 210.4-01(a)(1), which provides that financial statements that do not conform to GAAP are presumptively

misleading and inaccurate.

72 As a result of the foregoing accounting improprieties, particularly with respect to the Winstar Defendants' accounting for the Company's transactions with Lucent, Defendants also violated at least the following provisions of GAAP:

a0 The principle that financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit and similar decisions was violated (FASB Statement of Concepts No. 1, 34);
b0 The principle that financial reporting should provide information about the economic resources of an enterprise, the claims to those resources, and the effects of transactions, events and circumstances that change resources and claims to those resources was violated (FASB Statement of Concepts No. 1, 40);
c0 The principle that financial reporting should provide information about how management of an enterprise has discharged its stewardship responsibility to owners for the use of enterprise resources entrusted to it was violated. To the extent that management offers securities of the enterprise to the public, it voluntarily accepts wider responsibilities for accountability to prospective investors and to the public in general (FASB Statement of Concepts No. 1, 50);
d0 The principle that financial reporting should provide information about an enterprise's financial performance during a period was violated. Investors and creditors often use information about the past to help in assessing the prospects of an enterprise. Thus, although investment and credit decisions reflect investors' expectations about future enterprise performance, those expectations are commonly based at least partly on evaluations of past enterprise performance (FASB Statement of Concepts No. 1, 42);
e0 The principle that financial reporting should be reliable in that it represents what it purports to represent was violated. That information should be reliable as well as relevant to a notion that is central to accounting (FASB Statement of Concepts No. 2, 58-59);
f0 The principle of completeness, which means that nothing is left out of the information that may be necessary to ensure that it validly represents underlying events and conditions, was violated (FASB Statement of Concepts No. 2, 79); and
g0 The principle that conservatism be used as a prudent reaction to uncertainty to try to ensure that uncertainties and risks inherent in business situations are adequately considered was violated. The best way to avoid injury to investors is to try to ensure that what is reported represents what it purports to represent (FASB Statement of Concepts No. 2, 95, 97).

73 Grant Thornton's opinions, insofar as they stated that its audits of the Company's financial statements were conducted in accordance with GAAS, were false and misleading because the following GAAS (AU 150) were knowingly and recklessly violated:

a0 Standard Of Field Work No. 2 was violated, which standard requires that a sufficient understanding of the internal control structure is to be obtained to plan the audit and to determine the nature, timing and extent of tests to be performed.
b0 Standard Of Field Work No. 3 was violated, which standard requires that sufficient competent evidential matter is to be obtained through inspection, observation, inquiries, and confirmations to afford a reasonable basis for an opinion regarding the financial statements under examination.
c0 Standard Of Reporting No. 1 was violated, which standard requires that the report shall state whether the financial statements are presented in accordance with generally accepted accounting principles.
d0 Standard Of Reporting No. 3 was violated, which standard requires that informative disclosures in the financial statements are to be regarded as reasonably adequate unless otherwise stated in the report.

74 The Winstar Defendants were required to disclose in the Company's financial statements the existence of the material facts described herein and to appropriately report transactions in conformity with GAAP. The Winstar Defendants failed to satisfy those obligations. Grant Thornton was, therefore, required pursuant to GAAS to express either a qualified or an adverse opinion on the Company's financial statements.

75 Grant Thornton violated GAAS in failing to express qualified or adverse opinions on the financial statements of the Company as of and for the fiscal year ended December 31, 1999.

B. Defendants' Material Misrepresentations And Omissions Concerning The Sources Of The Company's Revenues

76 As is specifically alleged below, throughout the Class Period, the Winstar Defendants made repeated representations concerning the Company's revenues in which they stated that those revenues were growing substantially as a result of customers' increasing acceptance of the products and services offered by Winstar.

77 In addition, each quarter during the Class Period the Winstar Defendants described the sources of the Company's revenues without making any mention of the fact that the largest single source of those revenues was the kick-backs paid to Winstar by Lucent for services purportedly performed by Winstar in designing and building its own broadband network.

78 The Company's heavy reliance upon Lucent as a source of revenues is demonstrated in an affidavit submitted by David Ackerman, an Executive Vice President at Winstar, in the Winstar Bankruptcy (the "Ackerman Affidavit"). In that affidavit, Ackerman states:
[Winstar] billed Lucent for build-out services on a quarterly basis. The bills increased over time and ranged from $25 million in the first quarter of 1999 to $67 million for the third quarter of 2000. The total billings for the years 1999 and 2000 were approximately $391 million, all of which Lucent paid.

79 Furthermore, the Lucent Complaint reveals that Winstar billed Lucent for $62 million in services performed by Winstar to build its own network during the first quarter of 2001.

80 In light of those facts, all of the Winstar Defendants' representations concerning the sources of the Company's revenue were

materially misleading as a result of Defendants' failure to disclose that the largest source of the Company's revenue was the fraudulent end-of-quarter transactions with Lucent.

81 Even putting aside the fraudulent nature of the Lucent-Winstar transactions, GAAP and applicable SEC regulations required Defendants to disclose that the Lucent transactions constituted such a significant portion of the Company's revenues.

82 The fact that Lucent was the source of such a large percentage of the Company's revenue was particularly significant to investors because of the numerous and substantial ties between the two companies. Indeed, had investors been informed that such a large percentage of the Company's revenue was generated through transactions with Lucent, investors would have disregarded the Winstar Defendants' statements that the Company was producing substantial revenue growth.

C. Defendants' Material Misrepresentations And Omissions Concerning The Status Of The Company's Relationship With Lucent And Its Efforts To Build-Out The Company's Broadband Network

83 As is specifically alleged below, throughout the Class Period, the Winstar Defendants made repeated statements concerning the purported success that they were enjoying in building-out the Company's nationwide broadband network. Furthermore, every Form 10-Q Quarterly Report and Form 10-K Annual Report filed by the Winstar Defendants with the SEC during the Class Period described the Credit Agreement and/or the Supply Agreement without disclosing that Winstar was experiencing any difficulty in its relationship with Lucent.

84 The terms of the Supply Agreement are described by Ackerman in the Ackerman Affidavit. In that document, Ackerman states that the Supply Agreement provided that "Lucent would eventually assume most, if not all, responsibility for the planning, development and construction of the [Winstar] network, after a short transition period." According to Ackerman, "The Supply Agreement had required Lucent to submit a transition plan within 45 days of the signing of the Supply Agreement to establish how Lucent would be taking over its responsibilities necessary for the expansion" of the Winstar network.

85 Critically, however, Winstar has conceded that, from shortly after the execution of the Supply Agreement in 1998, both Winstar and Lucent recognized that Lucent was incapable of providing the state of the art equipment or the engineering and construction services that it was supposed to deliver pursuant to the terms of the Supply Agreement. Specifically, in the Lucent Complaint, Winstar states: Despite the obligation to submit a transition plan within 45 days, Lucent did not supply any such plan at that time. In fact, Winstar began to experience problems with Lucent's technical expertise right from the start. Contrary to the representations in the Supply Agreement, Lucent did not have the required expertise to perform its functions under the Supply Agreement. Moreover, Lucent did not supply "Best of Breed" (which is defined as products and/or services that are commercially available and that have the best functionality for the lowest price) equipment.

86 Similarly, in the Lucent Complaint, Winstar has alleged that, "[a]lthough Lucent obligated itself to design, engineer, develop and construct the build-out of the network and to finance it, Lucent proved early on that it was unable to meet its obligations under the Supply Agreement." The Lucent Complaint also states, "Despite repeated requests by Winstar over a two-year period to develop the necessary expertise to meet its contractual obligations under the Supply Agreement, Lucent was unable to do so."

87 Likewise, the Ackerman Affidavit states, "What was worse, it turned out that Lucent did not have the expertise as represented in the Supply Agreement, and Lucent could therefore not meet its obligations under the Supply Agreement."

88 Thus, Winstar has stated that it was evident shortly after the signing of the Supply Agreement that Lucent could not perform its obligations under the Supply Agreement, including its obligation to supply Winstar with state of the art parts for its broadband network and to provide the engineering services necessary to design and build-out that network.

89 Winstar has also claimed in the Winstar Bankruptcy that, in order to supply a short term solution for Lucent's inability to perform its obligations under the Supply Agreement, the Company and Lucent agreed to enter a "Subcontract" whereby "Lucent retained [Winstar] to provided the network build-out support and services which the Supply Agreement had imposed on Lucent, but which Lucent was unable to perform."

90 The Ackerman Affidavit further provides:

The parties intended the Subcontract to be a limited solution, both in time and in functions, until Lucent was able to achieve the expertise necessary to undertake its responsibilities under the Supply Agreement. Unfortunately, Lucent made little effort to achieve such expertise, causing Winstar to become the primary source for planning, engineering, developing and building the network. Thus, [Winstar], which had anticipated supplying approximately 100 engineers and other employees to assist Lucent to oversee their work, had to retain more than 500 workers to perform the functions which Lucent was unable to perform, yet undertook to do so in the Supply Agreement.

91 The Lucent Complaint also demonstrates that Defendants were aware of Lucent's inability to perform its obligations under the Supply Agreement at all material times. In particular, Winstar has acknowledged that, "[t]hroughout the two-year period (1999-2000), Winstar repeatedly urged Lucent to assume full responsibility for all work related to the build-out of the network as the parties had agreed in the Supply Agreement. Lucent, however, failed to acquire the necessary expertise and management to implement the build-out plan."

92 The Ackerman Affidavit also reveals that friction between Lucent and Winstar concerning the requirements of the Supply Agreement

continued until the end of the Class Period. In that regard, the Ackerman Affidavit states that, as late as mid-December 2000, Winstar and Lucent were negotiating a "transition agreement" for Lucent to begin to perform its obligations under the Supply Agreement. Nevertheless, Ackerman states that, "upon information and belief, Lucent made decisions at or about that time that it was no longer interested in the services business; that it would not enter into any transition agreement; and that it would find ways to abandon its obligations under" certain agreements that provided for Lucent to build customer sites and traffic and distribution sites for Winstar. Furthermore, Ackerman states, "Beginning in early 2001, Lucent began to take steps to abandon the build-out related support activities and the financing of the network."

93 The existence of such conflicts between Lucent and Winstar was highly material to investors because of the nature of the ties between Lucent and Winstar. Indeed, in light of the fact that conflict between Lucent and Winstar eventually drove the Company into insolvency as a result of Lucent's refusal to continue to fund the Company's money-losing operations, the materiality of the disagreements between Lucent and Winstar is self-evident. These material facts were necessarily required to be included in the Company's financial statements for a complete and accurate understanding of Winstar's true financial position, and Defendants' failure to disclose these facts rendered the Company's financial statements - included audited financial statements - materially and grossly deficient and misleading at all relevant times.

94 The great materiality of the existence of conflict in the Winstar-Lucent relationship is also demonstrated by the Ackerman Affidavit. In that document, Ackerman states:

Lucent has created certain software and expertise for switching and other network gear and associated support systems, which are critical to the Winstar network, and Lucent is in control of that software and expertise. Lucent advised Winstar on April 10, 2001, that Lucent will provide no support or services to Winstar's network that is not specifically covered by warranty unless Lucent has received assurances of payment from Winstar. Most equipment in Winstar's network is not covered by warranty, and therefore in the event of outages or other problems with switches, fiber, ATM and other equipment and associated support systems, Lucent will refuse to use its customer technical support center to detect the problems and correct them. Such continued conduct by Lucent will cause concern among Winstar's customers and they may well look elsewhere for their communication services.

95 Furthermore, Ackerman states, "The abrupt abandonment of [Lucent's] technical support is placing the operations of the network and its related support systems in jeopardy, since Lucent is in control of the software, expertise and the customer technical support center which test and maintain the network and associated support systems.

96 Ackerman concluded, "Lucent's abandonment of its obligations under the Network Agreements has caused Winstar irreparable harm for which there is no remedy at law. Without injunctive relief, Winstar will face substantial, if not total loss of business."

97 The great significance of the existence of conflict in the Lucent-Winstar relationship is also demonstrated by an affidavit submitted in the Winstar Bankruptcy by Defendant Uhl. In that affidavit, Uhl states:

[W]ithout Lucent's financing and with their refusal to finance the first quarter's expenditures of $92 million, Winstar will not be able to pay its obligations as they become due. On April 16, 2001, Winstar was required to pay its noteholders approximately $75 million in interest. Winstar did not have the funds to make that payment. Thus, Winstar has been forced into bankruptcy, faces a loss of its business and has no adequate remedy at law.

98 Nevertheless, throughout the Class Period, investors were provided with no disclosures by Defendants concerning any disagreements between Lucent or Winstar or efforts undertaken by those two parties to correct any deficiencies in Lucent's performance under the terms of the Supply Agreement. To the contrary, Plaintiffs and the members of the Class were repeatedly assured that the Company's plans to expand its broadband network were proceeding according to, or ahead of, plan.

99 Defendants' representations concerning these matters - and their failure to make any disclosure concerning Winstar's efforts to force Lucent to comply with the terms of the Supply Agreement - were therefore materially misleading at all relevant times.

D. Defendants' Material Misrepresentations And Omissions Concerning Winstar's Liquidity And Ability To Fund The Expansion Of Its Broadband Network

100 During the Class Period, the Winstar Defendants assured Plaintiffs and the members of the Class on numerous occasions that Winstar had sufficient liquidity to fund its operations, including the Winstar Defendants' ambitious efforts to rapidly expand the Company's nationwide broadband network, an undertaking that would have required over $2 billion of capital expenditures by the Company by the end of 2002.

101 In fact, however, Winstar was perpetually on the verge of insolvency throughout the Class Period. For that reason, the Winstar Defendants repeatedly attempted to curry favor with Lucent by purchasing products from Lucent that the Company did not need. Furthermore, the Company's need for additional financing caused the Winstar Defendants to inflate the Company's revenues by means of the fraudulent end-of-quarter transactions with Lucent described above.

