

37

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

JOSEPH A. GANINO, ROBERT E. CREIGHTON,
LOUISE A. CREIGHTON, WILLIAM J. FRAY, THE
ESTATE OF NORMAN GARAND, THE GARAND
FAMILY PARTNERSHIP, A. JOHN KALIL, REZA
NAJAFZEDEH, JEFFREY T. NORTON, REBECCA L
NORTON, JOHN NORTON, MATTHEW NORTON,
LAURA NORTON, ALICE M. TOBIN
and BRANTLEY H. TUDOR, individually, and on
behalf of a class of persons similarly situated,

Plaintiffs,

vs.

CITIZENS UTILITIES COMPANY, LEONARD TOW,
LIVINGSTON E. ROSS, and ROBERT J. DESANTIS,

Defendants.

FILED
DEC 16 11 09 AM '98
CIVIL CASE NO.
398CV00480 (JBA) COURT
NEW HAVEN, CONN.
RMH

JURY TRIAL DEMANDED

December 15, 1998

SECOND AMENDED CLASS ACTION COMPLAINT

Plaintiffs, individually and on behalf of all others similarly situated, by their attorneys,
allege the following for their Second Amended Class Action Complaint.

NATURE OF THE ACTION

1. This is a class action on behalf of all purchasers/acquirors of the common stock
(including Class A and Class B common stock) of Citizens between May 7, 1996 and August 7,
1997, inclusive (the "Class Period"), seeking to pursue remedies under the Securities Exchange
Act of 1934 (the "Exchange Act"). Defendants engaged in a scheme to artificially inflate the
price of Citizens' stock by, among other things, overstating earnings and failing to disclose

2

material, non-recurring income from an investment in Hungarian Telephone and Cable Corp. ("HTCC"), a related party.

FACTUAL BASIS FOR CLAIMS

2. Plaintiffs assert these claims upon information and belief, except for those allegations pertaining to Plaintiffs, which are based on personal knowledge. Plaintiffs' information and belief is based upon an investigation by their counsel and accounting experts, which included a review and analysis of Defendants' public statements (including public filings with the United States Securities and Exchange Commission ("SEC")), published reports and news articles concerning Citizens Utilities Company ("Citizens" or the "Company"), interviews with persons associated with HTCC and knowledgeable about the events and conduct described herein, and internal documents prepared by HTCC and/or the Defendants. Plaintiffs believe that further substantial evidentiary support will exist for the allegations after Plaintiffs have a reasonable opportunity to perform discovery.

JURISDICTION AND VENUE

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

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

5. Venue is proper in this District pursuant to Section 27 of the Exchange Act, and 28 U.S.C. §1391(b). Citizens maintains its principal executive offices in the District, and the acts charged herein, including the preparation and dissemination of materially false and misleading information, occurred in substantial part in this District.

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

THE PARTIES

7. Plaintiffs Joseph A. Ganino, Robert E. Creighton, Louise A. Creighton, William J. Fray, The Estate of Norman Garand, The Garand Family Partnership, A. John Kalil, Reza Najafzadeh, Jeffrey T. Norton, Rebecca L. Norton, John Norton, Matthew Norton, Laura Norton, Alice M. Tobin and Brantley H. Tudor purchased and/or acquired Citizens common stock at artificially inflated prices during the Class Period and have been damaged thereby.

8. Defendant Citizens is a Delaware corporation with its principal executive offices at High Ridge Park, Stamford, Connecticut 06905. Citizens describes itself as a diversified communications and public services company which provides either directly or through subsidiaries, telecommunications, electric transmission and distribution, natural gas transmission and distribution, water distribution and wastewater treatment services to customers in twenty-two (22) states.

9. The individual Defendants identified below served, at all times material to the claims set forth herein, as senior officers of Citizens in the positions set forth (the "Individual Defendants"):

a. Leonard Tow ("Tow") was Chairman of the Board of Directors, Chief Executive Officer and Chief Financial Officer of the Company throughout the Class Period. Tow was a signatory to the Company's 1996 annual report filed with the SEC on Form 10-K, more particularly described below.

b. Robert J. DeSantis ("DeSantis") was Vice President and Treasurer of the Company throughout the Class Period.

c. Livingston E. Ross ("Ross") was Vice President and Controller of the Company throughout the Class Period. Ross was a signatory to (1) the Company's 1996 annual report filed with the SEC on Form 10-K, more particularly described below and (2) the Company's quarterly reports filed with the SEC on Form 10-Q for the fiscal quarters ended March 31, 1996, June 30, 1996 and September 30, 1996, more particularly described below.

d. The Individual Defendants participated in the day-to-day management of the Company at the highest levels and participated in the drafting, preparation, and/or approval of the various public shareholder and investor reports and other communications complained of herein. As a result, it is appropriate to treat the Individual Defendants as a group for pleading purposes and to presume that the materially false, misleading and incomplete information conveyed in the Company's public filings, press releases and other publications as alleged herein are the collective actions of this narrowly defined group of Defendants.

e. The Individual Defendants, as the chief financial officers of the Company, had access to the adverse undisclosed information described herein through access to internal corporate documents and were aware of or recklessly disregarded the misstatements contained therein and omissions therefrom, and were aware of their materially false and misleading nature. The Individual Defendants each had a duty to disseminate promptly accurate and truthful information with respect to the Company's business, operations, results and financial condition and to correct any previously-issued statements that had become materially misleading or untrue, so that the market price of the Company's publicly-traded securities would be based upon truthful and accurate information.

f. Because of their executive and managerial positions with Citizens, and their authority with respect to the financial statements and financial reporting of the Company, each of the Individual Defendants had the power to influence and control, and did control, the actions of the Company, including the content of the various SEC filings, press releases and other public statements pertaining to the Company during the Class Period which are at issue in this action. Accordingly, each of the Individual Defendants is liable as a control person to the extent that the Company is liable for any of the claims brought in this action.

10. Each of the Defendants is liable as a participant in a fraudulent scheme and course of business that operated as a fraud or deceit on purchasers of Citizens common stock, by disseminating materially false and misleading statements and/or concealing material adverse facts. The scheme deceived the investing public regarding Citizens' business, operations, results and financial condition and caused Plaintiffs and other members of the Class to purchase Citizens common stock at artificially inflated prices.

CLASS ACTION ALLEGATIONS

11. Plaintiffs bring this action as a class action pursuant to Rules 23(a) and (b)(3) of the Federal Rules of Civil Procedure on behalf of a Class consisting of all persons who purchased/acquired Citizens common stock between May 7, 1996 and August 7, 1997, inclusive (the "Class Period") and who were damaged thereby, excluding Defendants, the officers and directors of the Company, members of the Defendants' immediate families, Defendants' legal representatives, heirs, successors or assigns and any entity in which Defendants have or had a controlling interest (the "Class").

12. The members of the Class are so numerous that joinder of all members is impracticable. While the exact number of Class members is unknown to Plaintiffs at this time and can only be ascertained through appropriate discovery, Plaintiffs believe that there are hundreds or thousands of members of the proposed Class. As of April 29, 1997, Citizens reported that it had at least 156.3 million shares of Citizens' Class A common stock outstanding and at least 86.1 million shares of Citizens' Class B common stock outstanding. Throughout the Class Period, Citizens' common stock was actively traded on the New York Stock Exchange.

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

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

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

- a. Whether the federal securities laws were violated by Defendants' acts, as alleged herein;
- b. Whether statements made by Defendants to the investing public during the Class Period misrepresented material facts about the business and financial statements of Citizens;
- c. Whether the Individual Defendants are controlling persons of the Company within the meaning of Section 20 of the Exchange Act;
- d. Whether the market price of the Company's common stock was artificially inflated during the Class Period due to the material misrepresentations described herein; and
- e. To what extent the members of the Class have sustained damages and the proper measure of damages.

