

**UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF COLUMBIA**

**SECURITIES AND EXCHANGE COMMISSION  
100 F Street, N.E.  
Washington, D.C. 20549**

**Plaintiff,**

**v.**

**SAFENET, INC., ANTHONY CAPUTO,  
KENNETH MUELLER, CLINTON RONALD  
GREENMAN, JOHN WILROY, AND GREGORY  
PASKO,**

**Defendants.**

**Civil Action No.**

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**COMPLAINT**

Plaintiff Securities and Exchange Commission (the "Commission") alleges for its Complaint, as follows:

**SUMMARY OF ALLEGATIONS**

1. During the period from the fourth quarter of 2000 through May 2006, SafeNet, Inc. ("SafeNet" or the Company) engaged in two fraudulent schemes. First, SafeNet, through the actions of three former senior officers, engaged in a scheme to backdate option grants to senior executives and other employees in order to take advantage of low points in the Company's stock price, without recording the requisite compensation expense for these option grants. The three former senior officers who participated in the backdating of options were: Carole Argo ("Argo"), former Chief Financial Officer ("CFO"), defendant Anthony Caputo ("Caputo"), former Chief Executive Officer ("CEO"), and defendant Kenneth Mueller ("Mueller"), former CFO. Second,

from the third quarter of 2004 through the second quarter of 2005, SafeNet, through the actions of Mueller, Caputo and three former SafeNet accountants, Ron Greenman (“Greenman”), John Wilroy (“Wilroy”), and Gregory Pasko (“Pasko”), engaged in a scheme to meet or exceed quarterly earnings per share (“EPS”) targets through the use of improper accounting adjustments (hereinafter referred to as the “earnings management scheme”). As a direct result of each of these schemes, SafeNet materially misstated its financial results, and publicly disseminated materially false and misleading information concerning its financial condition.

2. With respect to the backdating scheme, Argo, in consultation with Caputo, looked back and selected historical dates when SafeNet’s stock price had closed at or near the low for a given period to use as grant dates for SafeNet option grants. By selecting these highly favorable dates and causing options to be granted on dates when they would be “in-the-money,” Argo and Caputo created opportunities for themselves and others at SafeNet to reap substantial profits.

3. Beginning in June 2004, Mueller was hired as SafeNet’s CFO. Shortly after his arrival, in late 2004, Mueller was apprised of SafeNet’s backdating practice by Argo. After learning of the practice, Mueller continued the backdating scheme by, among other actions, approving a highly favorable historical date, coinciding with a low closing stock price, to use as the grant date for option grants to himself and other SafeNet employees.

4. Argo, Caputo, and Mueller benefited from the backdating of option grants in several ways. For example, Argo, Caputo and Mueller each received significant in-the-money option grants. Caputo and Mueller also exercised backdated options and then sold the SafeNet shares that they received from these exercises. Caputo and Mueller realized illicit profits of approximately \$1.6 million and \$80,000, respectively, from these stock sales.

5. As a result of the backdating scheme, SafeNet's periodic reports, proxy statements, registration statements, and press releases contained materially misstated financial results and materially false and misleading information concerning SafeNet's financial condition and options granting practices. At various times during the relevant period, Argo, Mueller, and Caputo prepared, reviewed and/or signed SafeNet's materially false and misleading securities filings and press releases.

6. With respect to the earnings management scheme, from the third quarter of 2004 through the second quarter of 2005, SafeNet's senior management was under tremendous pressure to meet earnings targets. At the end of each of these quarters, Caputo and Mueller were aware that SafeNet would be unable to meet its earnings targets through normal business operations. In response, for each of these quarters, Caputo and Mueller took actions to ensure that SafeNet would meet its earnings targets. Mueller then directed his subordinates to make improper accounting entries in order to meet these targets. Specifically, based on Mueller's directions, Greenman, Wilroy and Pasko, made, or caused others to make, improper accounting adjustments to various expenses including: (i) the improper classification of ordinary operating expenses as integration expenses; (ii) the improper reduction of accruals for certain professional fees; and (iii) the improper reduction of inventory reserve accruals. At the time, Greenman, Wilroy and Pasko, knew, or should have known, that these adjustments were improper.