102 The fact that the Company bordered on insolvency throughout the Class Period is demonstrated by the swiftness of Winstar's bankruptcy filing following Lucent's declaration that Winstar was in default under the Credit Facility on April 16, 2001. The letter by which Lucent notified Winstar of that default stated that "an Event of Default has occurred and is continuing under clause (b) of Article VII of the [Credit Facility] as a result of the failure to pay the Refinancing Fee and interest and commitment fees on or prior to the

expiration of the Grace Period."

103 Within days of that declaration, Winstar was forced to withhold a $75 million interest payment from its bondholders and to file the Winstar Bankruptcy.

104 Furthermore, the events that led to the Winstar bankruptcy filing aptly demonstrate the Winstar Defendants' willingness to mislead investors concerning the Company's liquidity. At the end of 2001 and the beginning of 2001, the Winstar Defendants made repeated statements that the Company maintained adequate liquidity and that Lucent would continue to fund the Company's operations.

105 Winstar had admitted in the Lucent Complaint and the Ackerman Affidavit that, by that juncture, Winstar's relationship with Lucent had badly deteriorated.

106 For example, in the Lucent Complaint, Winstar alleges:

Beginning in January 2001, Lucent began in effect unilaterally to seek to amend the Network Agreements evidencing that it wished to withdraw from its obligations to build-out the network and to provide financing under the Network Agreements. Beginning in March 2001, Lucent simply walked away from its contractual obligations.

107 Furthermore, the Ackerman Affidavit states, "Beginning in early 2001, Lucent began to take steps to abandon the build-out related support activities and the financing of the network."

108 Lucent documents also reveal that Winstar had expressed grave concerns regarding its financial circumstances to Lucent well prior to the time the Winstar Defendants reassured investors concerning the Company's ability to continue to fund its operations. For example, in a September 18, 2000 e-mail from Harris to Aversano, Harris stated that Winstar was "vehement that [it was] out of money and [did] not want to spend money on product that [it] cannot immediately utilize. The deals of the past are haunting us . . . there's $87M [of inventory] in their warehouse."

109 Towards the end of the Class Period, the Winstar Defendants also denied that Winstar would utilize financing provided by Lucent to fund the Company's payment of interest to bondholders. As The Wall Street Journal reported on April 16, 2001, those representations were materially misleading because, in the Lucent Complaint, Winstar acknowledges that "its inability to make [the April 16, 2001] interest payment was directly caused by Lucent's refusal to make further loans to the company."

110 The falsity of the Winstar Defendants' representations concerning the Company's liquidity and ability to fund the Winstar Defendants' expansion plans is further demonstrated by the steps taken by Lucent to unload Winstar debt at bargain prices as early as June of 2000. At that point, Winstar retained Donaldson Lufkin & Jenrette and Bear Stearns to attempt to sell some of the loans that Lucent had extended to Winstar. Lucent's grave concerns with Winstar's ability to pay those loans was reflected by Lucent's willingness to sell those loans at less than 90 cents on the dollar. Because Winstar was aware that any such heavily discounted sale would be interpreted by investors as reflecting Lucent's lack of confidence in Winstar, the Company insisted that Lucent halt its efforts to sell the loans. Nevertheless, Lucent's expressed willingness to sell the debt at a sharp discount demonstrated that Lucent doubted Winstar's ability to repay its debts.

111 The Winstar Defendants' positive representations concerning the Company's liquidity are also belied by the Company's inability to pay its financial obligations - even for critical services - in a timely manner long before it filed its bankruptcy petition. For example, in a memorandum filed in the Winstar Bankruptcy, Winstar creditor Affiliated Computer Services, Inc. ("ACS") stated that Winstar was not complying with its obligation to pay ACS for providing "staffing for billing on long distance customer calls, local customer calls and call collection and mediation at Winstar's Rockville, Maryland and Herndon, Virginia facilities.

112 In particular, ACS stated:

Winstar is not complying with certain obligations under [its agreement with ACS] and, in fact, has been in material breach since well before the Petition Date. Winstar consistently failed to make timely payments to ACS pursuant to [the agreement]. Under the [agreement], Winstar was required to make payments to ACS on terms of net 30. Winstar has failed to remit payment since November 2000, and, in fact, as of the Petition Date, Winstar was indebted to ACS in the amount of $2,457,431.

E. Defendants Actively Fostered And Took Advantage Of A Business Culture With No Internal Controls

113 By March 10, 2000, the Company and Grant Thornton had identified numerous internal control deficiencies that served to undermine most of the Company's reported financial results, as described above, materially overstating assets and financial performance and serving to facilitate widespread internal corruption that allowed corporate officers to profit from misreported financial figures.

114 In an Affidavit submitted by Grant Thornton partner Gary Goldman in the Winstar Bankruptcy, Goldman states that Grant Thornton billed Winstar $5.13 million for accounting services and related expenses during 2000.

115 Grant Thornton prepared an Independent Auditors Report letter dated February 10, 2000, quoted in full below. The date of the report indicates that Grant Thornton's audit of Winstar was completed by that date. Among the dozens of accounting problems identified by Grant Thornton in the course of its audits of the Company's financial statements, financial accounting functions and internal controls were: (1) Numerous deficiencies relating to the identification and location of assets, such that Winstar could not identify where its assets

were located or even whether assets that had been paid for were received; (2) Inadequate documentation concerning the location and requisition of inventory and computer hardware; (3) Inadequate internal controls over asset purchasing, allowing decentralized requisition and procurement procedures, effectively allowing the Company to purchase assets without centralized accounting for the assets; (4) Inadequate bill-paying and invoicing procedures, effectively allowing bills to be paid from multiple departments; (5) Inadequate financial management software, undermining the ability of management to adequately plan and forecast financial requirements and performance, and undermining all business plans that formed the basis for internally generated and publicly shared financial projections; (6) No control over payments to vendors that might prevent payments to vendors that failed to perform services they billed (denoted in an internal Grant Thornton report with "time bomb" symbol); (7) No procedures to confirm the receipt of equipment purchased by the Company; (8) According to Grant Thornton, "there is no process or system to support the continuous tracking of systems assets after they have been deployed"; (9) According to Grant Thornton, "There is no standard cut-off point for determining when software projects are in development, released for in service, or abandoned. This affects whether it is considered an expense or a capital item"; (10) People leaving Winstar office locations were not required to have a building pass for the removal of Winstar property; (11) User ID's, logons and workstations are not retired or reassigned when an employee or contractor leaves Winstar; (12) Purchase orders are not properly matched with receivers and invoices; and (13) Duplicate invoices sent to multiple departments would result in overpayments to vendors.

116 These problems are outlined in lengthy documents prepared by Grant Thornton, including a 114-page study conducted by Grant Thornton and published by it in conjunction with Winstar's Internal Audit Department.

117 In recognition of the virtual total absence of controls over the Company's finances, assets, and procedures, senior management - including each member of the Company's senior management team named as a defendant herein - engaged in covert practices designed to benefit themselves at the expense of the Company and its investors. For example, defendants Rouhana and Kantor knowingly allowed numerous related parties to utilize Company assets without paying for them. Other executives developed and fostered an internal system of entering false customer information into the Company's customer databases, suggesting that the Company had more customers and had made more sales than in fact it actually had, and encouraging the payment of bribes - in the form of cash - to data entry personnel to look the other way. At the same time, management encouraged sales personnel to fabricate customer information, by agreeing to pay commissions on such fabricated sales. Employees who challenged these improper practices were ostracized.

118 Throughout the Class Period, the Company was also experiencing numerous problems with virtually all of its larger customers. Customer problems arose from such situations as erroneously drawn engineering drawings for hubs and other sites (according to an internal Grant Thornton report, 80% of engineering drawings contained errors, and "because there [are] no engineering walkthroughs, they usually do not find out that the drawings are inaccurate until customers are put on line.") Likewise, internal failures to communicate about technology and software upgrades caused the engineering department to routinely provide erroneous specifications to customers.

119 Notwithstanding the extraordinary problems being experienced by Winstar, Defendants actively covered-up any hint of accounting problems and actively promoted the Company as experiencing strong growth and improved financial controls.

120 Also taking advantage of the virtual total absence of internal controls, throughout the Class Period, the Winstar Defendants routinely encouraged or tacitly allowed sales personnel to engage in overt sales falsification, in a deliberate effort to overstate sales. The Winstar Defendants also wittingly abused a system-wide lack of internal controls that existed within the Company and encouraged the direct participation of sales personnel, encouraging sales personnel to take advantage of the lack of internal controls.

121 In particular, sales personnel routinely entered false sales information into the Company's computer systems, generating impressive sales figures and allowing the Company to report improving sales figures to the investing public, while the Winstar Defendants were aware that large numbers of such sales were in fact not actual sales and the data relating to the sales was often not entered into a separate computer system used to assign and schedule provisioning and installation. As a result, sales personnel could and did enter false sales into one computer system. That then allowed the sales personnel to generate commissions for themselves, yet none of the elements necessary for converting a sale to a revenue-generator were completed. Company employees who expressed disapproval with this system and the rife abuse that occurred under it were met with indifference, and the Company undertook no efforts to alter or correct these improper business practices.

122 These practices occurred throughout the Class Period in every significant sales office the Company maintained, and was especially rampant in the Company's Dallas, New York Phoenix, and Seattle offices, where hundreds of thousands of dollars in fraudulently obtained commissions were paid to sales representatives on millions of dollars' of false sales. Although such activities were frequently brought to the attention of the Company's senior management, no action was ever taken to correct it. As a result of the Winstar Defendants' tacit and knowing acceptance of these practices, eventually, more than half of all orders were either cancelled or deactivated within a very short period of time. As reflected on internal company documents available to the Winstar Defendants, and updated on a regular and rolling basis, in the period from March 2000 through February 2001, the Company reported orders of 20,521, of which 13,214 were cancelled. Of the net orders of 7,307, an estimated 7,227 were installed, 270 were de-installed, suggesting that the Company had net installations from orders for that period of 5,957. This suggests that 64.39% of orders were cancelled, and that only approximately 35.61% of orders resulted in actual deals for the Company. While the Winstar Defendants routinely received summary and detailed order and flash reports on at least a monthly basis that showed the number of new orders and the rising cancellations and de-installations, the Company routinely paid commissions to sales personnel on these false sales, further encouraging the widespread use of these false sales practices.

VI. THE MATERIALLY MISLEADING REPRESENTATIONS AND OMISSIONS MADE BY THE WINSTAR DEFENDANTS AND GRANT THORNTON

A. The Winstar Defendants' Materially False And Misleading Statements In The 1999 10-K And 1999 Annual Report

123 The Class Period commences on March 10, 2000, the date on which the Winstar Defendants filed with the SEC the Company's Annual Report on Form 10-K for the 1999 fiscal year. For the fiscal year ended December 31, 1999, the Company reported total revenues of $445.6 million, compared to revenues of $244.4 million a year earlier. The Winstar Defendants also reported that those revenues consisted of $234.80 million in core services revenue, $121.27 million in core enhanced network products revenue, $27.69 million in other communications services revenue, and $61.88 million in information services revenue. In addition, the Winstar Defendants and Grant Thornton reported that Winstar had produced a net loss for the year of $699.77 million.

124 In the financial statements included as part of the 10-K, the Winstar Defendants and Grant Thornton characterized the sources of Winstar's revenue as follows:

We classify revenues as communications revenues and information services revenues. Communications revenues are divided into two categories: core communications and other communications services.

Core communications revenues primarily include revenues derived from: local and long distance voice services, Internet connectivity, capacity and equipment sales; data transmission services; web hosting, web design and development services; and professional and enhanced services, including network design and implementation, equipment selection, procurement and installation. Sales of network capacity and telecommunications equipment through our enhanced service provider channel are classified as enhanced network products revenue.

Other communications services revenues are those derived from a portion of an acquired long distance customer base located in markets which we do not have current plans to serve with our fixed wireless services.

We also develop and distribute information content and provide related services through traditional media, such as television, video, cable and radio, and over the Internet.

125 Moreover, in describing the "principal factors that drive" the Company's revenues, the Winstar Defendants stated:

Core Services

Revenues from local and long distance voice services are driven primarily by the number of customer lines installed and in service. Customers are generally billed a flat monthly fee and/or a per-minute usage charge. Data services are generally billed at a flat monthly rate for capacity ordered. E-commerce and advertising revenues are billed when the ad runs or the transaction occurs. Professional services such as network design, network integration, installation and maintenance are billed on a project or a time and materials basis. Revenues from our enhanced service provider channel include sales of network capacity under long-term indefeasible rights of use to our long-haul or local networks, as well as the sale of private network services. This revenue channel also includes sales of network design, collocation services and equipment used to provide our core communication services, which are billed when the service is performed or the equipment is shipped. Sales of network capacity and sales of equipment from our enhanced service provider channel are generally classified as enhanced network products revenue. Core communication revenue growth depends upon our addition of new customers in existing markets, our sale of bundled services, our expansion into new markets and our introduction of new services. We expect our core revenues to increase as we expand our network and as we add more services to it.

126 Elsewhere in the Form 10-K, the Winstar Defendants stated:

Revenues from core services and enhanced network products increased by $214.6, or 151.7%, to $356.1 million for the year ended December 31, 1999, from $141.5 million for the year ended December 31, 1998. The revenue growth was primarily attributable to continued customer growth driven by growth in existing markets, the increase of domestic markets from 30 to 45, and the expansion of our broadband data application services and enhanced service provider offerings, which include our provision of end-to-end products and services to our customers. These include Internet connectivity, data transport, network assets and network integration services. The total number of our customers increased to approximately 23,300 businesses at December 31, 1999.