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

17. There will be no difficulty in the management of this action as a Class Action. Record owners and other members of the Class may be identified from records maintained by

Citizens or its transfer agent and may be noticed of the pendency of this action by mail, using the form of notice similar to that customarily used in securities class actions.

**APPLICABILITY OF PRESUMPTION OF RELIANCE
AND FRAUD-ON-THE-MARKET DOCTRINE**

18. At all relevant times, the market for Citizens stock was an efficient market for the following reasons:

- a. Citizens common stock met the requirements for listing, and was listed and actively traded on the New York Stock Exchange, a highly efficient and automated market;
- b. As a regulated issuer, Citizens filed periodic public reports with the SEC and the New York Stock Exchange;
- c. Citizens regularly communicated with public investors via established market communication mechanisms, including through regular disseminations of press releases on the national circuits of major newswire services and through other wide-ranging public disclosures, such as communications with the financial press and other similar reporting services; and
- d. Citizens was followed by securities analysts employed by major brokerage firms, including Merrill Lynch Pierce Fenner & Smith and Salomon Brothers Inc., which wrote reports which were distributed to the sales force and certain customers of their respective brokerage firms. Each of these reports was publicly available and entered the public marketplace.

19. The market for Citizens common stock digested current information regarding Citizens from the sources described above and reflected such information in Citizens' stock price. Under these circumstances, all purchasers of Citizens shares during the Class Period suffered similar injury through their purchase of shares at artificially inflated prices and a presumption of reliance applies.

SUBSTANTIVE ALLEGATIONS

20. Hungarian Telephone and Cable Corp. ("HTCC") is a U.S. company formed in 1992, which has sought to act as a provider of basic telephone services in five defined regions within the Republic of Hungary, pursuant to 25-year telecommunications concessions (the "Concession Contracts") granted by the Hungarian government.

a. HTCC acquired its concession rights from the Hungarian Ministry of Transportation, Telecommunications and Water Management (the "Ministry") and purchased existing telecommunications infrastructures, including approximately 60,000 access lines, from Magyar Tavkozlesi Rt. ("MATAV"), the formerly State-controlled monopoly telephone company.

b. Pursuant to the Hungarian Telecom Act and in accordance with the Concession Act of 1991, in connection with the award of a concession, each of the Local Telephone Operators (the "LTO's") entered into a Concession Contract with the Ministry governing the rights and obligations of the LTO with respect to each concession. Each of the Concession Contracts incorporates build-out milestones requiring 15.5% per year increases in installed access lines. In addition, as of January 1, 1997, in the case of Kelet-Nograd Com Rt.

("KNC") and Raba Com. Rt. ("Raba-Com") and by January 1, 1998, in the case of Hungarotel Tavkozlesi Rt. ("Hungarotel") and Papa es Tersege Telefon Koncesszios Rt. ("Papatel"), each of these operating companies (each a subsidiary of HTCC) would be required to meet 90% of its wait-listed demand within six months and 98% of such demand within one year.

c. The failure to meet build-out milestones were subject to the imposition of fines, the shortening of the exclusivity period provided by the Concession Contracts, or the levying of fines by the Ministry. Such fines are computed based on a contractual formula and may be substantial.

d. If an LTO is unable to comply with its Concession Contracts, the Ministry has the right to abrogate the Concession Contract. In such an instance, the Ministry has authority to determine alternative provisions for such service, which may include the sale of the LTO's telecommunications assets to another provider. In such case, the LTO would be obligated to sell its assets under the terms of a contract to the provider to whom the concession is transferred.

21. As of 1995, HTCC had been unprofitable since inception, had a substantial accumulated deficit, and did not have the funds required to fulfill the milestones under the Concession Contracts described above. Therefore, in 1995, HTCC began looking for a source of financing.

22. As of 1995, Citizens had reported 50 consecutive years of increased revenue, earnings and earnings per share, which was touted by Citizens in its public comments. It was important to the management of Citizens to continue that trend. As a result, Citizens was looking for a way to enhance Citizens' earnings. Taking de facto control of HTCC was the solution.

23. Beginning in May 1995, Citizens and HTCC entered into a series of agreements under which Citizens funded HTCC's construction costs and other construction-related obligations under the Concession Contracts. During 1995, Citizens, through CU Capital Corp ("CUCC"), a wholly-owned subsidiary, loaned HTCC significant amounts of money and guaranteed HTCC obligations.

a. The initial loan agreement between Citizens and HTCC provided for an initial advance by CUCC of up to \$4,300,000 to fund certain obligations pertaining to Concession Contracts in Hungary, and a possible second advance of up to an additional \$910,000 to fund the repayment for certain loans to HTCC from Teleconstruct (a company affiliated with HTCC). Approximately \$1,888,000 was advanced by CUCC on July 25, 1995 to fund certain of HTCC's obligations.

b. As disclosed by Citizens in its Form 10-Q for the quarterly period ended September 30, 1995, on September 28, 1995, HTCC and Citizens entered into an agreement pursuant to which Citizens agreed to provide up to \$33,200,000 of additional interim financial support.

c. On October 9, 1995, CUCC provided a letter of support to Citibank, which Citibank required as a condition to issuing a payment guarantee to Matav to secure HTCC's obligation to pay \$925,000 to Matav on or before December 1, 1995, as the purchase price for the shares in Papatel that HTCC purchased from MATAV.

d. On October 19, 1995, CUCC advanced \$2,800,000 to HTCC to enable HTCC to make loans to KNC and Raba-Com.

e. CUCC advanced further large amounts to HTCC, including approximately \$8,000,000 on November 6, 1995. On November 8, 1995, concession fees of approximately \$7,055,000 were paid by Papatel and Hungarotel with funds borrowed by HTCC from CUCC.

f. As of December 31, 1995, HTCC had received \$30.7 million pursuant to the financial support arrangement with Citizens and had requested an additional \$2.5 million.

24. Throughout the relationship with HTCC, Citizens engaged in actions which were designed to ensure that Citizens maintained control over HTCC and reported earnings from its relationship with HTCC, including but not limited to, the following:

a. At the time that Citizens entered into the agreement with HTCC in mid-1995, Citizens intended to acquire HTCC in approximately two years (i.e., by 1997) if HTCC proved to be profitable, and Citizens structured its transactions with HTCC to that end, including acquiring options to purchase over 50% of the stock of HTCC and protection against dilution for two years (i.e., until September 1997). However, Citizens was advised by its auditors, KPMG Peat Marwick ("KPMG"), that if Citizens was deemed to control HTCC, Citizens would be required by Generally Accepted Accounting Principles ("GAAP") to report its financial results on a consolidated basis with those of HTCC under principles of "equity accounting". As Citizens expected that HTCC would report substantial losses for 1995 and 1996 and did not want to include those losses as part of Citizen's financial statements, Citizens tried to make it appear that it did not control HTCC. As KPMG informed Citizens that Citizens would be presumed to be in control (and subject to equity accounting) if Citizens owned 20% of the stock of HTCC or had two board members, Citizen's agreement with HTCC provided that Citizens would select

one board member and own less than 20% (and receive options to increase its ownership interest to over 50%).

b. Citizens arranged for HTCC to replace its auditor, BDO Seidman, with KPMG, which also took place in mid-1995.

c. On September 12, 1995, HTCC submitted to its shareholders and had approved the agreement with Citizens, which provided a management fee of 5% of gross revenues or \$2.5 million, whichever was higher. On September 14, 1995, two days later, Citizens informed HTCC that it was increasing its minimum management fee to \$5 million from \$2.5 million, and that if HTCC did not immediately agree, Citizens would walk away from its commitment to fund HTCC.