7. These inappropriate adjustments materially misstated SafeNet's GAAP and non-GAAP earnings results for each quarter from the third quarter of 2004 through the second quarter of 2005 and for the year ended 2004. Consequently, SafeNet's periodic reports, registration statements, and press releases contained materially misstated financial results and materially false and misleading information concerning SafeNet's financial condition.

8. At various times during the earnings management scheme, Mueller, Caputo, Greenman, Wilroy, and Pasko prepared, reviewed and/or signed SafeNet's materially false and misleading securities filings and press releases.

9. By engaging in the conduct described in this Complaint, defendant SafeNet violated the antifraud provisions of Section 17(a) of the Securities Act of 1933 ("Securities Act") [15 U.S.C. § 77q(a)], Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5], the rule relating to the use of non-GAAP financial measures of Regulation G [17 C.F.R. § 244.100], the reporting, books and records and internal control provisions of Sections 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act [15 U.S.C. §§ 78m(a), 78m(b)(2)(A) and 78m(b)(2)(B)], and Rules 12b-20, 13a-1, 13a-11, and 13a-13 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, and 240.13a-13], and the proxy solicitation provisions of Section 14(a) of the Exchange Act [15 U.S.C. § 78n(a)] and Rule 14a-9 thereunder [17 C.F.R. §240.14a-9].

10. By engaging in the conduct described in this Complaint, defendant Caputo violated the antifraud provisions of Sections 17(a)(2) and 17(a)(3) of the Securities Act [15 U.S.C. §§ 77q(a)(2) and 77q(a)(3)], the rule relating to the use of non-GAAP financial measures of Regulation G [17 C.F.R. § 244.100], the internal controls and books and records provisions of Section 13(b)(5) of the Exchange Act [15 U.S.C. §78m(b)(5)] and Rule 13b2-1 thereunder [17 C.F.R. § 240.13b2-1], the misrepresentations to auditors provision of Exchange Act Rule 13b2-2 [17 C.F.R. § 240.13b2-2], the certification provision of Exchange Act Rule 13a-14 [17 C.F.R. § 240.13a-14], the proxy solicitation provision of Section 14(a) of the Exchange Act [15 U.S.C. § 78n(a)] and Rule 14a-9 thereunder [17 C.F.R. §240.14a-9], the beneficial ownership provision of Section 16(a) of the Exchange Act [15 U.S.C. §78p(a)] and Rule 16a-3 thereunder [17 C.F.R.

§240.16a-3], and aided and abetted SafeNet's violations of Sections 13(a), 13(b)(2)(A), 13(b)(2)(B), and 14(a) of the Exchange Act [15 U.S.C. §§ 78m(a), 78m(b)(2)(A), 78m(b)(2)(B), and 78n(a)], and Rules 12b-20, 13a-1, 13a-11, 13a-13, and 14a-9 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, 240.13a-13, and 240.14a-9].

11. By engaging in the conduct described in this Complaint, defendant Mueller violated the antifraud provisions of Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5], the rule relating to the use of non-GAAP financial measures of Regulation G [17 C.F.R. § 244.100], the internal controls and books and records provisions of Section 13(b)(5) of the Exchange Act [15 U.S.C. § 78m(b)(5)] and Rule 13b2-1 thereunder [17 C.F.R. § 240.13b2-1], the misrepresentations to auditors provision of Exchange Act Rule 13b2-2 [17 C.F.R. § 240.13b2-2], the certification provision of Exchange Act Rule 13a-14 [17 C.F.R. § 240.13a-14], the proxy solicitation provision of Section 14(a) of the Exchange Act [15 U.S.C. § 78n(a)] and Rule 14a-9 thereunder [17 C.F.R. § 240.14a-9], and the beneficial ownership provision of Section 16(a) of the Exchange Act [15 U.S.C. § 78p(a)] and Rule 16a-3 thereunder [17 C.F.R. § 240.16a-3], and aided and abetted SafeNet's violations of Sections 10(b), 13(a), 13(b)(2)(A), 13(b)(2)(B), and 14(a) of Exchange Act [15 U.S.C. §§ 78j(b), 78m(a), 78m(b)(2)(A), 78m(b)(2)(B), and 78n(a)] and Rules 10b-5, 12b-20, 13a-1, 13a-11, 13a-13, and 14a-9 thereunder [17 C.F.R. §§ 240.10b-5, 240.12b-20, 240.13a-1, 240.13a-11, 240.13a-13, and 240.14a-9 ].

