

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

	:	
SHIVA STEIN,	:	
	:	CIVIL ACTION NO.
Plaintiff,	:	
	:	
v.	:	COMPLAINT
	:	
APPLIED MATERIALS, INC., RANI	:	
BORKAR, JUDY BRUNER, XUN (ERIC)	:	
CHEN, AART J. de GEUS, GARY E.	:	
DICKERSON, THOMAS J. IANNOTTI,	:	
ALEXANDER A. KARSNER,	:	
ADRIANNA C. MA, YVONNE McGILL,	:	
and SCOTT A. McGREGOR,	:	
	:	
Defendants.	:	
	:	

Plaintiff, Shiva Stein, alleges, upon information and belief based upon, *inter alia*, the investigation made by and through her attorneys, except as to those allegations that pertain to the plaintiff herself, which are alleged upon knowledge, as follows:

PRELIMINARY STATEMENT

1. In 2006, in the wake of the Enron, WorldCom and Tyco options-related scandals, the Securities and Exchange Commission (“SEC”) implemented a new set of rules dictating how companies must disclose executive and director compensation to their stockholders. Among these requirements, the SEC mandated that companies disclose the “grant date fair value” of stock awards and option awards in their proxy statements following the fiscal year in which such awards were granted. This requirement has been codified in Regulation S-K, 17 C.F.R. § 229 (Item 402 (c)(2)(v) and (vi)).

2. In doing so, the SEC affirmed that full disclosure of executive and director compensation decisions is important for investors to know at the time – or soon after – those

decisions are made. Where that compensation is an unconditional cash award to an executive or director, the disclosure is transparent. Where the compensation is, however, an award of options or a complex equity instrument that expires or vests years later, the value of the compensation award on the date of grant is somewhat opaque. Providing the “grant date fair value” of such compensation in the proxy statement using approved accounting methods makes such compensation transparent to investors by assigning a dollar value to the awards.

3. But this rule mandating that companies provide the grant date fair value of equity-pay instruments is not as simple as disclosing the maximum possible award value. Instead, to determine the fair value of such awards on the date of grant often requires the use of mathematical models. Such models in turn require the implementation of assumptions concerning such awards. Such assumptions can include, but are not limited to: expected volatility, interest rates, and expected dividend yields.

4. Company managers have discretion over the assumptions that are fed into the models. Moreover, companies are incentivized to manipulate these assumptions to reduce the reported grant date fair value of equity awards. Indeed, many studies have demonstrated the selective discounting of such awards, thereby making the compensation appear less than it truly is. *See, e.g.*, Eli Bartov et al., *Managerial Discretion and the Economic Determinants of the Disclosed Volatility Parameter for Valuing ESOs*, 12 *Rev. Acct. Stud.* 155, 158 (2007) (finding in a sample of over 9000 firm-years from 1998 to 2004 that firms opportunistically selected volatility measures to reduce reported compensation); Preeti Choudhary, *Evidence on Differences Between Recognition and Disclosure: A Comparison of Inputs to Estimate Fair Values of Employee Stock Options*, 51 *J. Acct. & Econ.* 77, 91 (2011) (finding that opportunistic selection of volatility assumptions to minimize option value and compensation cost increased after stock option expensing was mandated in 2004); Leslie Davis Hodder et al., *Employee Stock*

Option Fair-Value Estimates: Do Managerial Discretion and Incentives Explain Accuracy?, 23 J. Contemp. Acct. Res. 933, 938-39 (2006) (finding use of discretion to reduce pro forma earnings among a subset of firms).