d. Due to its need for immediate funds, HTCC believed that it had no choice but to agree to Citizens' increased fee or lose the financing and jeopardize the viability of HTCC. HTCC told Citizens (including Don Robertson, a Citizens' senior executive who, at Citizens' direction, was made a director of HTCC and acted as a senior consultant to HTCC in Hungary during late 1995 and early 1996), that HTCC believed that the increased fee was improper and that HTCC was pursuing legal claims; Robertson and Citizens were aware that HTCC had contacted legal counsel in New York, who had prepared a lengthy complaint against Citizens which HTCC intended to file after take-out financing was arranged (i.e., from a source other than Citizens).

e. Citizens also billed HTCC additional excessive and unjustified amounts for services which were required to be provided as consideration for the management fee. For example, Citizens billed for the salary and other expenses of various employees of Citizens who

provided any assistance to HTCC, including Mr. Robertson, for whom Citizens billed HTCC \$800,000 for a portion of the six months that he was assigned by Citizens to work part-time with HTCC.

f. Although HTCC refused to voluntarily pay charges for "management services" and "reimbursement of expenses", and HTCC took the position that Citizens was not entitled to the entire amount of the fees and reimbursements billed, Citizens obtained payment for amounts billed in 1995 and early 1996 from its own loans to HTCC and from Citicorp as part of the closing of bridge financing obtained by HTCC in March 1996, which could not have taken place without Citizens' assistance.

g. Following the closing of the March 1996 financing from Citicorp, HTCC intended to terminate the relationship with Citizens and to cease further payment of the excessive and unjustified fees and "expenses" which Citizens was billing to HTCC. Mr. Robertson left the employ of Citizens and became employed directly by HTCC. Mr. Robertson and Robert Genova, the chairman of HTCC, expressed to Citizens HTCC's dissatisfaction with Citizens' excessive and unjustified billings of fees and also expressed that HTCC was not satisfied with the junk bond financing which Citizens was recommending as long-term financing for HTCC. In response to this expression of independence by members of HTCC management, Citizens arranged for Citicorp to send a letter to HTCC demanding that it replace management; several top members of management, including Mr. Genova and Mr. Robertson, were given severance packages totaling over \$7 million, which was to be funded by HTCC, and involved the issuance of a letter of credit by Citicorp which was guaranteed by Citizens. At the "suggestion" of Citizens, three "independent" directors were placed on the board of directors of HTCC, including

David Finley, a summer neighbor of Defendant Tow on Martha's Vineyard, as Chairman of the Board.

h. Despite the continued efforts by Citizens to strengthen its control over HTCC, and the attempts to have HTCC conclude the junk bond financing, HTCC arranged for a \$170,000,000 financing facility from Postabank, a Hungarian bank, and informed Citizens and Citicorp that Postabank would be the final lender. Realizing that it might not receive any additional funds from HTCC, Citizens thereupon arranged to "assist" in the transaction by providing a letter of comfort (but not a guarantee), and Citizens had Citicorp arrange with Postabank to pay Citizens \$5.1 million in claimed past due management fees and reimbursement of expenses from the proceeds of the new financing. Thereafter, at the urging of Finley and others who were under the control of Citizens, HTCC agreed to re-price certain options to purchase HTCC stock held by Citizens as a means of compensating Citizens without any cash being used and with the understanding that HTCC would thereafter not pay the exorbitant fees and expenses to Citizens.

i. After October 1996, despite the fact that HTCC refused to pay further amounts to Citizens, Citizens continued to bill HTCC, and Citizens continued to recognize revenue and earnings from the management fees and reimbursement of supposed expenses throughout the remainder of the Class Period and thereafter (which amounts had reached approximately \$5 million by the end of the Class Period and approximately \$7 million by the end of 1997). In 1997, HTCC was advised by legal counsel that HTCC was not obligated for the amounts billed by Citizens and that Citizens would owe some amounts to HTCC. In 1998, HTCC and Citizens both disclosed their disagreement. Citizens has taken a reserve for certain of

the amounts recognized in 1998 as income under the management agreement, but it has not reserved for any amounts accrued as earnings in prior periods.

25. Citizens disclosed certain aspects of its relationship with HTCC. For example, Citizens announced an agreement in principal in May 1995 and filed certain agreements with the SEC, and Citizens' Form 10-Q for the quarterly period ended June 30, 1995, which was filed with the SEC on or about August 14, 1995 (the "1995 Second Quarter 10-Q"), stated:

On May 31, 1995, the Company entered into definitive agreements with Hungarian Telephone and Cable Corp. ("HTCC"), a Delaware corporation, which generally provide certain rights for the Company to purchase shares of up to 51% of HTCC common stock; being granted certain registration rights with respect to HTCC common stock now owned or that may be acquired; providing certain management services on a cost-plus basis; and having the right to designate one member of the HTCC Board of Directors. On May 31, 1995, the Company also acquired 300,000, or 10% of HTCC common shares for \$4,200,000. HTCC presently controls the rights to own, operate and expand certain telecommunications services to the Sarvar and Salgotarjan areas of Hungary. On July 25, 1995, the company made a secured loan to HTCC in the amount of \$1,887,000.

26. Citizens' Form 10-K for the fiscal year ended December 31, 1995 (the "1995 Form 10-K"), which was filed with the SEC on or about March 6, 1996, stated:

In 1995, the Company made a \$4,200,000 investment in and entered into definitive agreements with Hungarian Telephone and Cable Corp. ("HTCC"), a Delaware corporation. Pursuant to these agreements (i) the Company has rights to purchase up to 54% of HTCC common stock, (ii) provides certain management services to HTCC on a cost-plus basis, (iii) has the right to and has designated one member of the HTCC Board of Directors, and (iv) has provided

HTCC with guarantees and financial support. HTCC presently controls the rights to own, operate and expand certain telecommunications services in certain regions of Hungary. The management services fee payable by HTCC to the Company is the greater of 5% of adjusted gross revenues of HTCC or a monthly fixed amount. In addition, expenses incurred by the Company in providing such services, including certain allocable overhead items, are to be reimbursed by HTCC. A subsidiary of the Company is the guarantor of a \$33,200,000 bank loan to HTCC. The Company has agreed to provide HTCC with up to \$20,000,000 of additional financial support. The Company has been compensated for such guarantees and financial support. The Company's investment in HTCC is accounted for using the cost method of accounting.

27. On February 26, 1996, HTCC and Citizens entered into a new loan agreement, pursuant to which Citizens agreed to lend HTCC up to \$46.0 million (in addition to \$33.2 million of financial support previously provided by Citizens). This \$46.0 million included an advance of up to:

a. \$16.0 million to enable HTCC to satisfy its obligations to Citibank, N.A. if Citibank, N.A.'s payment obligations to Matav arose pursuant to its payment guaranty to secure HTCC's asset purchase.

b. \$30.0 million, composed of up to \$20.0 million for certain limited purposes and up to \$10.0 million reserved for anticipated obligations under construction contracts to be approved by Citizens.

In connection with its financial support arrangement, Citizens loaned HTCC a total of \$18,200,000 during February/March 1996.

28. On March 29, 1996, HTCC entered into a \$75 million bridge loan with Citicorp North America, Inc. ("CNA"). In connection therewith, CUCC or an affiliate thereof provided a non-binding comfort letter to CNA.

29. On October 15, 1996, HTCC entered into a \$170 million 10-year Multi-Currency Credit Facility with Postabank, a Hungarian bank, to fund further construction activities. Approximately \$5.1 million of the proceeds from the Loan was used to pay management fees and reimbursable costs to Citizens.