12. By engaging in the conduct described in this Complaint, defendants Greenman, Wilroy and Pasko violated the antifraud provisions of Sections 17(a)(2) and 17(a)(3) of the Securities Act [15 U.S.C. §§ 77q(a)(2) and 77q(a)(3)], the books and records provision of Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1], the misrepresentations to auditors

provision of Exchange Act Rule 13b2-2 [17 C.F.R. §§ 240.13b2-2], and aided and abetted SafeNet's violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act [15 U.S.C. §§ 78m(a), 78m(b)(2)(A), and 78m(b)(2)(B)], and Rules 12b-20, 13a-1, 13a-11, and 13a-13 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, and 240.13a-13].

13. The Commission seeks an order permanently enjoining SafeNet, Mueller, Caputo, Greenman, Wilroy, and Pasko from future violations of the aforementioned provisions and rules, requiring Mueller, Caputo, and Greenman to disgorge any ill-gotten gains or benefits derived as a result of their violations, as well as prejudgment interest thereon, and requiring all defendants to pay appropriate civil money penalties. In addition, the Commission seeks an order prohibiting Mueller from acting as an officer or director of any issuer that has a class of securities registered pursuant to Exchange Act Section 12 [15 U.S.C. § 78l] or that is required to file reports pursuant to Exchange Act Section 15(d) [15 U.S.C. § 78o(d)].

#### **JURISDICTION AND VENUE**

14. The Court has jurisdiction over this action pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)] and Sections 21(d), 21(e), and 27 of the Exchange Act [15 U.S.C. §§ 78u(d), 78u(e), and 78aa]. The Defendants, directly or indirectly, used the means and instrumentalities of interstate commerce, or of the mails, or the facilities of a national securities exchange in connection with the acts, transactions, practices and courses of business alleged herein.

15. Venue is proper in the District of Columbia pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)] and Sections 21(d), 21(e), and 27 of the Exchange Act [15 U.S.C. §§ 78u(d), 78u(e), and 78aa].

## THE DEFENDANTS

16. Defendant SafeNet, Inc. is a Delaware corporation, with its headquarters in Belcamp, Maryland. SafeNet produces information security software products. During the relevant period, the Company's common stock was registered with the Commission pursuant to Section 12(g) of the Exchange Act and listed on the NASDAQ National Market under the symbol "SFNT." In April 2007, SafeNet was taken private as part of a private equity transaction.

17. Defendant **Anthony Caputo**, age 67, was SafeNet's Chairman of the Board and CEO from at least October 1987 until October 2006, when he resigned from both his officer and Board positions.

18. Defendant **Kenneth Mueller**, age 57, was SafeNet's CFO from June 26, 2004 until he resigned on April 6, 2006. Mueller is a certified public accountant ("CPA").

19. Defendant **Clinton Ronald Greenman**, age 41, was SafeNet's Corporate Controller from December 2002 through December 2004. Beginning in December 2004 through May 26, 2005, Greenman was the Director for the Americas Regional Operating Center at SafeNet. Greenman is a CPA.

20. Defendant **John Wilroy**, age 50, was SafeNet's Worldwide Controller from December 2004 (subsequent to the events alleged in this complaint with respect to the third quarter of 2004) through July 29, 2005. Wilroy was a CPA from April 2003 until August 2009.