In 1998, we primarily sold voice services to small and medium businesses. We continue to experience significant success selling these services to this customer base, as evidenced by increasing revenue from this group of customers, the increase in the total number of our customers and in the percentage of our customers who purchase more than one service. Moreover, the average revenue we derive from each customer has continued to increase and we have been successful penetrating buildings on our network.

We have also been successful selling data and voice-related products and services to both small and medium businesses and to larger accounts. We attribute this success to the continued growth of our network through the installation of additional local bandwidth, data and voice switching infrastructure and the addition of our local-and long-haul fiber. We have begun to realize increased revenue especially from the sale of these data-related products and services, including end-to-end broadband connectivity, equipment and network deployment solutions to our larger customers.

We are also continuing to see an increasing demand for data related enhanced communications solutions, and since the end of 1998 have sold such services to many large account customers, including communications industry customers such as AboveNet Communications, Cignal Global Communications, Lucent Technologies, Mindspring Enterprises, VoCall Communications, Wam!Net Inc. and Williams Communications.

127. The Form 10-K also flatly, and falsely stated, "No one customer comprises more than 10% of our consolidated revenues." In fact, Winstar has acknowledged in the Lucent Complaint and the Ackerman Affidavit that well in excess of $130 million of the Company's 1999 revenue, and perhaps a significantly higher portion of those revenues, was derived from transactions with Lucent. Even at the minimum level of $130 million, the Lucent transactions constituted in excess of 29% of the revenue derived by Winstar during 1999.

128. The Winstar Defendants' descriptions of the sources of the Company's revenues were materially misleading because of the Winstar Defendants' failure to disclose the facts alleged in section V of this Complaint. In particular, the Winstar Defendants' failure to disclose that 29% or more of the Company's 1999 revenue was attributable to the services that Winstar supposedly performed for Lucent in designing and building-out Winstar's own broadband network rendered their representations concerning the sources of the Company's revenues materially misleading.

129. The Winstar Defendants and Grant Thornton also emphasized in the Form 10-K that the Company had produced a negative "EBITDA," i.e., earnings before interest, taxes, depreciation and amortization, during 1999 of $297.3 million. Throughout the Class Period, the Winstar Defendants emphasized that the purported improvement of the EBITDA demonstrated the success of Winstar's business plan and their eventual ability to fund the Company's operations.

130. For the reasons outlined in section V of this Complaint, the foregoing representations concerning Winstar's financial results were materially false and misleading at the time they were made. In addition, as is specifically alleged in section V of this Complaint, the financial statements included in the 1999 10-K were materially misleading because the Winstar Defendants and Grant Thornton failed to disclose that at least 29%, and likely a significantly higher percentage, of the "revenue" reported by the Winstar Defendants in the financial statements was generated through Winstar's purported sale of services to Lucent that related exclusively to the Company's work in designing and building-out its own network. Those "revenues" should not have been recorded by the Winstar Defendants because they were not the result of transactions with any financial substance, but rather were designed to inflate Winstar's revenues.

131. As is true of every publicly-trade company, Winstar was required to have the financial statements that it included as part of its Form 10-K audited by an firm of certified public accountants - here Defendant Grant Thornton. Grant Thornton issued the following Independent Auditor's Report, dated February 10, 2000, concerning those financial statements:

We have audited the accompanying consolidated balance sheets of Winstar Communications, Inc. and Subsidiaries as of December 31, 1999 and 1998, and the related consolidated statements of operations, stockholders' deficit, and cash flows for each of the three years in the period ended December 31, 1999. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Winstar Communications, Inc. and Subsidiaries as of December 31, 1999 and 1998 and the consolidated results of their operations and their consolidated cash flows for each of the three years in the period ended December 31, 1999 in conformity with accounting principles generally accepted in the United States.

132. Grant Thornton's statement that the Company's financial statements were prepared in accordance with GAAP was materially false and misleading for the same reasons that the Winstar Defendants' representations concerning the Company's 1999 financial statements were false and misleading.

133. Plaintiffs and the members of the Class, like all investors, placed heavy reliance upon Grant Thornton's certification of Winstar's 1999 financial statements in deciding that the Company was an attractive investment.

134. Indeed, had Grant Thornton refused to issue a "clean" audit opinion concerning Winstar's financial statements, trading in the Company's securities would not have occurred, and, therefore, Plaintiffs and the members of the Class would not have purchased those securities. Furthermore, had Grant Thornton insisted, as it was obligated to do, that the Winstar Defendants adjust the Company's financial statements to accurately reflect Winstar's financial results and to fully disclose all material facts concerning those results, Winstar's securities would not have traded at the inflated prices that prevailed throughout the Class Period.

135. The Company's Annual Report for 1999, which the Winstar Defendants disseminated to investors on or about March 10, 2000, also included a number of materially misleading statements concerning the Company's financial results, operations and prospects.

136. In particular, the Annual Report included the Company's audited 1999 financial statements - including Grant Thornton's clean Independent Auditor's Report. As a result, the Annual Report repeated each of the material misrepresentations alleged in 122-130.

137. The Winstar Defendants also made statements in the Annual Report in which they falsely characterized Winstar as a growing and

highly successful company with a sustainable business plan. For example, in a letter to shareholders, Defendant Rouhana stated:

Our timing could not be better. We deliver the network, applications and services that enable a growing number of companies to use the Internet as an effective business tool. Our integrated approach to delivering broadband services makes Winstar's network a strategic tool, which enables our customers to manage their businesses better.

We have a business model that is strong and sustainable, and a superior ability to continue to implement our business strategy day in and day out. Winstar moves into 2000 ready to capitalize on a tremendous global market opportunity: The growing international demand for Winstar's winning array of productivity solutions. (Emphasis added.)

138. Similarly, in a letter to shareholders signed by Defendant Kantor, he stated, "The keys to Winstar's future progress are in place, and all the metrics are headed in the right direction."

139. Contrary to the highly positive representations made by Rouhana and Kantor, by March of 2000, Winstar was experiencing extraordinary difficulty in its effort to implement its business plan. As is specifically alleged in section V of this Complaint, while Winstar had wed itself to Lucent to design, build, provide equipment for and finance Winstar's broadband network, throughout the Class Period, Lucent was not fulfilling its contractual obligations to Winstar. Furthermore, as Plaintiffs allege in section V of this Complaint, the growth of the Company's revenue reported by the Winstar Defendants resulted primarily from the Company's bogus transactions with Lucent, rather than any market demand for Winstar's services.

140. Each of the foregoing misleading statements set forth in the 1999 Form 10-K or 1999 Annual Report concerning the Company's financial performance and operations had the effect of inflating the prices of Winstar's securities or maintaining Winstar's securities at prices those securities would not have traded had the truth concerning the Company's operations been disclosed to investors. Had the Winstar Defendants or Grant Thornton disclosed those adverse facts - as they were obligated to do - Plaintiffs either would not have purchased Winstar securities at all or would have purchased those securities at prices far lower than the prices that prevailed during the Class Period.

B. The Winstar Defendants' Materially Misleading Representations Concerning The Company's First Quarter 2000 Financial Results

141. On May 4, 2000, the Winstar Defendants announced the Company's financial results for the first quarter of fiscal year 2000 in a press release headlined "Winstar Results Continue Sharp Improvement."

142. In that press release, the Winstar Defendants reported total revenue for the quarter of $162.8 million, a purported 84.8% increase over the year-earlier figure. The Winstar Defendants also stated that the Company had generated "broadband services" revenue of $133.46 million and other revenue of $29.33 million for the quarter.

143. In addition, the Winstar Defendants stated in the press release that Winstar had produced a "sharp improvement in gross margin, which rose to an all-time high of 40.7% in the first quarter" of fiscal 2000, compared to 22.9% in the same quarter a year earlier. For the quarter, the Winstar Defendants reported that the Company generated an EBITDA loss of $56.6 million, a reported $23.1 million improvement over the first quarter of fiscal 1999. Furthermore, the Winstar Defendants claimed that the net loss posted by the Company during the quarter was $176 million, or $2.06 per share.

144. Each of those representations concerning the Company's purported financial results was materially misleading for the reasons specifically alleged in section V of this Complaint. Furthermore, those representations were materially misleading because the Winstar Defendants failed to disclose the highly material fact that 20% or more of the "revenues" purportedly generated by the Company during the quarter related to services supposedly performed by Winstar for Lucent in connection with the design and build-out of the Company's own network. Those "revenues" should not have been recorded by the Winstar Defendants because they were not the result of transactions with any financial substance, but rather were designed to inflate Winstar's revenues.

145. The press release also quoted Rouhana as stating, "Strong revenue growth and sharply improving margins have enabled us to deliver impressive results not just today, but for several quarters now."

146. That representation was materially misleading because, among other things: (a) as is specifically alleged in Section V of this Complaint, the revenue "growth" reported by the Winstar Defendants was the result of the Company's bogus transactions with Lucent; (b) the Winstar Defendants failed to disclose that payments purportedly made by Lucent for Winstar's work in designing and building-out the Company's own network represented 20% or more of the revenues reported by Winstar during the quarter; and (c) there was nothing "impressive" about the Company's financial results because they were the product of the accounting manipulations specifically alleged herein.

147. On May 5, 2000, Rouhana followed the Company's highly positive press release with yet more upbeat statements in an interview that he conducted with CNBC. When questioned when Winstar would begin to produce profitable operations, Rouhana stated:

We're very close now. The beginning of next year we'll go EBITDA positive, which is the measurement people look at in our industry. We've had 12 straight quarters of double-digit revenue growth, five straight quarters of margin improvement, three straight quarters of EBITDA loss reduction, so we're in a sort of an inexorable march toward EBITDA positive early next year.

148. Those representations concerning the Company's purported "inexorable march" to a positive EBITDA were materially misleading for the reasons specifically alleged in section V of this Complaint. These materially false and misleading statements were not accompanied by any cautionary or purportedly cautionary statements.

149. The Winstar Defendants made a number of additional positive representations during the course of a conference call with securities analysts and institutional investors held on May 5, 2000 to discuss the Company's quarterly results. During that call, one of the Winstar Defendants stated that the Company would meet the revenue, EBITDA and net income numbers that the Winstar Defendants had previously projected to the market for 2000 and that the Company's broadband network would grow five-fold in the ensuing 18 months.

150. Those positive statements concerning the Company's operations were materially misleading for the reasons alleged in section V of this Complaint.

151. On May 15, 2000, the Winstar Defendants filed with the SEC the Company's Form 10-Q quarterly report for the first quarter of 2000. The 10-Q was signed by defendant Uhl. In that document, the Winstar Defendants repeated the representations that they had earlier made concerning the Company's financial results for the first quarter.

152. In particular, the Winstar Defendants stated that Winstar had produced revenue of $162.79 million for the quarter, including broadband services revenue of $133.46 million. The Winstar Defendants also claimed that the Company had generated a net loss of $176 million, or $2.06 per share, during the quarter.

153. As is specifically alleged above, each of the foregoing representations concerning the Company's financial results for the first quarter was materially false and misleading at the time it was made.

154. In the 10-Q, the Winstar Defendants also stated:

The financial statements [set forth in the 10-Q] contain all adjustments (consisting only of normal recurring accrual adjustments) which, in our opinion, are necessary to fairly present our financial position as of March 31, 2000, the statements of operations for the three months ended March 31, 2000 and 1999, the statements of cash flows for the three months ended March 31, 2000 and 1999, and the statement of stockholders' equity for the three months ended March 31, 2000.

155. Contrary to those representations, the financial statements included in the Form 10-Q did not accurately set forth the Company's financial results and financial position. Rather, for the reasons specifically alleged in section V of this Complaint, those financial statements, and thus the Winstar Defendants' representation concerning their accuracy, were materially misleading.

156. In discussing the Company's liquidity and available financing in the first quarter Form 10-Q, the Winstar Defendants also stated, "We anticipate, based on our business plan and certain assumptions, that our existing financial resources will be sufficient to fund our planned operations and capital requirements through 2001."

157. As Plaintiffs allege in detail in section V of this Complaint, that representation was materially misleading at the time it was made because Winstar's ability to continue to fund its operations was dependent, throughout the Class Period, upon Lucent's willingness to continue to engage in the unlawful accounting practices designed to inflate the revenues of Winstar and Lucent that are described above.

158. The Winstar Defendants also provided investors with a misleading description of the sources of the Company's revenues in the first quarter Form 10-Q. Specifically, in describing the sources of the Company's revenue, the Winstar Defendants stated:

We classify revenue into two categories: broadband services and other.

Broadband services revenue primarily includes revenue derived from: Internet connectivity; data transmission services; web hosting; network capacity sales; local and long distance voice services; web design and development services; professional and enhanced services, including network design and implementation, equipment selection, procurement, sales and installation; and revenues derived from the development and distribution of information content and related services over the Internet.

We also develop and distribute information content through traditional media, such as television, video, cable and radio. These revenues and revenues from sales of broadcast and programming rights and licenses are classified as other revenue. Other revenues also include those derived from a portion of an acquired long distance customer base located in markets which we do not have current plans to serve with our broadband network.

159. In describing the Company's revenue-generating business segments, the Winstar Defendants also stated:

Our operating segments represent business units that offer different products and serve different markets. The Broadband Services segment derives its revenues by offering its customers a variety of individual and bundled services. The Traditional Media Services segment derives its revenues by marketing and distributing information content, licenses and services in traditional markets, such as television, video, cable and radio. Our Other Telecommunications Services segment derives its revenue from a portion of an acquired long distance customer base located in markets which we do not have current plans to serve with our broadband network. Substantially all of our revenue is attributable to customers in the United States, and our assets are predominately located in the United States.