THE MATERIAL MISREPRESENTATIONS

Failure To Disclose Material Facts About The Relationship With HTCC

30. Although Citizens disclosed the right to purchase up to 51% of HTCC's stock in the future and the right to designate one member of HTCC's board, Citizens failed to disclose from the inception of its relationship with HTCC and throughout the Class Period many material facts concerning its relationship, including but not limited to the facts that Citizen was able to, and did, exercise control over HTCC and was a related party of HTCC by virtue of its control over the financial survival of HTCC as set forth in Paragraph 24 above, and that Citizens' transactions with HTCC were therefore not at arms' length. The following additional undisclosed facts, among others, individually and in the aggregate establish that HTCC was a related party to Citizens and under the control of Citizens:

a. Although Citizen disclosed that it had designated a board member of Hungarian, Citizen did not disclose that that board member, Donald K. Robertson ("Robertson"), who had been the head of the telecommunications division of Citizens, was

reassigned to spend most of his time working at and effectively operating HTCC, for which HTCC was charged approximately \$800,000 by Citizens.

b. Certain voting agreements were entered into with the principal stockholders of HTCC (Robert Genova, Frank R. Cohen, and Peter E. Klenner) which provided that Robert Genova, Frank R. Cohen, and Peter E. Klenner would vote their shares of common stock for (a) the approval of the stock option agreement and the stock options, (b) "in favor of any persons designated by CUCC and nominated by the HTCC Board at any time to serve on the HTCC Board at every meeting of the shareholders of HTCC at which such an election is held and at every adjournment thereof," and (c) "against any merger, consolidation, business combination, sale of significant amount of assets . . . unless CUCC consents in writing to a vote in favor of any such transaction"

c. Citizens recognized millions of dollars of income from HTCC purportedly for providing services which Citizens did not provide. Although the management contract into which Citizens and HTCC had entered provided for Citizens or its subsidiary to provide services (corporate, financial, accounting, treasury, information management, legal, contract, human resource, public relations, marketing, sales, customer billing and collection, engineering, procurement, land and building, fleet maintenance, equipment repair, measurement, regulatory planning and rate case management, settlement, technical, construction, and operational) to HTCC and its subsidiaries, Citizens failed to provide many of those services or billed substantial additional amounts that were not subject to additional compensation under the management contract.

d. The agreements, taken as a whole, enabled Citizens to effectively control all of the significant acquisition, development, construction, and operating activities of HTCC.

31. In addition to failing to disclose that Citizens exercised control over HTCC and that HTCC was a related party, Citizens misled the investing public by stating that Citizens' investment in HTCC was accounted for using the "cost method" of accounting, while Citizens knew from its discussions with KPMG that such accounting was only appropriate if, and therefore constituted a representation that, there were no control relationship.

Misrepresentations (Overstatement) of Earnings

32. Citizens misleadingly recognized and overstated pre-tax income (revenue for which there was no corresponding expense) in its financial statements from the securities and cash which it had received as purported consideration for its relationship with HTCC, and Citizens (i) failed in its interim period filings on Form 10-Q to disclose that the income was from HTCC, (ii) failed in all filings to disclose that the income was from non-recurring sources, (iii) failed to disclose that these unusual one-time injections of earnings were substantially non-cash in nature and derived through transactions with a related party, (iv) failed to disclose that the income included accruals for management fees and reimbursement of expenses for which Citizens had not performed adequate services, and (v) failed to disclose that the income was purposely recognized pursuant to contrived transactions in periods which would enable Citizens to meet earnings targets.

33. On May 7, 1996, Citizens announced earnings of \$38.9 million for the quarter ended March 31, 1996, up 15% from \$33.9 million for the first quarter of 1995, reporting:

[Defendant] Tow announced that these results indicate Citizens is well on its way toward its 52nd consecutive year of increased revenues, net income and earnings per share, a record unequaled by any other publicly traded company in the United States. "These record results," Dr. Tow said, "reflect strong earnings growth in all business sectors."

The report also attributed to Defendant DeSantis the statement that the "first quarter results reflect Citizens' return to strong increases in earnings and earnings per share." These "record results" were also reflected in Citizens' Form 10-Q for the quarterly period ended March 31, 1996, which was filed with the SEC on or about May 14, 1996 (the "1996 First Quarter 10-Q").

34. The May 7, 1996 announcement and the 1996 First Quarter 10-Q were materially misleading in at least the following respects:

a. Defendants included no disclosure with respect to HTCC, and Defendants failed to disclose that the \$38.9 million in reported income included a material amount from HTCC, including as much as \$6.9 million from alleged income from loan activities and approximately \$625,000 in management fees and reimbursement;

b. Defendants failed to disclose that the reported income included a material amount that was non-recurring;

c. Defendants failed to disclose that the reported income included a material amount of earnings that were substantially non-cash in nature and derived through transactions with a related party,

d. Defendants failed to disclose the controlling or "related party" nature of the relationship between Citizens and HTCC or the material facts set forth above which establish the related party and controlling nature of Citizens' relationship with HTCC.

e. Defendants failed to disclose that the income was materially inflated by accruals for management fees and reimbursement of expenses for which Citizens had not performed adequate services; and

f. Defendants failed to disclose the material fact that as much as \$6.9 million of the \$38.9 million of reported income for the first quarter was HTCC related income which was deceptively "stored" by Citizens and was recognized in the first quarter of 1996 solely in order to permit Citizens (i) to reach targets for earnings set by analysts and (ii) to show an increasing amount of earnings compared to prior periods. Although this income related primarily, if not entirely, to amounts loaned and guaranteed in 1995, all the securities received as compensation for the loans and guarantees were received by Citizens in 1995, Citizens deferred recognizing any of this non-recurring income in 1995 to avoid making it difficult or impossible for 1996 to be a year of further increased earnings and recognized this "income" in the first quarter of 1996 because (i) the consensus estimates by Merrill Lynch and other analysts of 17 - 18 cents per share were met only as a result of this additional HTCC income and (ii) a substantial portion, if not all, of the increase in income for the first quarter of 1996 compared to the first quarter of 1995 was due to the income recognized from HTCC.

35. In a press release dated August 15, 1996, in which the Company announced "record . . . profits for the three- and six-month periods ended June 30, 1996", Citizens reported:

Net income of \$46.3 million for the second quarter grew 10% over net income of \$41.9 million for the same period last year and grew at an accelerated rate of 19% over first-quarter 1996 net income of \$38.9 million. Earnings per share of 20 cents for the second quarter increased 11% from 18 cents for the corresponding 1995 quarter and grew at the rate of 18% when compared to first quarter 1996 earnings per share of 17 cents. For the six months ended June 30th, DeSantis reported that . . . [n]et income of \$85.1 million increased 12% over net income of

\$75.8 million during the same period last year. Earnings per share of 37 cents for this period was also up 12% over earnings per share of 33 cents during the corresponding period in 1995. Commenting on these financial results, DeSantis said, "Citizens' excellent performance is attributable to continuous above-average growth in volume and profitability in each of its sectors, particularly telecommunications. Such growth has enabled the company to increase its cash flow by 53% to \$150 million for the first six months of 1996."

(emphasis added). These financial results were also reflected in Citizens' Form 10-Q for the quarterly period and six months ended June 30, 1996, which was filed with the SEC on or about August 14, 1996 (the "1996 Second Quarter 10-Q").