21. Defendant **Gregory Pasko**, age 43, was SafeNet's Director of External Reporting from January 2005 through May 2005. Beginning in May 2005 through June 2, 2009, Pasko was the Director for the Americas Regional Operating Center at SafeNet. Pasko is a CPA.

## FACTS

### A. Stock Options Backdating

#### Accounting for Stock Options

22. Generally Accepted Accounting Principles (“GAAP”) are standards, rules, and conventions that are established by the Financial Accounting Standards Board and other related bodies. Under Commission regulations, financial statements that are filed with the Commission must be prepared in conformity with GAAP.

23. SafeNet was required to comply with the GAAP standards governing accounting for stock options. The relevant accounting standard pertaining to options accounting was Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* (“APB 25”), which was applicable to the company throughout the period during which the illegal conduct alleged herein occurred. APB 25 required companies to record an expense for the “intrinsic” value of an employee stock option on its “measurement date.” A stock option has intrinsic value if the exercise price of the option is lower than the market price of the underlying stock on the measurement date. The measurement date is the date upon which the company, acting through a person or entity with the requisite legal authority, has determined the exercise price of the option, the number of options to be granted, and the name of the option recipient. Under APB 25, a company that grants an employee in-the-money options is required to calculate compensation expense as the difference between the exercise price and the market price of the stock on the measurement date and recognize that expense in the income statement over the vesting period of the option grant.



24. Although SafeNet routinely granted its employees in-the-money options, in almost all instances, it failed to record the attendant compensation expenses as required by APB 25.

25. From the fourth quarter of 2000 through May 2006, SafeNet inaccurately represented, in periodic reports filed with the Commission, that it complied with APB 25 and that it had properly accounted for its option grants using the intrinsic value method prescribed by APB 25.

#### **SafeNet's Option Granting Process**

26. Between 2000 and 2005, several independent SafeNet directors comprised the Compensation Committee which, among other things, was authorized to award stock options under SafeNet's stock option plans. During 1999 and the first half of 2000, the Compensation Committee primarily awarded option grants during regularly scheduled meetings of SafeNet's Board of Directors. Sometime after mid-2000, SafeNet amended its procedure for granting options and allowed a grant to be awarded by the unanimous written consent of the Compensation Committee.

27. Pursuant to SafeNet's stock options plan in effect during this period, the "grant date" was defined as "the date on which the [Compensation] Committee formally acts to grant an Award to a grantee or such other date as the [Compensation] Committee shall so designate at the time of taking such formal action." However, if the Compensation Committee granted in-the-money options as a result of selecting an historical date as the "grant date," GAAP required SafeNet to calculate compensation expense for the in-the-money portion of the options and amortize it over the vesting period of the options.

28. Beginning in mid-2000, Argo and Caputo made recommendations to the Compensation Committee concerning the specific employees or executives who should receive stock options and the number of options to be granted. The Compensation Committee would then award the grants, if appropriate.

29. In May 2000, Argo and Caputo drafted and sent a memorandum to the Compensation Committee concerning the granting of stock options. In this memorandum, Argo and Caputo stated that, "accounting rules for stock option compensation are becoming more stringent and it is important to establish procedures that ensure options are issued without a charge to compensation expense."

**Backdating of Option Grants by Argo, Caputo, and Mueller**

30. Beginning not later than October 2000, Argo's practice was to direct an administrative assistant to prepare a written consent ("Consent") for each grant of stock options by the Compensation Committee. Argo would then provide the administrative assistant with the pertinent information for the Consent, including the name of the stock option recipient, the number of options to be granted, and the grant date to be used. To select the date to be used as the grant date, Argo, or an administrative assistant acting at Argo's direction, looked back to find dates when the market price of SafeNet's stock had closed at or near the low for that quarter. On a number of occasions, Argo consulted with Caputo in order to determine the particular historical date to be used as the proposed grant date. After Argo reviewed and approved the draft Consents, they were forwarded to the Compensation Committee to have the options granted. The purported grant date for stock option grants was typically written at the top of the Consents, with the Consents stating that certain individuals named in the Consents or in an attachment were granted a specified number of options as of the date written at the top of the Consents. In

addition, the Consents typically stated that the exercise price for the option was “the last sale price of the Company’s Common Stock on the NASDAQ National Market, on the above listed date.”