160. Furthermore, the Winstar Defendants described the Company's broadband services revenue as follows:

Broadband Services Revenue

Revenue from broadband services increased by $64.9 million, or 94.6%, to $133.5 million for the three months ended March 31, 2000, from $68.6 million for the three months ended March 31, 1999. We experienced continued growth in all types of broadband services revenue, driven principally by growth in the number of addressable customers, the number of customers ordering multiple services, and the addition of a number of new commercial contracts. Revenue from large account solutions was $61.0 million for the three months ended March 31, 2000, compared to $15.9 million for the three months ended March 31, 1999. We attribute this success to the continued growth of our network through the installation of additional local bandwidth, data and voice switching infrastructure and the addition of our local and long-haul fiber. We are continuing to realize increased revenue especially from the sale of these data-related products and services, including end-to-end broadband connectivity, equipment and network deployment solutions to our larger customers. We have now signed contracts totaling over $1.2 billion from our large account customers (excluding the federal government). We expect to recognize approximately $140.0 million of this amount as revenue over the next 12 months.

161. The foregoing descriptions of the sources of the Company's revenues were materially misleading because of the Winstar Defendants' failure to disclose the facts alleged in section V of this Complaint. The Winstar Defendants' failure to disclose that 20% or more of the Company's quarterly revenue was attributable to the services that Winstar supposedly performed for Lucent in designing and building-out the Winstar broadband network rendered their representations concerning the sources of the Company's revenues materially misleading.

162. Each of the foregoing misrepresentations and omissions made by the Winstar Defendants concerning the Company's first quarter 2000 financial results had the effect of inflating the prices of Winstar securities or of maintaining the prices of those securities at levels that would not have prevailed had the Winstar Defendants disclosed the truth concerning Winstar's operations - as they were obligated to do. Had the Winstar Defendants made such disclosures, Plaintiffs and the members of the Class would not have purchased Winstar securities or, alternatively, would not have purchased those securities at the inflated prices that prevailed during the Class Period. C. The Winstar Defendants' Materially Misleading Representations Concerning The Company's Second Quarter 2000 Financial Results And Operations

163. On August 2, 2000, the Winstar Defendants issued a press release announcing the Company's financial results for the second quarter of fiscal year 2000.

164. In that press release, the Winstar Defendants reported that the Company had generated total revenue of $176.3 million for the quarter ended June 30, 2000, a purported 82.7% increase over the year-ago quarter. The Winstar Defendants also stated that the Company had produced broadband services revenue of $152.8 million and a net loss of $343.57 million, or $3.84 per share.

165. In announcing the Company's results, the Winstar Defendants also stated that Winstar's "stronger than expected revenue performance was augmented by continued sharp improvement in gross margin, which rose to an all-time high of 44.1% in the second quarter," compared to claimed gross margins of 40.7% in the prior quarter, 24.0% in the year-ago quarter, and 10.5% as recently as six quarters earlier.

166. The Winstar Defendants also stated that "[t]he company expects gross margins to continue to improve throughout the balance of the year" and that "[d]riven largely by strong revenue growth and higher margins, Winstar narrowed its EBITDA loss for the quarter to $44.8 million, a $38.3 million improvement from the year-ago quarter, and an $11.8 million sequential improvement from the prior quarter." In addition, the Winstar Defendants emphasized, "This is the company's fourth consecutive quarter of strong improvement since posting its peak EBITDA loss in the second quarter of 1999."

167. As is specifically alleged in section V of this Complaint, all of the foregoing representations concerning the Company's second quarter 2000 financial results were materially misleading because the Company's revenues, margins, EBITDA and net income were materially inflated as a result of the accounting improprieties in which the Winstar Defendants engaged with the assistance of Lucent. Additionally, the Winstar Defendants' representations concerning the Company's revenues were materially misleading because they failed to disclose that 20% or more of those purported "revenues" were the product of the Company's improper arrangement of billing Lucent for services supposedly provided to design and build-out the Company's own broadband network.

168. Commenting on the Company's results in the second quarter press release, Rouhana also misled investors regarding the reasons for Winstar's purported success. Specifically, Rouhana stated: Our strong growth continues to be driven by the emergence of a high-capacity broadband network that is both increasingly available to customers, and increasingly enriched by services that set it apart. As we made clear at our recent analyst meeting, our strategic focus is the continued expansion of both our network and our unique product set - and the execution of that strategy is apparent in our results. Continued execution will be even more important in the quarters ahead, as we ramp up for the high-growth stage of our development.

169. Contrary to those statements, the Company was not experiencing meaningful growth in its revenue. Rather, as is specifically alleged in section V of this Complaint, the reason for the purported "growth" that Winstar was experiencing was the Winstar Defendants' improper arrangements with Lucent to inflate the Company's revenues. Moreover, as fiscal 2000 progressed, it was increasingly obvious to the Winstar Defendants that Lucent was no longer willing or able to "pay" Winstar for the bogus "services" purportedly performed by Winstar for Lucent. As a result, Winstar's continued viability as a company was severely threatened by the time the Winstar Defendants made the foregoing positive statements.

170. Defendant Kantor also made highly positive representations concerning the Company's financial performance in the press release. Specifically, Kantor stated:

Strong blocking and tackling, combined with solid overall execution, has enabled us to deliver another quarter of steadily improving financials. With both network expansion and product development on track, we continue to broaden and enrich the market for our sales force. Growing sales momentum has enabled us to again deliver strong revenue growth despite focusing sales and installation activity almost entirely on our own network. This disciplined approach resulted in on-net lines added during the quarter surging to an all-time high of 73%, contributing significantly to our increased margins and strong financial performance.

171. Those representations were materially misleading at the time they were made because, among other things: (a) as is alleged in section V of this Complaint, the financial results reported by the Winstar Defendants for the second quarter were materially overstated; (b) the Winstar Defendants' characterizations of the reasons for the purported "growth" in Winstar's revenue and the improvement in its other financial measures were materially misleading as a result of the Winstar Defendants' failure to disclose that those improvements resulted from the bogus payments supposedly made by Lucent to Winstar for services performed by Winstar in designing and building-out its own broadband network; and (c) Winstar was experiencing limited demand for its products and services, other than the artificial demand resulting from the Winstar Defendants' agreement with Lucent to inflate both companies' reported revenue through the fraudulent activity described in section V of this Complaint.

172. The Winstar Defendants repeated the false statements made in the August 2, 2000 second quarter press release when they filed Winstar's Form 10-Q for the second quarter with the SEC on or about August 14, 2000. That Form 10-Q was signed by defendant Uhl.

173. In that Form 10-Q, the Winstar Defendants represented that, during the second quarter: (a) Winstar had generated broadband services revenue of $152.82 million, other revenue of $23.47 million and total revenue of $176.29 million; and (b) the Company had produced a net loss of $343.57 million, or $3.84 per share. In another portion of the Form 10-Q, the Winstar Defendants stated that, during the second quarter, the Company produced broadband services revenue of $152.82 million, traditional media services revenue of $19.43 million and other telecommunications services revenue of $4.04 million.

174. The Winstar Defendants also stated:

The financial statements contain all adjustments (consisting only of normal recurring accrual adjustments) which, in our opinion, are necessary to fairly present our financial position as of June 30, 2000, the statements of operations for the three and six months ended June 30, 2000 and 1999, the statements of cash flows for the six months ended June 30, 2000 and 1999, and the statement of stockholders' equity (deficit) for the six months ended June 30, 2000.

175. Those representations concerning the financial results generated by the Company during the second quarter of 2000 were materially false and misleading for the reasons alleged in section V of this Complaint.

176. The Form 10-Q also delivered the following materially misleading description of the sources of Winstar's revenues:

We classify revenue into two categories: broadband services and other.

Broadband services revenue primarily includes revenue derived from: Internet connectivity; data transmission services; web hosting; network capacity sales; local and long distance voice services; web design and development services; professional and enhanced services, including network design and implementation, equipment selection, procurement, sales and installation; and revenues derived from the development and distribution of information content and related services over the Internet.

We also develop and distribute information content through traditional media, such as television, video, cable and radio. These revenues and revenues from sales of broadcast and programming rights and licenses are classified as other revenue. Other revenues also include those derived from a portion of an acquired long distance customer base located in markets which we do not have current plans to serve with our broadband network.

177. Elsewhere in the Form 10-Q, the Winstar Defendants stated:

Broadband services revenue growth depends upon our addition of new customers in existing markets, our sale of bundled services, our expansion into new markets, our introduction of new services and continued growth in the large account solutions business. We expect our broadband services revenue to increase as we expand our network and add more services to it.

178. Similarly, in describing the business "segments" in which the Company operated, the Winstar Defendants stated:

Our operating segments represent business units that offer different products and serve different markets. The Broadband Services segment derives its revenues by offering its customers a variety of individual and bundled services. The Traditional Media Services segment derives its revenues by marketing and distributing information content, licenses and services in traditional markets, such as television, video, cable and radio. Our Other Telecommunications Services segment derives its revenue from a portion of an acquired long distance customer base located in markets which we do not have current plans to serve with our broadband network.

179. In discussing the Company's broadband services revenue, the Winstar Defendants also stated: Revenue from broadband services increased by $75.9 million, or 98.7%, to $152.8 million for the three months ended June 30, 2000, from $76.9 million for the three

months ended June 30, 1999. We experienced continued growth in all types of broadband services revenue, driven principally by growth in the number of addressable customers, the number of customers ordering multiple services, and the addition of a number of new commercial contracts. Revenue from large account solutions was $72.6 million for the three months ended June 30, 2000, compared to $20.1 million for the three months ended June 30, 1999. We attribute this success to the continued growth of our network through the installation of additional local bandwidth, data and voice switching infrastructure and the addition of our local and long-haul fiber. We are continuing to realize increased revenue especially from the sale of these data-related products and services, including end-to-end broadband connectivity, equipment and network deployment solutions to our larger customers.

180. Those descriptions of the sources of the Company's revenues were materially misleading because of the Winstar Defendants' failure to disclose the facts alleged in section V of this Complaint. In particular, the Winstar Defendants' failure to disclose that 20% or more of the Company's revenue was attributable to the services that Winstar supposedly performed for Lucent in designing and building-out the Winstar broadband network rendered their representations concerning the sources of the Company's revenues materially misleading.

181. In discussing the Company's liquidity and available financing in the Form 10-Q, the Winstar Defendants also stated, "We anticipate, based on our business plan and certain assumptions, that our existing financial resources will be sufficient to fund our planned operations and capital requirements through 2001. These financial resources include the $2 billion Lucent credit facility."

182. As Plaintiffs allege in detail in section V of this Complaint, that representation was materially misleading at the time it was made because Winstar's ability to continue to fund its operations was dependent, throughout the Class Period, upon Lucent's willingness to continue to engage in the unlawful accounting practices designed to inflate the revenue of Lucent and Winstar described therein. Furthermore, by the time the second quarter Form 10-Q was filed by the Winstar Defendants, Lucent was expressing strong reservations to the Winstar Defendants concerning its willingness to continue to fund the Company's operations, particularly through the type of fraudulent transactions described in section V of this Complaint. Accordingly, the Winstar Defendants' failure to disclose that the Lucent Facility would not be available to fund the Company's operations rendered their description of the Company's liquidity materially false and misleading.

183. All of the foregoing misleading statements concerning the Company's second quarter financial results and financial position had the effect of either: (a) inflating the market prices of Winstar securities; or (b) maintaining the market prices of those securities at levels that would not have prevailed had the Winstar Defendants made accurate disclosures concerning the Company, its operations and its prospects. Accordingly, all of those misleading statements had the effect of damaging those members of the Class who purchased Winstar securities after the Winstar Defendants made those representations.

D. The Winstar Defendants' Materially Misleading Representations Concerning The Company's Third Quarter 2000 Financial Results And Operations

184. On September 15, 2000, key members of Winstar's senior management team, including the Winstar Defendants, held a conference called the "Winstar General Business Q3 Leadership Meeting" in which members of the Company's management team discussed in detail the Company's "revenue challenges." Among other things, the Winstar Defendants discussed in detail the fact that the Company was falling significantly short of its business plans and revenue targets for the quarter. The Winstar Defendants' discussions included reviewing and discussing slides or handouts describing the Company's planned revenues for the third quarter and which showed that the Company's actual revenues at that time were estimated to be less than what the Company planned. Based on this meeting, it was clear to the Winstar Defendants that the Company's business plans were failing to produce revenue even remotely in line with what the Winstar Defendants had planned, and that the Company was facing significant "revenue challenges."

185. On November 8, 2000, the Winstar Defendants issued a press release announcing the Company's financial results for the third quarter of fiscal 2000, the quarterly period ended September 30, 2000.

186. In that press release, the Winstar Defendants reported that, during the third quarter, the Company had generated total revenue of $195.1 million, a supposed 63.3% increase over the year-ago quarter. The Winstar Defendants further reported that the Company had produced a net loss of $227.4 million, or $2.50 per share, $0.04 better than consensus analyst earnings expectations. Additionally, the Winstar Defendants stated that the Company's broadband services revenue for the quarter rose to $175.9 million, up 80.2% from the prior year and up 15.1% from the previous quarter.

187. In reporting those results, the Winstar Defendants stated that "stronger than expected revenue performance was augmented by continued sharp improvement in gross margin, which rose to an all-time high of 47.3% in the third quarter" which compared to claimed gross margins of 44.1% in the prior quarter, 30.1% a year ago, and 10.5% seven quarters earlier. Furthermore, the Winstar Defendants stated:

The company expects gross margin to continue to improve throughout the balance of the year and beyond. Driven largely by strong revenue growth and margin improvement, Winstar narrowed its EBITDA loss for the quarter to $32.0 million, a $40.6 million improvement from the year-ago quarter, and a $12.8 million improvement from the prior quarter. This is the company's fifth consecutive quarter of strong improvement since posting its peak EBITDA loss in the second quarter of 1999. Winstar expects its EBITDA losses to continue to decline until it reaches EBITDA breakeven, which is expected to occur during the first half of 2001. The company's $12.8 million improvement in EBITDA for the quarter was achieved despite a discretionary investment of approximately $6.5 million in sales and marketing initiatives....