36. The August 15, 1996 announcement and the 1996 Second Quarter 10-Q were materially misleading in at least the following respects:

- a. Defendants included no disclosure with respect to HTCC, and Defendants failed to disclose that the \$46.3 million in reported income for the second quarter included a material amount from HTCC and that the \$85.1 million in reported income for the six months ended June 30, 1996 included no less than approximately \$10 million in financial support fees from HTCC and no less than approximately \$1.4 million in management fees from HTCC;
- b. Defendants failed to disclose that the reported income included a material amount that was non-recurring;
- c. Defendants failed to disclose that the reported income included a material amount of earnings that were substantially non-cash in nature and derived through transactions with a related party;
- d. Defendants failed to disclose the controlling or "related party" nature of the relationship between Citizens and HTCC or the material facts set forth above which establish the related party and controlling nature of Citizens' relationship with HTCC.

e. Defendants failed to disclose that the income was materially inflated by accruals for management fees and reimbursement of expenses for which Citizens had not performed adequate services; and

f. Defendants failed to disclose the material fact that approximately \$10 million of the \$85.1 million of reported income for the six months ended June 30, 1996 was HTCC related income which was deceptively “stored” by Citizens and was recognized during the first half of 1996 solely in order to permit Citizens (i) to reach targets for earnings set by analysts and (ii) to show an increasing amount of earnings compared to prior periods. This \$10 million of income derived at least in significant part from securities received by Citizens from HTCC in 1995 relating to Citizens’ interim loan guarantees and financial support to HTCC in 1995. The consensus estimates by Merrill Lynch and other analysts for income for the first six (6) months of 1996 were met and exceeded only as a result of this additional HTCC-related income, and the increase in income for the first six months of 1996 compared to the first six months of 1995 was due entirely to the income recognized from HTCC.

37. The misrepresentations in the disclosures of income for the periods ending March 31, 1996 and June 30, 1996 were even more misleading because the Company’s 1995 10-K filed with the SEC (the “1995 10-K”) stated that Citizens “has been compensated for such guarantees and financial support [provided by Citizens to HTCC]”, thus inferring that any income for the 1995 loan and guarantee transactions had already been recognized in 1995. In this regard, Accounting Principles Board Opinion No. 28 states:

There is a presumption that users of summarized interim financial data will have read the latest published annual report, including the financial disclosures required by generally accepted accounting principles and management’s commentary

concerning the annual financial results, and that the summarized interim financial data will be viewed in that context.

Management neglected their responsibility to correct the misleading inference which was created by the 1995 10-K.

38. In a press release dated November 12, 1996, the Defendants announced the Company's earnings and earnings per share for the three and nine-month periods ended September 30, 1996, which Defendant DeSantis characterized as a "strong performance". Defendants represented in this press release that for the third quarter, excluding certain charges, net income for the period increased 21% to \$54.3 million. Defendants further represented in this press release that excluding certain charges, for the nine months ended September 30, 1996, net income grew to \$139.5 million, a 15% increase. These financial results were also reflected in Citizens' Form 10-Q for the quarterly period and nine months ended September 30, 1996, which was filed with the SEC on or about November 13, 1996 (the "1996 Third Quarter 10-Q").

39. The November 13, 1996 announcement and the 1996 Third Quarter 10-Q were materially misleading in at least the following respects:

a. Defendants included no disclosure with respect to HTCC, and Defendants failed to disclose that the \$139.5 million in reported income for the first nine months of 1996 included no less than approximately 10.1 million in financial support fees from HTCC and no less than \$2.4 million in management fees;

b. Defendants failed to disclose that the reported income included a material amount that was non-recurring;

c. Defendants failed to disclose that the reported income included a material amount of earnings that were substantially non-cash in nature and derived through transactions with a related party,

d. Defendants failed to disclose the controlling or "related party" nature of the relationship between Citizens and HTCC or the material facts set forth above which establish the related party and controlling nature of Citizens' relationship with HTCC; and

e. Defendants failed to disclose that the income was materially inflated by accruals for management fees and reimbursement of expenses for which Citizens had not performed adequate services.

40. On March 16, 1997, Defendants issued a press release disclosing earnings of \$47.5 million for the fourth quarter of 1996 (20 cents per share), and \$178.7 million for the whole of fiscal 1996 (77 cents per share), which were precisely in line with forecasts previously issued by Merrill Lynch and other analysts. The press release reported:

[Defendant] DeSantis said "Citizens' financial performance for 1996 was exceptional across the board". . . . Mr. DeSantis said that Citizens 1996 record results represented the Company's 52nd consecutive year of increased revenue, earnings and earnings per share.

41. Citizens' Form 10-K for the fiscal year ended December 31, 1996 (the "1996 Form 10-K"), which was filed with the SEC on or about March 17, 1997, confirmed these financial results and stated:

In 1995, the Company made a \$4,200,000 investment in and entered into definitive agreements with Hungarian Telephone and Cable Corp. ("HTCC"), a Delaware corporation, which owns and operates local telephone concessions in Hungary. Pursuant to these agreements, as amended, (i) the Company has rights to

purchase up to 58% of HTCC common stock, (ii) provides certain management services to HTCC on a cost-plus basis, (iii) has the right to and has designated one member, out of seven, of the HTCC Board of Directors, and (iv) provided HTCC with guarantees and financial support. The management services fee payable by HTCC to the Company is the greater of 5% of adjusted gross revenues of HTCC or a monthly fixed amount. In addition, expenses incurred by the Company in providing such services, including certain allocable overhead items, are reimbursed by HTCC. The Company has been compensated for all guarantees and financial support which it has provided to HTCC. The Company's investment in HTCC is accounted for using the cost method of accounting.

RONALD E. SPEARS has been associated with the Registrant since June 1995 and has been Vice President, Telecommunications since that date . . . He is currently a Director of Hungarian Telephone and Cable Corp.

The increase in investment income in 1996 is primarily due to \$22 million earned from Hungarian Telephone and Cable Corp. for guarantees and financial support provided by the Company.

42. Citizens' March 16, 1997 press release and 1996 Form 10-K were materially misleading in at least the following respects:

a. Defendants failed to disclose that the Company had included in income for 1996 a material amount derived from the value of stock and options received in 1995 from HTCC for the loan guarantees and support provided by Citizens in 1995, which income was represented by Defendants to have been earned in 1995.

b. Although Citizens had disclosed the "investment" in HTCC and implied that the investment was continuing, Defendants failed to disclose that the \$22 million recognized as investment income from HTCC was a non-recurring related party source of income, and that the investment income was not likely to continue.

c. Although Citizens represented that the \$22 million from HTCC had been "earned", Citizens had not earned most of that amount because it had not performed the requisite services, or because the services for which it billed HTCC in addition to the management fee were required to be included as part of the management fee pursuant to the terms of the management agreement.

d. Defendants failed to disclose the controlling or "related party" nature of the relationship between Citizens and HTCC or the material facts set forth above which establish the related party and controlling nature of Citizens' relationship with HTCC.

e. Defendants failed to disclose that the income was materially inflated by accruals for management fees and reimbursement of expenses for which Citizens had not performed adequate services; and

f. Defendants failed to disclose that the reported income of \$47.5 million for the fourth quarter of 1996 included a material amount of income attributable to transactions with HTCC, including approximately \$11.2 million for options issued and extended by HTCC, \$750,000 for a fee for various purported services and no less than \$1.1 million for purported management services.

43. On April 30, 1997, the Company issued a press release announcing its earnings for the first quarter of 1997, the period ending March 31, 1997. The Company reported net

income for the first quarter of \$30.2 million compared with net income of \$38.9 million for the same period in the prior year. The reported earnings of 13 cents per share were lower than the estimates by Merrill Lynch and other analysts. The Company failed to disclose that the decrease in earnings was due in substantial part to the decrease in income reported from HTCC compared to the first quarter of 1996; instead, the press release misleadingly focused only on increased expenses.

44. On or about May 1, 1997, Citizens filed a Form 10-Q with the SEC for the first quarter of 1997 (the "1997 First Quarter 10-Q"). The 1997 First Quarter 10-Q was signed by Defendant Ross and confirmed previously announced financial results but contained no disclosures with respect to HTCC or the investment in HTCC.