31. The dates on the Consents submitted to the Compensation Committee were selected by Argo and Caputo because they were historical dates on which the closing price of SafeNet’s stock was particularly low, and often at or near the quarterly low closing price for the stock. These backdated Consents created the false appearance that the dates reflected at the top of the Consents were the actual dates when the options were granted by the Compensation Committee. When providing Consents to the Compensation Committee, neither Argo nor Caputo disclosed that SafeNet had a practice of looking back and selecting dates that coincided with particularly low stock prices as the grant dates for option grants.

32. During the period from the fourth quarter of 2000 through the second quarter of 2004, numerous option grants were backdated and presented to the Compensation Committee in order to grant Caputo, Argo, and other SafeNet employees’ in-the-money options at or near low prices for SafeNet’s stock. Argo failed to cause SafeNet to record the requisite compensation expense for these in-the-money option grants.

33. In June 2004, Argo was promoted to president and Chief Operating Officer (“COO”) of SafeNet, and Mueller was hired as SafeNet’s new CFO. In furtherance of the scheme, in an e-mail dated September 15, 2004, Argo informed Mueller of SafeNet’s past practice of backdating option grants as follows:

Our past practice has been to aggregate options for performance awards or new hires in the quarter and pick the best price after the hire date. We then send the unanimous consent to the comp committee and the options are approved. I think this is a good practice because of the volatility of our stock price. Who wants to

have an option priced on your start date and then have the option underwater a month later when you are notified of the award price.

34. After Argo apprised Mueller of SafeNet's inappropriate backdating practice, Mueller became responsible for the day-to-day administration of SafeNet's option granting process and continued the backdating practice. Specifically, in October 2004, Mueller approved the highly favorable historical date of July 28, 2004, which coincided with a low point in SafeNet's stock price, to use as a grant date for option grants to himself and other SafeNet employees.

35. During the relevant period, Argo and Mueller had significant interaction with SafeNet's independent auditor (the "Auditor"). However, they never disclosed to the Auditor that SafeNet routinely looked back to find favorable dates that coincided with particularly low stock prices to use as the grant dates for option grants. In addition, they never disclosed to SafeNet's Auditor that the dates written at the top of the Consents signed by the Compensation Committee were not the dates on which the committee had granted the options.

36. From the fourth quarter of 2000 through the first quarter of 2006, Caputo signed management representation letters to SafeNet's Auditor that contained inaccurate representations. Similarly, from the third quarter of 2004 through the first quarter 2006, Mueller signed management representation letters to SafeNet's Auditor that contained inaccurate representations.

#### **Caputo and Mueller Benefited from the Backdating of Options**

37. Both Caputo and Mueller benefited from the backdating of options when they obtained in-the-money option grants from SafeNet. The in-the-money portions of the backdated options that Caputo and Mueller received were worth approximately \$4,024,500 and \$626,000 respectively at the time of the grants. The vesting period of the grants to Caputo varied from

immediate vesting to vesting over four years on a pro rata basis. Mueller's option grants had a vesting period of four-years on a pro rata basis.

38. During 2003, 2005 and 2006, Caputo exercised 200,000 options from backdated grants that were purportedly awarded on October 1, 2001 and October 8, 2002. Upon selling the shares from these backdated grants, Caputo realized an illicit profit of \$1,691,000.

39. During 2005, Mueller exercised 12,500 options from a backdated grant that was purportedly awarded to him on July 28, 2004. Upon selling the shares received from this backdated option grant, Mueller realized an illicit profit of approximately \$78,000.