188. Each of the foregoing representations concerning the financial results posted by the Company during the third quarter of 2000 was

materially misleading for the reasons outlined in section V of this Complaint. Contrary to the Winstar Defendants' representations, Winstar was not a growing Company well on its way to profitability. Rather, the Company was unable to fund its operations without engaging in the accounting manipulations alleged herein.

189. The third quarter press release contained additional misrepresentations by which the Winstar Defendants attempted to create the false impression that the Company was quickly moving towards profitability. The press release quoted Defendant Rouhana as stating: Our strong growth and steadily improving performance are driven by discipline and execution. Implementation of our strategy to build a widely available broadband network and make it useful to customers has enabled us to deliver industry-leading on-net performance. Successful execution of these highly focused initiatives has dramatically improved our financial results over the last six quarters.

190. The third quarter press release also quoted Defendant Kantor as stating: Execution is driving our results - pure and simple. With both network expansion and product development on track or ahead of schedule, we continue to broaden and enrich the market for our sales force. The resulting sales momentum has enabled us to deliver strong revenue growth across all channels.

191. Those positive representations concerning the Company's business strategy, financial condition and network were materially misleading. In fact, as Plaintiffs allege in detail in section V of this Complaint, Winstar's ability to report improving financial results was completely dependent upon the Winstar Defendants' scheme to record tens of millions of dollars of bogus revenue each quarter in connection with the Company's work in designing and building-out its own broadband network. Furthermore, the Winstar Defendants' failure to disclose the substantial problems the Company was experiencing in connection with its efforts to convince Lucent to perform its contractual responsibilities to design and build the Company's broadband network rendered the Winstar Defendants' positive representations concerning that network materially misleading.

192. In conjunction with the Winstar Defendants' disclosure of the Company's third quarter financial results, they also engaged in extensive discussions with securities analysts in which the Winstar Defendants made bold, positive statements concerning the Company's financial performance and operations.

193. For example, Dow Jones reported on November 8, 2000 that, during the course of the Company's quarterly conference call to discuss the Company's financial results, Defendant Uhl stated that the Company would be at "the high end" of revenue estimates of $700 million to $740 million in fiscal 2000, and would produce revenues of $900 million to $1 billion in fiscal 2001. Dow Jones also reported that Defendant Rouhana stated that the Company had the "capital we need to get past the point we need to get to be EBITDA positive in the first half of next year and into the first part of 2002, and through the completion of (Winstar's) core network buildout."

194. Those highly positive representations were materially misleading at the time they were made. Uhl was well aware at the time he made his statement concerning the Company's revenues that his figures were attainable only if Winstar and Lucent continued to engage in their fraudulent scheme to increase Winstar's revenues. Likewise, Rouhana was aware that: Winstar's ability to fund its operations was completely dependent upon Lucent's willingness to continue to finance Winstar by means of the bogus payments for services purportedly provided to Lucent by Winstar; Lucent was unwilling to continue to make such payments; and Winstar would therefore be unable to finance its overly ambitious expansion plans.

195. On November 14, 2000, the Winstar Defendants filed with the SEC a Form 10-Q quarterly report concerning the third quarter of 2000. In that document, the Winstar Defendants stated that, during the third quarter, the Company had generated broadband services revenue of $175.90 million, other revenue of $19.22 million and total revenue of $195.12 million. Elsewhere in the Form 10-Q, the Winstar Defendants stated that, during the third quarter, Winstar had produced broadband services revenue of $175.90 million, traditional media services revenue of $15.36 million and other telecom services revenue of $3.86 million. The Winstar Defendants also stated that Winstar had posted a quarterly loss of $227.43 million, or $2.50 per share.

196. In discussing the purported improvement in Winstar's EBITDA, the Winstar Defendants also stated:

Cash used to fund negative EBITDA during the three and nine months ended September 30, 2000 was approximately $32.0 million and $133.4 million, respectively, compared to $72.6 million and $235.5 million during the same periods in 1999. We expect our EBITDA losses to continue to decline and to reach EBITDA breakeven during the first half of 2001.

197. The Winstar Defendants also falsely assured investors that the financial statements included as part of the 10-Q:

contain all adjustments (consisting only of normal recurring accrual adjustments) which, in our opinion, are necessary to fairly present our financial position as of September 30, 2000, the statements of operations for the three and nine months ended September 30, 2000 and 1999, the statements of cash flows for the nine months ended September 30, 2000 and 1999, and the statement of stockholders' deficit for the nine months ended September 30, 2000.

198. Those representations concerning the financial results generated by the Company during the third quarter of 2000 were materially false and misleading for the reasons alleged in section V of this Complaint.

199. In describing the sources of the Company's revenues in that Form 10-Q, the Winstar Defendants stated:

We classify revenue into two categories: broadband services and other.

Broadband services revenue primarily includes revenue derived from: Internet connectivity; data transmission services; web hosting;

network capacity sales; local and long distance voice services; web design and development services; professional and enhanced services, including network design and implementation, equipment selection, procurement, sales and installation; and revenues derived from the development and distribution of information content and related services over the Internet.

We also develop and distribute information content through traditional media, such as television, video, cable and radio. These revenues and revenues from sales of broadcast and programming rights and licenses are classified as other revenue. Other revenues also include those derived from a portion of an acquired long distance customer base located in markets which we do not have current plans to serve with our broadband network.

200. The Winstar Defendants also made the following materially misleading representations concerning the business segments in which Winstar operated:

Our operating segments represent business units that offer different products and serve different markets. The Broadband Services segment derives its revenues by offering its customers a variety of individual and bundled services. The Traditional Media Services segment derives its revenues by marketing and distributing information content, licenses and services in traditional markets, such as television, video, cable and radio. Our Other Telecommunications Services segment derives its revenue from a portion of an acquired long distance customer base located in markets which we do not have current plans to serve with our broadband network. Substantially all of our revenue is attributable to customers in the United States, and our assets are predominately located in the United States. Shared administrative services provided to the business units are classified as Corporate Expenses.

201. In discussing the Company's broadband services revenue for the quarter, the Winstar Defendants also stated:

Revenue from broadband services increased by $78.3 million, or 80.2%, to $175.9 million for the three months ended September 30, 2000, from $97.6 million for the three months ended September 30, 1999. We experienced continued growth in all types of broadband services revenue, driven principally by the combination of our expanding network footprint, our enhanced product set, and our evolving strength in provisioning. Revenue from large account solutions was $86.4 million for the three months ended September 30, 2000, compared to $35.4 million for the three months ended September 30, 1999. We attribute this growth to the continued expansion of our network through the installation of additional local bandwidth, data and voice switching infrastructure and the addition of our local and long-haul fiber. We are continuing to realize increased revenue especially from the sale of these data-related products and services, including end-to-end broadband connectivity, equipment and network deployment solutions to our larger customers. We have now signed contracts totaling approximately $1.4 billion from our large account customers (excluding the federal government). We expect to recognize approximately $175 million of this amount as revenue over the next 12 months.

202. The foregoing descriptions of the sources of the Company's third quarter revenues were materially misleading because of the Winstar Defendants' failure to disclose the facts alleged in section V of this Complaint. In particular, the Winstar Defendants' failure to disclose that approximately 34% of the Company's third quarter revenue was attributable to the services that Winstar supposedly performed for Lucent in designing and building-out the Winstar broadband network rendered their representations concerning the sources of the Company's revenues materially misleading.

203. The Winstar Defendants also assured investors in the third quarter Form 10-Q that the Company's existing financing was sufficient to fund Winstar's operations through the end of 2001. Specifically, the Winstar Defendants stated:

We anticipate, based on our business plan and certain assumptions, that our existing financial resources will be sufficient to fund our planned operations and capital requirements into the first quarter of 2002. These financial resources include our existing cash balances and amounts we expect to receive in connection with our Series H financing and expansion of our credit facility, as well as amounts we expect will be immediately available under our vendor financing facilities with Lucent, Cisco and Compaq. In addition, we will have additional amounts available to us under the Lucent facility as any portion of our outstanding Lucent loans is syndicated (up to the aggregate facility amount of $2 billion), and up to an additional $250 million available under the Cisco facility as we meet certain conditions described elsewhere in this report. As a result of our recently announced financing commitments, our expectation to be EBITDA breakeven in the first half of 2001 and the expectation that our core network infrastructure will be completed by the end of 2001, we believe we will have the flexibility to grow our business at whatever pace is appropriate for the existing capital environment.

204. As Plaintiffs allege in detail in section V of this Complaint, those representations were materially misleading at the time they were made because Winstar's ability to continue to fund its operations was dependent, throughout the Class Period, upon Lucent's willingness to continue to engage in the unlawful accounting practices designed to inflate the revenue of Lucent and Winstar described therein. Furthermore, by the time the Winstar Defendants filed the third quarter Form 10-Q with the SEC, Lucent had expressed strong reservations to the Winstar Defendants concerning its willingness to continue to fund the Company's operations, particularly through the type of fraudulent transactions described in section V of the Complaint. Accordingly, the Winstar Defendants' failure to disclose that the Lucent Facility would not be available to fund the Company's operations rendered their description of the Company's liquidity materially false and misleading.

205. All of the foregoing misleading statements concerning the Company's third quarter financial results and financial position had the effect of either: (a) inflating the market prices of Winstar securities; or (b) maintaining the market prices of those securities at levels that would not have prevailed had Defendants made accurate disclosures concerning the Company, its operations and its prospects. Accordingly, those misleading statements had the effect of damaging Class members who purchased Winstar securities after the Winstar Defendants made the representations.

E. The Winstar Defendants' Materially Misleading Representations Concerning The Company's Fourth Quarter 2000 Financial Results And Operations

206. On February 27, 2001, the Winstar Defendants issued a press release announcing the Company's financial results for the fourth quarter and full 2000 fiscal year.

207. In that press release, the Winstar Defendants attempted to create the impression that Winstar was a thriving enterprise. For example, the Winstar Defendants reported that the Company had produced total revenue of $225.1 million for the quarter ended December 31, 2000, a claimed 59.1% increase over the year-ago quarter. The Winstar Defendants also stated that the Company's broadband services revenue for the quarter was $197.3 million, reportedly up 74.6% from the prior year and up 12.2% from the previous quarter.

208. The press release also contained the following description of the Company's financial results for the fourth quarter and fiscal year 2000:

Winstar's stronger than expected revenue performance was augmented by its eighth consecutive quarter of sharp improvement in gross margin. The company posted an all-time high gross margin of 50.3% for the quarter, as compared to 47.3% in the prior quarter, 35.4% a year ago, and 10.5% as recently as two years ago. The company expects execution of its on-net strategy to continue to drive gross margin improvement throughout 2001.

The combination of strong revenue growth and margin improvement enabled Winstar to narrow its EBITDA loss for the quarter to $19.9 million, a $41.9 million improvement from the year-ago quarter, and a $12.0 million, or 37.7%, improvement from the prior quarter. This is the company's sixth consecutive quarter of significant improvement since posting its peak EBITDA loss in the second quarter of 1999. Winstar expects its EBITDA losses to continue to decline until it reaches EBITDA breakeven, which is expected to occur during the second quarter of 2001.

The company reported a net loss for the quarter applicable to common shareholders of $255.1 million, or $2.76 per share, $0.02 better than consensus analyst earnings expectations. For the full year ended December 31, 2000 Winstar reported total revenue of $759.3 million, a 70.4% increase over 1999. Broadband services revenue increased to $659.5 million, up 85.2% from the prior year. EBITDA losses for the year were $153.4 million, down over 48% from $297.3 million in 1999.

209. Each of the foregoing representations concerning the financial results posted by the Company during the fourth quarter of 2000 and the 2000 fiscal year was materially misleading for the reasons outlined in section V of this Complaint.

210. The fourth quarter press release contained a number of additional material misrepresentations concerning the status of the Company's operations. The press release quoted Defendant Rouhana as stating:

Solid and sustained execution of our business strategy has enabled us to deliver another quarter of results that exceed consensus expectations. Our performance in two key areas has driven much of that success. First, consistent execution of our strategy to accelerate the build-out of our broadband network, while enhancing its value with a wide range of broadband services, continues to pay dividends. Second, the unprecedented success of our disciplined on-net strategy has resulted in sharply improved financial performance for eight consecutive quarters.

211. The press release also quoted Defendant Kantor as stating:

Execution is driving our results - pure and simple. With both network expansion and product development on track or ahead of schedule, we continue to broaden and enrich the market for our sales force. The resulting sales momentum has enabled us to deliver strong revenue growth across all channels. Given our goal of doubling our addressable market again in 2001, we clearly expect that momentum to continue.

212. Contrary to those statements, it was evident to the Winstar Defendants long before the fourth quarter press release was issued that the Company was in severe financial turmoil. As is specifically alleged in section V of the Complaint, the Company was not experiencing the "success" referred to by Rouhana. Rather, the Winstar Defendants had long propped up the Company's financial results by engaging in the bogus transactions with Lucent that are described in detail in section V of this Complaint.

213. Moreover, by the time the fourth quarter press release was issued, the Winstar Defendants had been informed by Lucent that Lucent would not continue to funnel "revenue" to Winstar in the form of payments for services rendered in connection with the design and build-out of the Winstar broadband network. Additionally, Lucent had clearly indicated to the Winstar Defendants by that date that Lucent would not continue to provide additional vendor financing to Winstar because of the Company's insolvency. As a result, Winstar's continued viability as a company was severely threatened by the time the Winstar Defendants made the foregoing positive statements.

214. Despite those mounting problems, the Winstar Defendants continued to make additional positive statements concerning the status of the Company's operations following the announcement of the fourth quarter and year-end results. For example, during a February 27, 2001 interview on CNBC, Rouhana made a number of uniformly positive statements concerning the Company's operations.