45. The April 30, 1997 press release and the 1997 First Quarter 10-Q failed to disclose the facts set forth above regarding the extent of Citizens' business transactions with HTCC and the fact that as of March 31, 1997, Citizens' balance sheet reflected a receivable of approximately \$2.8 million purportedly attributable to reimbursable management costs and management fees accrued under the management services agreement.

46. On or about May 5, 1997, S&P lowered its long-term debt rating on the Company to "Negative" from "Stable". A May 5, 1997 Business Wire release indicated that the change in the rating stemmed in part from Citizens' earnings weaknesses. This Business Wire release also indicated that continuation of these trends would weaken Citizens' very strong financial and business position, resulting in some reduction in credit quality.

47. On May 13, 1997, Merrill Lynch released a research report which reported on the earnings reported by Citizens, mentioned the investment in HTCC, and stated that "the additional

earnings estimate reductions relate to a lowering of [Merrill Lynch's] expectations for other income."

48. The expectation of lower earnings for "other income", which included the income derived from HTCC, was confirmed on August 7, 1997, the date on which Citizens filed with the SEC the Company's Form 10-Q for the quarterly period ended June 30, 1997 (the "Second Quarter 10-Q"), in which the Defendants disclosed that:

Investment income for the second quarter and six months ended June 30, 1997 decreased \$5.3 million, or 38%, and \$4.2 million, or 19%, respectively, as compared with the prior year periods primarily due to income earned in 1996 for financial support provided to Hungarian Telephone and Cable Corporation.

This disclosure also confirmed that the reported income for the first and second quarters of fiscal 1996 had included material income derived from HTCC.

49. Throughout the Class Period, Defendants' misrepresented (overstated) earnings from management fees and reimbursement of expenses, including but not limited to billing of HTCC (i) \$342,139.22 for Citizens personnel (at an average cost of \$445.99 per hour) for the period October 1996 through June 1997, (ii) \$109,092.02 for 200 hours of Defendant Tow's time during 1996, and (iii) \$131,822.51 for miscellaneous out-of-pocket costs for the period October 1996 through June 1997, which included such costs as \$15,735.50 for tickets for Defendant and Mrs. Tow to travel to London on the Concorde.

Misrepresentations That The Financial Statements Were In Compliance With GAAP

50. Regulation S-X provides that financial statements filed with the SEC which are not in accordance with GAAP are presumed to be materially misleading.

51. Citizens' financial statements, as contained in publicly disseminated documents throughout the Class Period, were materially false and misleading in that they constituted a substantial departure from GAAP, as set forth below.

52. Throughout the Class Period, Citizens disseminated financial statements which failed to disclose the fact that it was an active and controlling owner/investor in HTCC, that HTCC was a related party, and that Citizens had recognized material amounts of income on transactions with the related party. In this regard, Citizens issued financial statements which failed to provide related party disclosures required by GAAP and constituted a substantial departure from GAAP.

a. GAAP, contained in authoritative accounting literature (FASB No. 57), provides that related parties includes:

parties with which the enterprise may deal if one party controls or can significantly influence the management or operating policies of the other to an extent that one of the transacting parties might be prevented from fully pursuing its own separate interests.

FASB No. 57, further states that:

Without disclosure to the contrary, there is a general presumption that transactions reflected in financial statements have been consummated on an arm's-length basis between independent parties. However, that presumption is not justified when related party transactions exist because the requisite conditions of competitive, free-market dealings may not exist. Because it is possible for related party transactions to be arranged to obtain certain results desired by the related parties, the resulting accounting measures may not represent what they usually would be expected to represent.

(emphasis added). Because of this, FASB No. 57 also states that:

Information about transactions with related parties is useful to users of financial statements in attempting to compare an enterprise's results of operations and financial position with those of prior periods and with those of other enterprises. It helps them to detect and explain possible differences. Therefore, information about transactions with related parties that would make a difference in decision making should be disclosed so that users of the financial statements can evaluate their significance.

(emphasis added).

b. As alleged and as further particularized herein, transactions between Citizens and HTCC (a related party) were arranged to obtain certain results desired by Citizens. In accounting for these transactions, the resulting accounting measures did not represent what they usually would be expected to represent, because the economic substance of the transactions was ignored for financial accounting purposes. Consequently, the overall impression created by the financial statements was inconsistent with the business realities of the Company's financial position and results of operations. In this regard, by virtue of its failure to present mandated disclosures regarding related party transactions, Citizens effectively concealed its fraudulent inflation of income and earnings from the investing public.

c. By failing to provide commentary with regard to Citizens' relationship with HTCC and its recognition of revenue (and resulting earnings) on transactions with HTCC, Defendants violated the disclosure rules of the SEC. Moreover, the Individual Defendants violated GAAP (APB Opinion No. 28), which provides that, "management should provide commentary relating to the effects of significant events upon the interim financial results."

53. Citizens' financial statements also violated GAAP and constituted a substantial departure from GAAP in failing to disclose the material unusual, non-recurring income received from HTCC in the first and second quarters of 1996.

a. GAAP (APB Opinion No. 28, Interim Financial Reporting) provides that:

... the effects of ... extraordinary, unusual or infrequently occurring events and transactions on the results of operations in an interim period will often be more pronounced than they will be on the results for the annual period. Special attention must be given to disclosure of the impact of these items on financial information for interim periods.

b. The mandates of APB Opinion No. 28 are consistent with the provisions of APB Opinion No. 30, Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions, which states in paragraph 26:

A material event or transaction that is unusual in nature or occurs infrequently, but not both, and therefore does not meet both criteria for classification as an extraordinary item should be reported as a separate component of income from continuing operations. The nature and financial effects of each event or transaction should be disclosed on the face of the income statement or, alternatively, in notes to the financial statements. Gains or losses of a similar nature that are not individually material shall be aggregated.

54. Citizens' financial statements also violated GAAP (APB Opinion No. 28) and constituted a substantial departure from GAAP by failing to disclose the HTCC-related income recognized in the fourth quarter of 1996. Citizens reported pre-tax income of

\$70,920,000 for the quarter ended December 31, 1996. No less than \$13,155,400 of this \$70,920,000 amount (18.55%) was recognized as income by Citizens as a result of transactions with HTCC. This fact was not disclosed in the December 31, 1996 Form 10-K or in the financial statements contained therein in contravention of GAAP (APB Opinion No. 28, paragraph 31), which states:

When interim financial data and disclosures are not separately reported for the fourth quarter, security holders often make inferences about that quarter by subtracting data based on the third quarter interim report from the annual results. In the absence of a separate fourth quarter report or disclosure of the results...for that quarter in the annual report...extraordinary, unusual, or infrequently occurring items recognized in the fourth quarter, as well as the aggregate effect of year-end adjustments which are material to the results of that quarter... should be disclosed in the annual report in a note to the annual financial statements.

55. Throughout the Class Period, Citizens also violated GAAP by failing to use equity accounting to properly account for its investment in, and income or loss from, HTCC. GAAP (Accounting Principles Board Opinion No. 18) requires equity accounting where one company (Citizens) is not merely a passive investor but is involved in controlling the activities of an investee (HTCC). As the control relationship would otherwise permit the controlling party to manipulate financial reporting to not properly reflect the investment and return, under equity accounting, the controlling investor (Citizens) must account for the investment as if reporting on a consolidated basis with the investee (HTCC). As a result, "intercompany" profits are eliminated, and the investor (Citizens) instead must report the investor's share of the investee's

profits or losses. By failing to use the equity method of accounting for its investment in HTCC, Citizens failed to eliminate intercompany gains on transactions with HTCC, and Citizens failed to recognize its share of the HTCC's losses after the date of acquisition. In this regard, during the Class Period, Citizens materially overstated its results of operations by (i) failing to eliminate and, thus, improperly recognizing no less than \$6.7 million of management fee income from HTCC, (ii) failing to eliminate and, thus, improperly recognizing approximately \$22 million of financial support fees from HTCC, and (iii) failing to recognize at least \$4.2 of losses on its investment in HTCC, as its share of HTCC's losses.