5. To police such manipulation, at the same time the SEC required the disclosure of the grant date fair values of such equity-based awards in 2006, the SEC also required that companies disclose the model and assumptions they use to calculate such values. This requirement is codified in Instruction 1 to Regulation S-K, 17 C.F.R. § 229 (Item 402 (c)(2)(v) and (vi)). Using these assumptions, it is possible for analysts (and shareholders) to re-run the calculation to confirm the disclosed grant date fair values by using a free online pricing calculator.¹

6. But despite this SEC requirement, Defendant Applied Materials Inc. (“Applied Materials” or the “Company”) does not disclose such information. *For every year since at least fiscal 2008, Applied Materials has represented in its proxy statements that the assumptions used to calculate its most highly-compensated executives’ equity-based compensation are available in the corresponding annual report on Form 10-K provided with the proxy statement. But that has never been true.* From fiscal 2008 to fiscal 2018, the Company did not even divulge the type of model used to value this compensation, and instead it represented that such valuations were arrived at by simply using the price of the stock on the date of grant, which is verifiably false as demonstrated below. Since fiscal 2019, the Company has claimed to use a Monte Carlo simulation, but it continues to withhold the assumptions it makes with this model. These omissions are all the more glaring because Applied Materials does provide the model and assumptions used to calculate *employee purchases* of common stock under its Employee Stock

¹ For example, Radford, a compensation consulting company, provides such a calculator. https://www.radford.com/home/portal/underwater_exchange_calculator.asp

Purchase Plans, and these are disclosed in the exact place in the Form 10-K where Applied Materials should (and claims it does) disclose the assumptions regarding executive compensation.

7. A review of the Form 10-Ks from these years, including the most recent Form 10-K published on December 17, 2021 in advance of the upcoming March 10, 2022 annual stockholders meeting, shows that Applied Materials has failed to provide this information to stockholders.

8. Plaintiff brings this action to rectify this failure to provide essential information concerning the compensation granted to Applied Materials' most highly-compensated executives and directors. Plaintiff also brings this action to determine whether Defendants have failed to accurately disclose the fair value of their compensation, which can only be done by knowing the assumptions Applied Materials makes to calculate the grant date fair values.

JURISDICTION

9. The jurisdiction of this court is founded upon the application of questions of federal law pursuant to § 27 of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), 15 U.S.C. § 78aa, and 28 U.S.C. § 1331.

10. The claims herein arise under § 14(a) of the Exchange Act, 15 U.S.C. §78n(a) and Rule 14a-3, 17 C.F.R. § 240.14a-3, Rule 14a-9, 17 C.F.R. § 240.14a-9, Schedule 14A, 17 C.F.R. § 240.14a-101, and Regulation S-K, 17 C.F.R. § 229, of the United States Securities and Exchange Commission (the "SEC").

THE PARTIES

11. Plaintiff Shiva Stein is a stockholder of Defendant Applied Materials, and she has been such since June 11, 2014, and continuously to date.

12. Applied is a Delaware corporation with its principal place of business in Santa Clara, California. It is authorized to do business in the State of New York and is found in New York County, as it states in its filing with the New York Secretary of State. Its stock is traded on the Nasdaq Global Select Market under the symbol AMAT. It is in the computer technology business. Its fiscal year ends on the last Sunday of October so that its last fiscal year ended October 31, 2021.

13. Defendants Rani Borkar, Judy Bruner, Xun (Eric) Chen, Aart J. de Geus, Gary E. Dickerson, Thomas J. Iannotti, Alexander A. Karsner, Adrianna C. Ma, Yvonne McGill, and Scott A. McGregor are all the members of the Applied board of directors. Defendant Gary E. Dickerson is also Applied's president and chief executive officer.

WRONGFUL ACTS AND OMISSIONS

14. The compensation of corporate directors and key officers is a matter of direct and deep concern to shareholders in the exercise of their right to vote. The SEC addresses this concern with detailed, explicit disclosure rules and regulations. This complaint challenges Applied Materials' proxy statements for omitting information specifically required by those rules and regulations and providing misinformation.

The False and Misleading 2022 Proxy Statement

15. While, as demonstrated further below, Applied Materials has failed to accurately and adequately disclose how it calculates the equity compensation awarded to its top executive officers since at least fiscal 2008, this Action is principally concerned with remedying the January 26, 2022 proxy statement furnished in advance of the March 10, 2022 annual stockholders meeting (the "2022 Proxy Statement").

16. In the 2022 Proxy Statement, the board of directors solicits the stockholders' proxies to vote in favor of the election of the ten Defendant directors named therein, including

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