215. In that interview, Rouhana stated:

Well, we are doing a little bit better than we thought we would be doing. We have a little bit more revenue than expected. Our margins are a little bit stronger and we are seeing customer acceptance at a slightly higher rate.

216. Furthermore, Rouhana informed investors that he and Winstar were "pretty comfortable about what we've projected for the rest of the year" and stated, "I think we'll make those [projected] numbers."

217. Moreover, in the Company's February 27, 2000 conference call with securities analysts and institutional investors, Defendant Uhl sought to debunk reports that the Company's vendor credit agreements were in jeopardy. In that regard, Uhl stated, "This is not true. . . . We have not defaulted on any debt obligations, vendor, high-yield or senior, nor do we expect to. Further, our credit agreements are fully in effect . . . and we expect to utilize them going forward."

218. Moreover, as The Wall Street Journal reported on April 19, 2001, in a March 16, 2001 interview, Rouhana stated that Winstar would have no difficulty making the $75 million interest payment due on April 16, 2001 on which Winstar eventually defaulted. Moreover, in the same interview Rouhana falsely emphasized that the Company had not been utilizing money that it borrowed from Lucent to make interest payments and that it had no plans or need to do so.

219. The representations made by the Winstar Defendants during the CNBC interview and in conferences with the investing public were materially false and misleading for the reasons alleged in section V of this Complaint. Contrary to the highly positive representations, by February 27, 2001, the Company was clearly unable to continue to fund its operations and would not be able to pay its creditors, much less post the dramatically improved revenue, EBITDA and net income numbers Rouhana and the Winstar Defendants constantly assured investors the Company would attain.

220. All of the foregoing misleading statements concerning the Company's fourth quarter financial results and financial position had the effect of either: (a) inflating the market prices of Winstar securities; or (b) maintaining the market prices of those securities at levels that would not have prevailed had the Winstar Defendants made accurate disclosures concerning the Company, its operations and its prospects. Accordingly, all of those misleading statements had the effect of damaging those members of the Class who purchased Winstar securities after the Winstar Defendants made those representations.

VII. DEFENDANT LUCENT'S PARTICIPATION IN THE FRAUDULENT SCHEME TO FALSELY INFLATE WINSTAR'S FINANCIAL RESULTS

221. As is alleged in detail above, defendant Lucent directly and actively participated with the Winstar Defendants in a fraudulent scheme to falsely inflate the Company's financial results by engaging in material transactions with Winstar that lacked economic substance, but enabled both Winstar and Lucent to report excessive revenues.

222. The Winstar Defendants and Lucent engaged in that fraudulent scheme to create the impression that Winstar was a rapidly growing enterprise and to attract additional investors to finance Winstar's expansion plans. Throughout the Class Period, however, Winstar was suffering staggering losses as a result of the billions of dollars in capital expenditures it made in an effort to build out the Company's broadband network before investors learned the true status of the Company's financial operations. Lucent participated in this fraudulent scheme because Winstar agreed to "purchase" material amounts of Lucent products that Winstar did not want or need, thereby inflating Lucent's revenues.

223. The fraudulent transactions engaged in by Lucent and the Winstar Defendants in furtherance of this scheme include the following:

a. Lucent frequently requested that Winstar make substantial purchases of Lucent telecommunications equipment which Winstar did not need or want in order to enable Lucent to meets its revenue objectives, in exchange for providing Winstar with funds to finance its expansion plans.
b. Pursuant to a "bill and hold" letter from Winstar, Winstar purchased large inventories of equipment from Lucent for which Winstar had no current use as the Company's financial status rapidly deteriorated toward bankruptcy. The fraudulent nature of these "sales" is further indicated by the fact that Lucent stored the "sold" equipment in its warehouses at Lucent's expense.
c. Lucent and Winstar entered into a fraudulent arrangement with respect to consulting services that inflated both companies' revenues. Winstar contracted with Lucent for the development of a broadband network for Winstar by Lucent and for the purchase of special professional services from Lucent. Lucent, in turn, hired Winstar to provide the special professional services and the network development. This fraudulent arrangement supposedly justified Winstar's recognizing revenue on services that Winstar provided to itself. These services were in effect laundered through Lucent for the fraudulent purpose of generating revenue for Winstar. Lucent reciprocally benefitted from this fraudulent scheme by recognizing revenue for services that Lucent did not perform.
d. Lucent and Winstar frequently engaged in end-of-quarter transactions for which Lucent immediately recorded revenue but agreed to refrain from billing Winstar until after the end of the quarter to allow Winstar to avoid recording expenses on the Company's quarterly financial statements.

224. As a result of the fraudulent Lucent-Winstar transactions specifically described herein, Winstar materially overstated its revenues and understated its expenses during the Class Period and Lucent recognized $385.9 million of revenue during Lucent's fiscal year ended September 30, 2000. In this way, both Lucent and Winstar benefitted from these fraudulent transactions because both companies were able to report the kind of substantial revenue growth that they had promised investors they could expect.

225. As demonstrated by the e-mail correspondence regarding these fraudulent transactions between and among Lucent's officers,

Lucent's senior executives and the Winstar Defendants, it is evident that the highest levels of both Lucent's and Winstar's management were aware of and/or involved in the efforts undertaken by Winstar and Lucent to falsely inflate each other's reported revenues.

226. Lucent also furthered the fraudulent scheme in which it participated with the Winstar Defendants by making positive representations concerning its relationship with Winstar long after that relationship was demonstrating the serious problems described in detail above.

227. For example, as late as December 7, 2000, Lucent issued a joint press release with Winstar in which Lucent made several positive statements concerning the Lucent-Winstar relationship. In the joint press release, Lucent touted an agreement that would "assist[] Winstar in building out its international wireless broadband network in Asia."

228. Although Lucent was well aware by that time that it was not performing the network design and build-out services it had contracted to provide for Winstar, Lucent also stated, "Under the agreement, Lucent provides network design, integration and build-out services, including all of Winstar's voice and data service offerings."

229. In direct contrast to the admissions made by Winstar in the Lucent Complaint, Lucent and Winstar also stated, "Using its best-of-breed technology and equipment for a state-of-art network solution, Lucent also accesses, tests and integrates all elements in Winstar's network offering, including equipment from other manufacturers."

230. Thus, long after Winstar had acknowledged that Lucent had proven itself incapable of building out the Winstar network and of providing the best-of-breed technology touted in the December 7, 2000 press release, Lucent and the Winstar Defendants continued to describe their relationship, and Lucent's contribution to Winstar's ability to complete the build out of its network, in the most positive terms.

VIII. WINSTAR'S BANKRUPTCY

231. On April 2, 2001, the Winstar Defendants' house of cards fell when the Company disclosed in a filing with the SEC that it would not be submitting its Form 10-K annual report for the 2000 fiscal year in a timely manner. In that filing, the Winstar Defendants stated:

The Company is engaged in discussions concerning certain material transactions which have not been completed. In light of (1) the uncertainty over these potential transactions and (2) the required use of corporate personnel and resources that would otherwise have been used for the preparation of the annual report on Form 10-K, the Company is unable to file such report within the prescribed time period. The Company expects to file such report not later than April 17, 2001.

232. The Company's failure to file its Form 10-K in a timely manner sparked market rumors that Winstar was insolvent and would be forced to seek to reorganize itself in bankruptcy court. As a result, the Company's common stock, which had traded as high as $32.00 during the Class Period, collapsed to $0.875 per share, on volume of more than 16 million shares. The Company's publicly traded bonds similarly declined in value. To date, Winstar has failed to file any additional financial statements with the SEC.

233. Those declines represented remarkable retreats from the prices at which Winstar securities had traded during the Class Period. In the weeks preceding the belated announcement of the Company's financial problems, Winstar common stock had closed at $2.16 per share on March 30, 2001, $12.50 per share on March 1, 2001 and $17.56 per share on February 1, 2001. Earlier in the Class Period, the stock closed as high as $32.00 per share. Today, both Winstar common stock and the Company's its publicly traded bonds are essentially worthless. Moreover, while the Winstar Defendants repeatedly professed that the Company was well-capitalized into 2002, Winstar can muster the resources to pay its bondholders only a few pennies on the dollar.

234. Following the announcement of the Company's inability to file its Form 10-K in a timely manner, Winstar moved steadily towards bankruptcy court. On April 5, 2001, the Company announced that it was "halting" its expansion plans and laying off 2,000 of its workers (representing about 50% of its workforce).

235. As The Wall Street Journal reported in an April 6, 2001 article, those job cuts were announced after the Company failed to make hundreds of millions of dollars in asset sales during the first quarter of 2001. In particular, the article noted that the Company had been attempting to sell excess capacity on its broadband network. Thus, while the Winstar Defendants had repeatedly emphasized the great significance of their efforts to increase the scope of the network, the fact of the matter was that the network was far more expansive than was necessary to service the Company's limited customer base.

236. On April 16, 2001, Winstar defaulted on its senior debt by failing to make an interest payment of $75 million. On that date, the Company also announced that it was considering filing for bankruptcy protection. In the press release announcing those developments, Winstar also revealed that Lucent had declared the Company to be in default on its loans from Lucent.

237. In an April 17, 2001 article reporting those facts, The Wall Street Journal observed that "the news belies recent cheery pronouncements by company executives, who as recently as two weeks ago had insisted the company had enough cash to meet its obligations through the rest of the year."

238. On or about April 18, 2001, Winstar filed for Chapter 11 bankruptcy protection in Delaware.

239. On or about April 26, 2001, Winstar was delisted from the NASDAQ exchange.

IX. PLAINTIFFS AND THE CLASS REASONABLY RELIED UPON THE INTEGRITY OF THE MARKET PRICES FOR WINSTAR SECURITIES IN PURCHASING THOSE SECURITIES DURING THE CLASS PERIOD

240. Plaintiffs and all of the members of the Class are entitled to the presumption of reliance upon the material misrepresentations and omissions alleged herein that is provided by the fraud on the market doctrine.

241. The fraud on the market doctrine's presumption of reliance arises here for the following reasons:

a. As a regulated issuer, Winstar filed periodic public reports with the SEC that disclosed information that was promptly disseminated to investors.
b. Winstar regularly communicated with public investors via established market communication mechanisms such as the regular dissemination of press releases on major newswire services, regular communications with the financial and trade press and through meetings with institutional investors and other major Winstar shareholders.
c. Winstar securities were traded in developed and efficient markets. That is, the information disclosed by Defendants to the public concerning Winstar was incorporated by the market for Winstar securities into the market price for those securities in a manner that caused the market price of Winstar securities to reflect all publicly-available information concerning Winstar. Of course, the market price of Winstar securities did not reflect the information that Defendants concealed from the market throughout the Class Period. By concealing that information, Defendants therefore caused the Company's securities to trade at inflated prices throughout the Class Period.
d. Throughout the Class Period, Winstar common stock met the requirements for listing on the NASDAQ system, a highly efficient market. During that time frame, Winstar securities were actively traded on the NASDAQ and other public markets.
e. Winstar was followed by several securities analysts employed by major brokerage firms and institutional investors who analyzed the Company's operations and prospects on a regular basis and who recommended the purchase or sale of Winstar stock and bonds on the basis of those analyses.
f. Defendants made material misrepresentations during the Class Period and failed to disclose materials facts that they were obligated to disclose under the circumstances.
g. Plaintiffs and the other members of the Class purchased their Winstar securities between the time Defendants made the misrepresentations and omissions alleged herein and the time the market learned the adverse facts concerning the Company's operations that Defendants concealed throughout the Class Period.

242. Plaintiffs and the members of the Class are therefore entitled to a presumption of reliance upon the integrity of the market for Winstar securities for the purposes of class certification and for the ultimate proof of their claims on the merits. Similarly, Plaintiffs and the members of the Class are entitled to a presumption of reliance upon the material omissions alleged herein.

X. ADDITIONAL FACTS AND CIRCUMSTANCES THAT DEMONSTRATE THAT DEFENDANTS ACTED WITH SCIENTER

243. Defendants made the misrepresentations and omissions concerning then-existing facts complained of herein with scienter in that they knew or recklessly disregarded that their representations concerning the Company were materially false and misleading when made.

244. With respect to any forward-looking misrepresentations or omissions alleged herein, Defendants made such misrepresentations or omissions with knowledge that their statements were materially false. The facts alleged in the following paragraphs, among others, strongly support the conclusion that Defendants acted with scienter.

A. The Winstar Defendants Possessed Substantial Motives To Commit The Fraudulent Acts Alleged Herein

245. The Winstar Defendants possessed substantial motives for making the misrepresentations and for failing to disclose the material facts identified in this Complaint.

246. Prior to and throughout the Class Period, Winstar posted substantial net losses as the Winstar Defendants raced to build out the Company's broadband network before investors' willingness to supply their capital to the Company expired.

247. As the Company's bankruptcy filing demonstrates, in order to continue to attract investors' capital, the Winstar Defendants needed to create the impression that the Company was growing such that its revenue would be sufficient to pay the enormous costs associated with building the Company's network. Once Lucent or other potential investors became convinced that Winstar would not be successful in growing its revenue to that magnitude, the Company was destined for bankruptcy because the Winstar Defendants were aware that the Company would not be a profitable operation - even under the unduly optimistic projections that they shared with securities analysts and other investors - until at least 2004.

248. Thus, throughout the Class Period, the Winstar Defendants were fighting a constant battle to demonstrate that they could implement the expansion plans that they repeatedly described and to grow the Company's revenues substantially in order to achieve profitable operations.

249. The pressure to create that favorable impression was particularly great because, throughout the Class Period, the Winstar

Defendants were attempting to raise additional financing from investors. Had the Company announced disappointing results - particularly in the adverse market for telecommunications concerns that prevailed in 2000 - Winstar would have been unable to raise additional financing and would have been forced into bankruptcy.