Regulation S-K

56. SEC Rule 13a-13 requires issuers to file quarterly reports. SEC Rule 12b-20 requires that periodic reports contain such further information as is necessary to make the required statements, in light of the circumstances under which they are made, not misleading. In addition, Item 303 of Regulation S-K requires that, for interim periods, the MD&A must include, among other things, a discussion of any material changes in the registrant's results of operations with respect to the most recent fiscal year-to-date period for which an income statement is provided. Instructions to Item 303 require that this discussion identify any significant elements of the registrant's income or loss from continuing operations that do not arise from or are not necessarily representative of the registrant's ongoing business.

DAMAGES AND CAUSATION

57. Plaintiffs and the other members of the Class purchased or otherwise acquired Citizens common stock and have been damaged thereby.

58. At all relevant times, the material misrepresentations and omissions particularized in this Complaint directly or proximately caused or were a substantial contributing cause of the damages sustained by Plaintiffs and other members of the Class. As described herein, during the Class Period, Defendants made or caused to be made a series of materially false or misleading statements about Citizens' business and financial statements. These material misstatements and omissions had the cause and effect of creating in the market an unrealistically positive assessment of Citizens and its business, thus causing the Company's common stock to be overvalued and artificially inflated at all relevant times. Defendants' materially false and misleading statements during the Class Period resulted in Plaintiffs and other members of the Class purchasing the Company's common stock at an artificially inflated price, thus causing the damages complained of herein. If Defendants had not made the misrepresentations and, instead, had disclosed all material facts, Plaintiffs and the other members of the Class would not have purchased their Citizens' stock or would not have purchased/acquired their Citizens' stock at artificially inflated prices.

ADDITIONAL SCIENTER ALLEGATIONS

59. As alleged herein, the Defendants acted with scienter in that Defendants knew that the public documents and statements issued or disseminated in the name of the Company were materially false and misleading; knew that such statements or documents would be issued or disseminated to the investing public; and knowingly and substantially participated or acquiesced

in the issuance or dissemination of such statements or documents as primary violations of the federal securities laws. Actual knowledge of the terms of the transactions with HTCC, the receipt of the stock and options from HTCC and the financial reporting with respect to the stock and options received is necessarily attributable to Citizens itself by virtue of the fact that the transactions were done by Citizens and on its behalf by its principal officers, including Defendant Tow.

60. In addition to the facts set forth above, the following facts also strongly infer that Defendants made the misrepresentations set forth herein knowingly or recklessly:

a. Citizens had a representative on HTCC's Board of Directors and serving as a senior advisor and through such representation, through the agreements between Citizens and HTCC and through the public filings of HTCC which were reviewed by Citizens, Defendants were aware of all of the facts relating to the relationship and agreements between Citizens and HTCC, as well as when loans and loan obligations arose and when stock and options were transferred, or payments were made by HTCC to Citizens.

b. KPMG Peat Marwick served as auditor for both Citizens and HTCC throughout the Class Period, and, through this source as well, Defendants were aware of the information about HTCC which was not disclosed.

c. In approximately November 1996, at a presentation to Citizens' Board of Directors regarding telecommunications expansion plans, the Board was told that Citizens' core business income had been substantially less than reported income and had required many one-time non-recurring items to make the reported income targets.

d. According to a former financial officer of Citizens, Defendants Tow and

DeSantis believed that they needed to find additional sources of outside income to boost earnings beginning in 1995, because 1995 was the first year in which approximately \$38 million of annual revenue from Pacific Bell (received during 1991-1994) would not be received. Also according to the former financial officer, by the end of 1995, Citizens found that it had approximately \$46 million in one-time revenue items without using any income from HTCC. Therefore, Citizens delayed the recognition of income from HTCC until 1996, not only because additional income in 1995 was not necessary to meet analysts' expectations and report.

61. Citizens and the Individual Defendants also had motives to intentionally or recklessly mislead the investing public, including the following:

a. Throughout the Class Period, Defendants had the motive to maintain the price of Citizens' stock as high as possible in order to use that stock as currency in acquisitions. For example, by February 1996, Citizens began negotiating for the acquisition of Conference-Call USA, an independent provider of telecommunications products, which ultimately culminated in execution of an acquisition agreement in October 1996 and an actual acquisition in December 1996; throughout the negotiation, Citizens insisted that the payment for Conference-Call USA would be entirely in stock, and the purchase price was eventually set at \$15,500,000 at closing and up to an additional \$17,500,000 as an earn-out over three years, all \$33,000,000 to be paid in stock at a value of \$12.125, set as a result of the price of the stock during 1996 when it was being maintained at an artificially high price as a result of the misrepresentations of the Defendants described above.

b. Also as a direct result of Defendants' wrongful conduct during the Class Period, Citizens was able to raise more than \$200,000,000 by means of a debenture offering in

December 1996 at a price that was artificially inflated. Citizens needed the funds to fuel its aggressive telecommunications expansion and to expand its other businesses as well. Among other incentives, the debenture offering, like the acquisition of Conference-Call USA, gave Defendants the motive during the Class Period to withhold the material information described above. In January 1997, the Company acquired the Hawaii gas distribution unit of Australia's Broken Hill Proprietary for \$100 million in cash, using the cash received from the debenture offering.

c. The Individual Defendants engaged in the scheme described above to inflate the price of Citizens common stock not only to benefit Citizens, as set forth above, but also in order to: (i) protect and enhance their executive positions and the substantial compensation and prestige they obtained thereby; and (ii) enhance the value of their personal Citizens securities and allow for profitable insider sales generating insider trading profits during the Class Period, as set forth below.

d. Defendants' insider selling infers Defendants' scienter and is part of Defendants' scheme, artifice to defraud or acts, practices or course of business in violation of Section 10(b) and Rule 10b-5. While Defendants were issuing false favorable financial statements, Defendants DeSantis and Ross, as well as another officer, J. Michael Love, were benefitting from the course of conduct described in this complaint by selling the Company's common stock at artificially inflated prices without disclosing the material adverse facts about the Company to which they were privy. Such sales were unusual in the number of shares sold and in the timing of the sales. The following table shows the insider selling of these officers during the Class Period:

<u>J. Michael Love</u>	<u>Shares</u>	<u>Price</u>	<u>Proceeds</u>
9/05/96	2,000 [Class B]	11.75	\$23,500.00
9/10/96	2,895 [Class B]	\$12.00	\$34,740.00
12/3/96	16,045	\$11.13	\$178,580.85
		Total:	\$236,820.85

<u>Livingston E. Ross</u>	<u>Shares</u>	<u>Price</u>	<u>Proceeds</u>
9/25/96	7,500	\$12.00	\$90,000.00
9/26/96	5,500	\$12.00	\$66,000.00
	1,088	\$12.25	\$13,328.00
9/27/96	9,600	\$12.25	\$117,600.00
10/8/96	2,000	\$12.13	\$24,260.00
		Total:	\$311,188.00

<u>Robert J. DeSantis</u>	<u>Shares</u>	<u>Price</u>	<u>Proceeds</u>
12/6/96	1,110	\$11.25	\$12,487.50
		Total:	\$12,487.50

Total: Shares: 47,738 Proceeds: \$560,496.35

FIRST CLAIM
(Violations of Section 10(b) of The Exchange Act And Rule 10b-5
Promulgated Thereunder Against All Defendants)

62. Plaintiffs repeat and reallege each and every allegation contained above as if fully set forth herein.

63. Throughout the Class Period, Citizens and the Individual Defendants, and each of them, carried out a plan, scheme and course of conduct which was intended to and did: (i)

deceive the investing public, including Plaintiffs and the other Class members, as alleged herein; (ii) artificially inflate and maintain the market price of Citizens securities, and (iii) cause Plaintiffs and other members of the Class to purchase Citizens common stock at inflated prices. In furtherance of this unlawful scheme, plan and course of conduct, Defendants, and each of them, took the actions set forth herein.

64. Defendants (a) employed devices, schemes, and artifices to defraud; (b) made untrue statements of material fact and/or omitted to state material facts necessary to make the statements not misleading; and (c) engaged in acts, practices, and a course of business which operated as a fraud and deceit upon the purchasers of the Company's securities in an effort to maintain artificially high market prices for Citizens' securities in violation of Section 10(b) of the Exchange Act, 15 U.S.C. §78j(b), and Rule 10b-5, promulgated by the S.E.C. thereunder. All Defendants are sued either as primary participants in the wrongful and illegal conduct charged herein or as controlling persons as alleged below.

65. In addition to the duties of full disclosure imposed on Defendants as a result of their making of affirmative statements and reports, or participation in the making of affirmative statements and reports to the investing public, the Defendants had a duty to promptly disseminate truthful information that would be material to investors in compliance with the integrated disclosure provisions of the SEC as embodied in SEC Regulation S-X (17 C.F.R. Sections 210.01 et seq.) and Regulation S-K (17 C.F.R. Sections 229.10 et seq.) and other SEC regulations, including accurate and truthful information with respect to the Company's operations, financial condition and earnings so that the market price of the Company's common stock would be based upon truthful, complete and accurate information.

66. Citizens and the Individual Defendants, individually and in concert, directly and indirectly, by the use, means or instrumentalities of interstate commerce and/or of the mails, engaged and participated in a continuous course of conduct to conceal material information about the business, operations, results and financial condition of Citizens, as specified herein. These Defendants employed devices, schemes and artifices to defraud, while in possession of material adverse non-public information and engaged in acts, practices, and a course of conduct as alleged herein in an effort to assure investors of Citizens' value, which included the making of, or the participation in the making of, untrue statements of material facts and omitting to state material facts necessary in order to make the statements made about Citizens and its business, operations, results and financial condition, in the light of the circumstances under which they were made, not misleading, as set forth more particularly herein, and engaged in transactions, practices and a course of business which operated as a fraud and deceit upon the purchasers of Citizens common stock during the Class Period.

67. Each of the Individual Defendants' primary liability, and controlling person liability, arises from the following facts: (i) the Individual Defendants were high-level senior executives and/or directors at the Company during the Class Period and were members of the Company's management team or had control thereof; (ii) by virtue of responsibilities and activities as a senior officer and/or director of the Company, each of these Defendants was privy to and participated in the creation, development and reporting of the Company's financial reports and other filings; (iii) each of these Defendants enjoyed significant personal contact and familiarity with the other Defendants and was advised of and had access to other members of the Company's management team, internal reports and other data and information about the

Company's finances and operations at all relevant times; and (iv) each of these Defendants was aware of the Company's dissemination of information to the investing public and knew or recklessly disregarded that it was materially false and misleading.

68. The Defendants had actual knowledge of the misrepresentations and omissions of material facts set forth herein, or acted with reckless disregard for the truth in that they failed to ascertain and to disclose such facts, even though such facts were available to them. The Defendants' material misrepresentations and/or omissions were done knowingly or recklessly and for the purpose and effect of concealing material facts about Citizens' business, operations, results and financial condition from the investing public and supporting the artificially inflated price of its securities. If Defendants did not have actual knowledge of the misrepresentations and omissions alleged, they were reckless in failing to obtain such knowledge by deliberately refraining from taking those steps necessary to discover whether those statements were false or misleading.

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

70. At the time of said misrepresentations and omissions, Plaintiffs and other members of the class were ignorant of their falsity, and believed them to be true. Had Plaintiffs and the other members of the Class and the marketplace known of the true financial condition and business of Citizens, which were not disclosed by Defendants, Plaintiffs and other members of the Class would not have purchased or otherwise acquired their Citizens securities during the Class Period, or, if they had acquired such securities during the Class Period they would not have done so at the artificially inflated prices which they paid.

71. By virtue of the foregoing, Defendants have violated Section 10(b) of the Exchange Act, and Rule 10b-5 promulgated thereunder.

72. As a direct and proximate result of Defendants' wrongful conduct, Plaintiffs and the other members of the Class suffered damages in connection with their purchases of the Company's securities during the Class Period.

SECOND CLAIM
(Violation of Section 20(a) of the Exchange Act
Against Individual Defendants)

73. Plaintiffs repeat and reallege each and every allegation contained above as if fully set forth herein.

74. The Individual Defendants acted as controlling persons of Citizens within the meaning of Section 20(a) of the Exchange Act as alleged herein. By virtue of their high-level positions, their ownership and contractual rights, their participation in and/or awareness of the Company's operations and/or intimate knowledge of the Company's expansion plans and implementation thereof, the Individual Defendants had the power to influence and control, and

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

75. In particular, each of these Defendants had direct and supervisory involvement in the day-to-day operations of the Company and the financial reporting by the Company, and, therefore, each of the Defendants is presumed to have had the power to control or influence the particular transactions giving rise to the securities violations as alleged herein, and exercised the same. The Individual Defendants' culpably participated in the commission of the wrongs alleged herein.

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

WHEREFORE, Plaintiffs pray for relief and judgment, as follows:

(a) Determining that this action is a proper class action under Rule 23 of the Federal Rules of Civil Procedure;

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

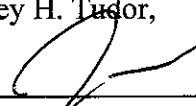
(c) Awarding Plaintiffs and the Class their reasonable costs and expenses incurred in this action, including counsel fees and expert fees; and

(d) Granting such other and further relief as the Court may deem just and proper.

JURY TRIAL DEMANDED

Plaintiffs hereby demand a trial by jury.

Lead Plaintiffs Joseph A. Ganino, Robert E. Creighton, Louise A. Creighton, William J. Fray, The Estate of Norman Garand, The Garand Family Partnership, A. John Kalil, Reza Najafzadeh, Jeffrey T. Norton, Rebecca L. Norton, John Norton, Matthew Norton, Laura Norton, Alice M. Tobin and Brantley H. Tudor,

By: 
Andrew M. Schatz (ct 00603)
Jeffrey S. Nobel (ct 04855)
Schatz & Nobel, P.C.
216 Main Street
Hartford, Connecticut 06106-1817
(860) 493-6292
Their Attorneys

ADDITIONAL COUNSEL FOR PLAINTIFFS:

Lasky & Rifkind, Ltd.
100 Park Avenue
New York, New York 10017

Goodkind Labaton Rudoff & Sucharow
100 Park Avenue
New York, New York 10017

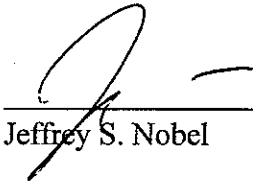
Finklestein & Krinsk
The Koll Center
501 West Broadway, Suite 1250
San Diego, California 92101-3579

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing was sent by U.S. Mail, postage prepaid, this
15th day of December, 1998 to the following:

James F. Stapleton, Esquire
Jonathan B. Tropp
Day, Berry & Howard
One Canterbury Green
Stamford, Connecticut 06901

George A. Zimmerman, Esquire
Shoshanah V. Asnis, Esquire
Skadden, Arps, Slate, Meagher & Flom LLP
919 Third Avenue
New York, New York 10022



Jeffrey S. Nobel