250. The specific transactions that provided the Winstar Defendants with substantial incentive to make materially misleading representations concerning the Company's operations included the following:

a. In the second quarter of 2000, the Winstar Defendants attempted and succeeded in conducting an exchange offer for much of the Company's outstanding debt. In connection with that exchange offer, Winstar issued $2.08 billion in securities, including: (i) $325 million of 12-1/2% senior exchange notes due 2008; (ii) $637,653,000 in 12-3/4% senior exchange notes due 2010; (iii) $926,957,000 in 14-3/4% senior discount exchange notes due 2010; (iv) $190,040,000 in Euro-denominated 12-3/4% senior exchange notes due 2010; (v) $1,340,000 in 12-3/4% senior exchange notes due 2010; and (vi) $3,904,000 in 14-3/4% senior discount exchange notes due 2010.
b. In May 2000, the Winstar Defendants secured a line of credit in the amount of $1.15 billion from a consortium of banks and other financial institutions.v c. At the time that line of credit was secured, the Winstar Defendants paid off the balance owed to Lucent under the Company's existing vendor financing facility with Lucent. At the same time, the Winstar Defendants succeeded in obtaining a commitment of $2 billion in vendor financing from Lucent. By the end of the third quarter, Winstar had drawn down $497 million of that available financing. By the end of 2000, the amount outstanding under the Lucent facility exceeded $745 million.
d. On August 4, 2000, Winstar filed with the SEC a "shelf" Registration Statement for a $2 billion offering of an indeterminate number of shares of the Company's common stock, preferred stock, debt securities and depositary shares. While the Winstar Defendants did not complete that offering, the fact that they were continuing to explore additional financing for the Company is demonstrated by their willingness to undertake the substantial cost and effort associated with filing the Registration Statement with the SEC.
e. In early November 2000, Winstar announced that it had "completed a $1.02 billion financing package." That financing package included "$270 million in private equity" from investors that included Credit Suisse First Boston Equity Partners, L.P., Welsh, Carson, Anderson & Stowe VIII, L.P., Microsoft Corporation, CPQ Holdings, Inc., a wholly-owned subsidiary of Compaq Computer Corporation ("Compaq"), and other investors.
f. In addition, the Winstar Defendants reported that the Company had secured vendor financing of up to $500 million from a subsidiary of Cisco Systems, Inc. and up to $50 million in vendor financing from a subsidiary of Compaq Computer Corporation.
g. Winstar also used its stock as currency during the Class Period to acquire other companies, including Technet, a significant German Internet Service Provider.

251. Each of the foregoing transactions was a necessary step in the Winstar Defendants' constant battle to finance the Company's money-losing operations. Furthermore, all of the Winstar Defendants were well aware throughout the Class Period that none of those transactions would have been consummated had they disclosed the true state of the Company's operations.

252. Accordingly, the Winstar Defendants' need to raise massive amounts of money to offset the constant and substantial losses suffered by the Company provided the Winstar Defendants with a powerful motive to mislead investors concerning the status of the Company's operations and financial performance.

B. Lucent Had Substantial Motives To Commit The Fraudulent Acts Alleged Herein

253. Lucent also possessed substantial motives for engaging in the fraudulent scheme alleged herein.

254. As Plaintiffs allege in detail above, throughout the Class Period, Lucent and Winstar cultivated a synergistic relationship whereby both companies agreed to take steps necessary to create the appearance that they were both producing growing revenues.

255. Pursuant to that relationship, Lucent frequently demanded that Winstar make substantial end-of-quarter purchases of telecommunications equipment from Lucent in order to facilitate Lucent's ability to produce the financial results that it had informed investors they could expect.

256. Winstar agreed to make those end-of-quarter purchases in exchange for Lucent's agreement to permit Winstar to bill Lucent for engineering and design services performed by Winstar to build its own network.

257. Thus, Lucent, which was facing increasing difficulty in "making its numbers" as the Class Period progressed, possessed substantial motives for engaging in a fraudulent scheme to inflate Winstar's reported financial results. In fact, Lucent's participation in that scheme was a necessary aspect of its efforts to inflate its own financial results.

258. Ultimately, those efforts proved disastrous, as Lucent was forced to restate its own financial results to reduce its fiscal 2000 revenue by $679 million. That massive restatement has triggered numerous shareholder lawsuits against Lucent as well as an ongoing SEC investigation of Lucent's financial reporting, including its relationship with Winstar.

259. Lucent was also initially motivated to participate in the fraudulent scheme to inflate Winstar's financial results by Lucent's desire to secure the repayment of the enormous vendor financing that Lucent extended to Winstar. As became clear at the end of the Class Period, Winstar could not repay the many millions of dollars that it borrowed from Lucent unless investors continued to provide additional financing to the Company. As a result, it was necessary for Winstar and Lucent to create the appearance that Winstar was increasing its revenue in order to create any possibility that Lucent would receive payment from Winstar for the millions of dollars in vendor financing that Lucent extended to Winstar.

C. The Access Of The Winstar Defendants And Lucent To The Adverse Information Concerning The Company's Operations

260. The conclusion that the Winstar Defendants and Lucent acted with scienter is also supported by the fact that those Defendants were provided with complete access to all of the adverse information concerning Winstar's operations that is alleged herein.

261. The Winstar Defendants were aware of that information as a result of their status as the Company's highest ranking executives.

262. Likewise, Lucent was provided with access to that information because the single most important aspect of the fraudulent scheme alleged by Plaintiffs was Winstar's fraudulent transactions with Lucent, particularly the end-of-quarter transactions whereby both companies attempted to inflate their reported financial results.

263. Each of the Winstar Defendant is a sophisticated individual who held a senior executive position with the Company for a number of years. Those positions provided the Winstar Defendants with access to the material adverse information that was concealed from the members of the Class throughout the Class Period.

264. The Winstar Defendants were provided with such adverse, material information by means of, inter alia, their access to internal corporate documents (including the Company's operating plans, budgets and forecasts and reports of actual operations compared thereto), regular communications with other officers and employees at Winstar, attendance at meetings of the management and Board of the Company and committees thereof, and via reports and other information provided to them in connection therewith.

265. In particular, each of the Winstar Defendants was regularly provided with management reports that demonstrated, among other things, that: (a) the Company was continually entering large end-of-quarter transactions with Lucent that lacked economic substance; (b) a large percentage of the Company's total revenue was generated through those highly unusual transactions; (c) the Company was experiencing difficulty inducing Lucent to fulfill its obligations to Winstar under the Supply Agreement; and (d) Lucent was growing increasingly resistant to continuing to provide Winstar with financing to fund the build-out of the Company's broadband network. Because of its participation in the foregoing transactions, as well as its status as the Company's largest supplier and principal source of financing, Lucent was also provided with complete access to the foregoing information.

266. In addition, the Winstar Defendants' scienter is demonstrated by the fact that their materially misleading representations concerned the most important aspects of the Company's operations and substantial transactions about which the Winstar Defendants - as the Company's principal executives - could not reasonably have been unaware. Similarly, because Lucent was a participant in many of the fraudulent transactions central to the fraud perpetrated by Defendants, Lucent was equally aware of the misleading nature of Defendants' representations and omissions.

267. The Winstar Defendants and Lucent were also aware that the SEC had commenced an inquiry-level investigation into the nature of the relationship between Lucent and Winstar by the fourth quarter of 1999, further highlighting to the Defendants that the Company's transactions with Lucent were suspicious in nature.

268. In particular, the Winstar Defendants and Lucent were completely cognizant that the Company was generating tens of millions of dollars each quarter from bogus transactions with Lucent that had no economic substance. Indeed, Defendant Kantor stated in an e-mail specifically described herein that he and Lucent executives had agreed to engage in such transactions a million times.

269. Additionally, Winstar has admitted in the Winstar Bankruptcy that it was aware from the start of its relationship with Lucent (and before the Class Period) that Lucent was incapable of performing its obligations of designing and building Winstar's broadband network. Nevertheless, the Winstar Defendants and Lucent repeatedly stated during the Class Period that the build-out of the network was proceeding according to plan and that the network was being built with Lucent's state-of-the-art equipment and never mentioned any problems that the Company was experiencing in its all-important relationship with Lucent.

270. The Winstar Defendants' failure to disclose that sales of services to Lucent constituted a large percentage of the Company's supposed revenue also demonstrates their scienter. By virtue of the size of the business conducted between Winstar and Lucent alone, the Winstar Defendants - as the Company's principal executives - either knew or should have known of the magnitude of those transactions.

271. Furthermore, as is specifically alleged above, many of the Company's large revenue-generating transactions with Lucent were conducted at the end of financial quarters as a quid pro quo for Winstar's agreement to purchase large dollar amounts of Lucent products. The instructions to push for those substantial end-of-quarter transactions came from the Winstar Defendants.

272. Defendant Uhl was particularly remiss in failing to disclose the adverse facts concerning the Company's financial operations that are alleged herein. As the Company's CFO, Uhl was ultimately responsible for the content of Winstar's financial statements, including the accuracy of the footnotes and other disclosures contained in those financial statements. Furthermore, Uhl was personally responsible for implementing the financial controls necessary to prevent the Company from engaging in fraudulent transactions, such as Winstar's revenue-swapping transactions with Lucent and those transactions in which Winstar recognized revenue although it had provided its customer with a right to return the merchandise "sold" by the Company.

273. Uhl was also personally responsible for guaranteeing that the Company's financial statements complied with GAAP by, among other things, disclosing that approximately 32% of the Company's revenue for 1999 and 2000 was derived from transactions with Lucent, even setting aside the fact that those transactions were fraudulent from the outset.

D. Winstar Has Publicly Admitted Facts That Demonstrate That The Winstar Defendants And Lucent Acted With Scienter

274. In the documents filed by Winstar in the Winstar Bankruptcy, the Company has admitted several critical facts that demonstrate that the Winstar Defendants and Lucent acted with scienter in making the misrepresentations and omissions alleged herein.

275. For example, in the Lucent Complaint and the Ackerman Affidavit, Winstar has conceded that transactions with Lucent were responsible for over 32% of the revenue generated by the Company during 1999 and 2000. Yet, none of the Winstar Defendants made any disclosure regarding that concentration of the Company's revenue during the Class Period.

276. Furthermore, Winstar had conceded in the Winstar Complaint and the Ackerman Affidavit that Winstar experienced extreme difficulty in its efforts to convince Lucent to perform its obligations under the Supply Agreement from the outset of the Lucent-Winstar relationship. Again, however, neither the Winstar Defendants nor Lucent made any disclosure concerning those problems during the Class Period. To the contrary, the Winstar Defendants and Lucent repeatedly stated that their efforts to build the Company's broadband network were proceeding according to plan through Winstar's use of the supposedly "state-of-the-art" components purchased from Lucent.

277. Winstar has also conceded in the Lucent Complaint and the Ackerman Affidavit that the Winstar Defendants were aware long before the Winstar Defendants made positive representations concerning the Company's ability to fund its operations on February 27, 2001 and March 16, 2001 that Lucent was making a concerted effort to avoid any continued responsibility to fund Winstar. Nevertheless, in order to maintain the possibility of raising additional capital from other investors, the Winstar Defendants flatly denied market rumors that Lucent was refusing to fund the Company's operations.

E. The Timing Of The Winstar Bankruptcy Filing Further Evidences The Winstar Defendants' Scienter

278. As is specifically alleged above, Winstar's bankruptcy filing followed closely on the heels of the Winstar Defendants' highly positive statements concerning the results posted by the Company during the fourth quarter of 2000 and the Company's financial position.

279. Particularly in light of the fact that Lucent had repeatedly informed the Winstar Defendants that it did not intend to continue to fund Winstar's operations, those representations were grossly misleading at the time they were made. As a result, the temporal proximity between the Winstar Defendants' uniformly positive representations and the ultimate disclosure of the Company's insolvency further supports the strong inference that the Winstar Defendants acted with scienter.

F. Additional Facts That Demonstrate That Grant Thornton Acted With Scienter

280. In delivering a clean audit opinion concerning the Company's 1999 financial statements, Grant Thornton ignored numerous red flags that demonstrated that those financial statements were not prepared in accordance with GAAP. Because those red flags were of such an obvious character, Grant Thornton either knew of their existence, but nevertheless ignored them, or was grossly reckless in failing to take note of those facts.

281. In either event, Grant Thornton's clean audit opinion - perhaps the most critical statement delivered by any of the Defendants during the Class Period - was grossly reckless.

282. Among other red flags, Grant Thornton ignored the fact that Winstar was generating between 20% and 35% of its revenue from the bogus transactions with Lucent alleged herein. The magnitude of those transactions, and the fact that most were entered into at or near the end of the fiscal quarters of 1999, should have caused Grant Thornton to further examine the substance of those transactions.

283. Had Grant Thornton further investigated those transactions - as it was obligated to do - it would have determined that they were merely part of Winstar's agreements with Lucent to swap revenue-generating transactions in order to create the false impression that the two companies were enjoying substantial revenue growth.

284. Furthermore, the magnitude of the Lucent transactions should have caused Grant Thornton to require the Winstar Defendants to disclose that 32% or more of the Company's 1999 revenue was generated in connection with transactions with Lucent. Under GAAP and applicable SEC regulations, the Winstar Defendants, and therefore Grant Thornton, were required to disclose that heavy concentration in the Company's revenue stream. Moreover, in light of Lucent's status as Winstar's principal supplier of equipment and financing for that equipment and other operations, the fact that Lucent was such a significant source of the Company's revenues was particularly material to Winstar investors.

285. By virtue of its position as Winstar's longtime independent accountant and auditor, Grant Thornton had complete access to the files and key employees of the Company at all relevant times. In particular, prior to issuing its clean audit opinion with respect to the Company's 1999 financial statements, Grant Thornton had complete access to Winstar's confidential financial, operating and business information. Documents and information that did or would have revealed the Winstar Defendants' accounting fraud to Grant Thornton were therefore readily accessible to Grant Thornton prior to the time that it issued its materially misleading audit opinion.

286. Furthermore, Grant Thornton employees were frequently present at Winstar's headquarters and other offices. During 2000 alone, Grant Thornton billed Winstar in excess of $5 million for its services. As a result, Grant Thornton had ample opportunity to discover the obvious accounting improprieties alleged herein, none of which Winstar attempted to conceal from Grant Thornton.

287. In issuing its clean audit opinion, Grant Thornton also ignored red flags that demonstrated that the accounting controls employed by Winstar were inadequate to discover the accounting improprieties alleged herein.

288. In failing to discover the fraudulent transactions with Lucent, Grant Thornton also ignored the red flag that, throughout 1999, Winstar and the Winstar Defendants were under pressure to raise substantial additional financing in order to fund the Company's money-losing operations. Grant Thornton was particularly cognizant of the Company's need to raise additional funding because it assisted Winstar in attempting to raise that financing.

289. Grant Thornton also knew or should have known that the Winstar Defendants were under significant pressure to report improving financial results and to "make the numbers" that they projected to Wall Street analysts as a result of the Company's need to raise additional financing. As Grant Thornton was aware, any shortfalls in the Company's projected financial results would have made it all but impossible for the Winstar Defendants to raise the substantial additional financing that they needed to raise during the Class Period.

290. The accounting profession recognizes that the possibility of management utilizing fraudulent accounting practices is particularly strong in such circumstances. As a result, Grant Thornton was required by AU §§ 150.02, 311.07 and 311.06 to give such factors heightened consideration in planning its audit. Yet, Grant Thornton failed to conduct its audit in a manner designed to uncover the fraudulent transactions conducted by Lucent and Winstar.

291. The nature of the fraud engaged in by the Winstar Defendants during the Class Period also supports the conclusion that Grant Thornton acted knowingly or in a grossly reckless manner in issuing its clean audit opinion in that the "audit" was so deficient as to amount to no audit at all.

292. Although the Winstar Defendants' fraud involved significant dollar amounts, it was neither sophisticated nor difficult to uncover. Rather, that fraud focused heavily upon very large, end of quarter transactions with a single customer - Lucent. In light of the size of those transactions, and their suspicious timing, they should have been particularly easy for Grant Thornton to detect. Indeed, any appropriately designed audit would have taken special note of the unusual Lucent-Winstar transactions.

293. Furthermore, the fact that the transactions were conducted with Lucent should also have been a red flag to Grant Thornton. In light of Winstar's status as one of Lucent's largest customers, and the substantial sums of money Lucent had invested in Winstar's success, Lucent had a clear incentive to take whatever steps were necessary to prop up Winstar's financial results. Furthermore, Winstar's contention that Lucent required Winstar's expertise to install Lucent's own equipment on Winstar's broadband network - the explanation delivered in the Lucent Complaint for the huge amount of "engineering fees" paid to Winstar by Lucent during the Class Period - is sorely lacking in credibility. Lucent is one of, if not the most, sophisticated telecommunications equipment suppliers in the world. Grant Thornton should not have accepted Winstar's assertion that Lucent required Winstar's expertise to install and implement Lucent's own equipment at face value.

294. Thus, in violation of its obligations under generally accepted auditing standards ("GAAS") - particularly its obligations under AU § 316.05 to design its audit to provide reasonable assurance of detecting errors and intentional misstatements and under AU § 230.01 to exercise due professional care in performing its audit - Grant Thornton either failed to determine that the Winstar Defendants were fraudulently accounting for the Lucent transactions or recklessly disregarded that information.

XI.DEFENDANTS' MATERIALLY FALSE REPRESENTATIONS AND OMISSIONS AND FRAUDULENT COURSE OF CONDUCT WERE THE CAUSE OF THE DAMAGES SUFFERED BY PLAINTIFFS AND THE CLASS

295. As described herein, Defendants made or caused to be made a series of false statements and failed to disclose various material information concerning Winstar. At all material times, Defendants' misrepresentations had the effect of either inflating the market price of Winstar securities or of maintaining the price of those securities at values those securities would not have traded had the truth concerning the Company's operations been disclosed to investors. Likewise, throughout the Class Period, Defendants' material omissions and other acts in furtherance of the scheme to defraud described herein had the effect of maintaining the prices of Winstar securities at levels those securities would not have traded had the truth concerning the Company's operations been disclosed to investors.

296. Defendants' false portrayal of Winstar's business operations during the Class Period and fraudulent course of conduct resulted in Plaintiffs and other members of the Class purchasing Winstar securities at prices significantly in excess of the actual value of those securities.

297. Plaintiffs and other members of the Class would not have purchased Winstar securities at the prices that prevailed during the Class Period, if at all, had they been aware of the true facts concerning the Company's business operations and prospects.

298. When the market determined the true status of Winstar's operations, the prices of the Company's securities declined substantially in value. Indeed, the securities held by the members of the Class are completely worthless.

299. Accordingly, the material misrepresentations, omissions, acts, practices and schemes alleged herein were the proximate causes of the damages sustained by Class members in connection with their purchases of the Company's securities during the Class Period.

XII. NO SAFE HARBOR

300. The statutory safe harbor provided for forward-looking statements under certain circumstances does not apply to any of the misrepresentations or omissions alleged herein.

301. Defendants did not adequately identify any of the misrepresentations alleged herein as "forward-looking statements" at the time those representations were made.

302. Furthermore, those representations were not accompanied by meaningful cautionary language identifying important factors that could cause actual results to differ materially from those in the specific statements.

303. To the extent that the statutory safe harbor could apply to any of the misrepresentations pleaded herein, those statements are actionable because, at the time those representations were made, the speaker knew that the particular forward-looking statement was false, and/or the forward-looking statement was made by or with the approval of an executive officer of Winstar who knew that the statement was false or misleading.

COUNT I
(Violation Of § 10(b) Of The Exchange Act Against
the Winstar Defendants and Grant Thornton)

304. Plaintiffs repeat and reallege each of the foregoing allegations as if fully set forth herein. 305. This claim is brought against the Winstar Defendants and Grant Thornton on behalf of Plaintiffs and the Class with respect to the entire Class Period.

306. During the Class Period, the defendants named in this count, individually and in concert, engaged in a plan, scheme and course of conduct, pursuant to which they knowingly and/or recklessly engaged in acts, transactions, practices, and courses of business which operated as a fraud upon Plaintiffs and other members of the Class.

307. The Winstar Defendants and Grant Thornton perpetrated this fraudulent scheme by making various representations that were false or which omitted material facts necessary in order to make the statements, in light of the circumstances under which they were made, not misleading.

308. The Winstar Defendants and Grant Thornton were obligated to supplement and update the disclosures that they made during the Class Period because: (a) they voluntarily made materially misleading statements regarding Winstar's operations and prospects throughout the Class Period; (b) Winstar sold large amounts of securities to the public while the Winstar Defendants were in possession of material, adverse information concerning the Company's operations; and (c) such disclosures were mandated by SEC regulations, including Item 303 of SEC Regulation S-K.

309. The Winstar Defendants and Grant Thornton had actual knowledge that the statements specifically alleged above were materially false and misleading and that additional disclosures were necessary to correct the misleading effect of their statements. In the alternative, the Winstar Defendants and Grant Thornton acted with reckless disregard for the truth in that they failed or refused to ascertain that their optimistic assessments of the Company's business, operations and prospects lacked a reasonable basis when made.

310. As a direct and proximate result of the foregoing material misrepresentations and omissions, the market prices of Winstar common stock and Winstar's publicly traded bonds were artificially inflated throughout the Class Period.

311. In ignorance of the materially misleading and/or incomplete nature of the Class Period representations made by the Winstar Defendants and Grant Thornton, Plaintiffs and other members of the Class relied to their detriment upon the accuracy and completeness of those statements and/or upon the integrity and efficiency of the market for Winstar common stock and Winstar's publicly traded bonds.

312. Plaintiffs and the other members of the Class would not have purchased Winstar securities at the market prices that prevailed during the Class Period, if at all, had they been aware of the true facts concerning the Company's operations and future prospects.

313. The market price of Winstar's common stock and Winstar's publicly traded bonds declined gradually as investors belatedly learned the adverse facts that had been concealed and misrepresented by the Winstar Defendants and Grant Thornton during the Class Period. Plaintiffs and other members of the Class have therefore suffered substantial damages as a direct and proximate result of the misconduct committed by the Winstar Defendants and Grant Thornton.

314. By reason of the foregoing, the Winstar Defendants and Grant Thornton knowingly or recklessly violated Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder in that they: (a) employed devices, schemes and artifices to defraud; (b) made material misrepresentations of fact and failed to disclose material facts necessary in order to make their statements, in light of the circumstances under which they were made, not misleading; or (c) engaged in acts, practices and a course of business that operated as a fraud or deceit upon Plaintiffs and other members of the Class in connection with their purchases of Winstar securities during the Class Period.

315. Plaintiffs and the members of the Class are therefore entitled to damages in an amount to be determined at trial.

COUNT II
(Violations of § 20(a) of the Exchange Act Against The Winstar Defendants)

316. Plaintiffs repeat and reallege the foregoing allegations as if fully set forth herein.

317. This Count is brought against the Winstar Defendants on behalf of Plaintiffs and the Class with respect to the entire Class Period.

318. As is particularized above, during the entire Class Period, the Winstar Defendants were"controlling persons" of the Company within the meaning of § 20(a) of the Exchange Act.

319. The Winstar Defendants qualify as "controlling persons" because they had the power to cause Winstar and the Winstar Defendants to engage in the unlawful conduct complained of herein and because they could have prevented the unlawful conduct that Plaintiffs allege.

320. Because each of the Winstar Defendants is a "controlling person" of Winstar and the other Winstar Defendants, each of whom is a person who has committed violations of Section 10(b) of the Exchange Act, the Winstar Defendants are secondarily liable for those primary violations pursuant to Section 20(a) of the Exchange Act.

COUNT III
(Violations of § 10(b) Of The Exchange Act Against Defendant Lucent)

321. Plaintiffs repeat and reallege the foregoing allegations as if fully set forth herein.

322. This Count is brought against Lucent on behalf of Plaintiffs and the Class with respect to the entire Class Period.

323. During the Class Period, Lucent, individually and in concert with the other Defendants, engaged in a plan, scheme and course of conduct, pursuant to which Lucent knowingly and/or recklessly engaged in acts, transactions, practices, and courses of business which operated as a fraud upon Plaintiffs and other members of the Class. The purpose of the fraudulent scheme in which Lucent participated was to enable Winstar to falsely inflate its financial results throughout the Class Period.

324. In part, Lucent perpetrated this fraudulent scheme by making representations that were false and by failing to disclose material facts necessary in order to make the statements, in light of the circumstances under which they were made, not misleading. Lucent was obligated to supplement and update the disclosures that it made during the Class Period because it voluntarily made materially misleading statements regarding Winstar's operations and the status of Winstar's relationship with Lucent.

325. Lucent had actual knowledge that the statements specifically alleged above were materially false and misleading and that additional disclosures were necessary to correct the misleading effect of their statements and of the fraudulent scheme to falsely inflate Winstar's revenues during the Class Period. In the alternative, Lucent acted with reckless disregard for the truth in that it failed or refused to ascertain that its statements concerning the Company's business and operations lacked a reasonable basis when made and failed or refused to ascertain the existence of the fraudulent scheme alleged by Plaintiffs.

326. As a direct and proximate result of the foregoing material misrepresentations and omissions and the fraudulent scheme in which Lucent participated, the market prices of Winstar common stock and Winstar's publicly traded bonds were artificially inflated throughout the Class Period.

327. In ignorance of the materially misleading and/or incomplete nature of the Class Period representations made by Lucent and Lucent's participation in the fraudulent scheme alleged herein, Plaintiffs and other members of the Class relied to their detriment upon the accuracy and completeness of Lucent's statements and/or upon the integrity and efficiency of the market for Winstar common stock and Winstar's publicly traded bonds.

328. Plaintiffs and the other members of the Class would not have purchased Winstar securities at the market prices that prevailed during the Class Period, if at all, had they been aware of the true facts concerning the Company's operations and future prospects or Lucent's participation in a fraudulent scheme to inflate Winstar's reported revenue.

329. The market price of Winstar's common stock and Winstar's publicly traded bonds declined gradually as investors belatedly learned the adverse facts that had been concealed and misrepresented by Lucent during the Class Period. Plaintiffs and other members of the Class have therefore suffered substantial damages as a direct and proximate result of the misconduct committed by Lucent.

330. By reason of the foregoing, Lucent knowingly or recklessly violated Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder in that it: (a) employed devices, schemes and artifices to defraud; (b) made material misrepresentations of fact and failed to disclose material facts necessary in order to make their statements, in light of the circumstances under which they were made, not misleading; or (c) engaged in acts, practices and a course of business that operated as a fraud or deceit upon Plaintiffs and other members of the Class in connection with their purchases of Winstar securities during the Class Period.

331. Plaintiffs and the members of the Class are therefore entitled to damages in an amount to be determined at trial.

PRAYER FOR RELIEF

WHEREFORE, plaintiffs pray for judgment as follows:

A. An order certifying the Class as set forth herein and designating Plaintiffs as the Class representatives and their counsel as Class counsel;
B. A judgment declaring the conduct of the Defendants to be in violation of law as set forth herein;
C. A judgment awarding Plaintiffs and the other members of the Class compensation for the damages that they have sustained as a result of the Defendants' unlawful conduct, as alleged above;
D. A judgment awarding Plaintiffs' reasonable attorneys' fees, experts' fees, interest and cost of suit; and
E. Such other and further relief as this Court may deem just.

JURY TRIAL DEMANDED

Plaintiff hereby demands a trial by jury.

DATED: March 25, 2002

Respectfully submitted,

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By:______________________________

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