### **Specific Examples of Backdated Option Grants**

#### **The October 1, 2001 Grants**

40. During the summer of 2001, the Compensation Committee was involved in ongoing discussions with Caputo concerning the number of options that he would receive in connection with his new employment contract. During these negotiations, Caputo requested that the Compensation Committee award him 200,000 options. However, the Compensation Committee ultimately decided to grant Caputo only 50,000 options as part of his new employment contract.

41. In late October 2001, after consulting with Caputo, Argo looked back and selected October 1, 2001, the date when SafeNet's stock had closed at its lowest price during that quarter, to use as the grant date for option awards to herself and Caputo. On or about October 25, 2001, Argo sent a written consent, dated October 1, 2001, to the Compensation Committee to award 50,000 options to Caputo and 20,000 options to Argo, both at the exercise price of \$5.85, the closing price of SafeNet's stock on October 1, 2001. The exercise price of \$5.85 was extremely

advantageous to Argo and Caputo because, on October 25, 2001, SafeNet's stock closed at \$9.85 per share.

42. On or about October 28, 2001, the Compensation Committee executed the Consent granting these stock options to Caputo and Argo at exercise prices of \$5.85 per share.

43. Caputo, however, was dissatisfied that he had only been awarded 50,000 options. As a compromise, on or about December 12, 2001, the Compensation Committee agreed to grant Caputo an additional 100,000 options, as an inducement for him to execute a new employment contract with SafeNet. On December 12, 2001, Caputo agreed to sign his new employment contract, and the board approved Caputo's new contract.

44. The contract, which was also dated December 12, 2001, stated that Caputo had been "issued 150,000 incentive stock options" and that the options "were issued at the fair market value of [SafeNet's] common stock as of the date of the grant." The 150,000 options referred to in the contract included the 50,000 options that the Compensation Committee had agreed to grant to Caputo on or about October 28, 2001.

45. On or about January 4, 2002, Caputo and Argo again selected October 1, 2001, the date when SafeNet's stock had closed at its lowest price during the fourth quarter 2001, as the grant date for the option awards to themselves and another executive. At Caputo's direction, on January 4, 2002, Argo requested that the Compensation Committee execute a written consent, dated October 1, 2001, granting 150,000 options to Caputo, 45,000 options to Argo, and 10,000 options to another SafeNet executive. On January 4, 2002, the closing price of SafeNet stock was \$18.65 per share.

46. In a cover letter accompanying these Consents, Argo explained to the Compensation Committee that the new consent would “modify” the initial grants made to her and Caputo during the prior quarter.

47. On January 4, 2002, the Compensation Committee executed these Consents. Thus, these option grants were awarded on January 4, 2002, three months after the purported grant date of October 1, 2001 that was stated in the Consents. Because these option grants were awarded on January 4, 2002, when SafeNet’s stock price closed at \$18.65, but were backdated to October 1, 2001, when the closing stock price was \$5.85, Argo and Caputo received option grants that were in-the-money by \$12.80 per share, which gave them an illicit benefit of approximately \$576,000 and \$1,920,000, respectively.

48. As a result of the conduct of Argo and Caputo, SafeNet failed to record a compensation expense for these option grants.

#### The July 28, 2004 Grants

49. After informing Mueller of SafeNet’s option backdating practice in her September 15, 2004 email, Argo added that she had asked the vice president of human resources (“HR VP”), to assist Mueller in getting options priced and approved by the Compensation Committee. On September 27, 2004, the HR VP sent an e-mail to Mueller, attaching a spreadsheet containing a list of SafeNet employees hired during the third quarter of 2004, and the number of options each was to receive in connection with a contemplated new hire grant. After reviewing this list, Mueller approved July 28 as the grant date to be used for his and the other option grants. This date coincided with the lowest closing price for SafeNet’s stock during the third quarter of 2004.

50. Subsequently, at Mueller’s direction, a backdated Consent was sent to the Compensation Committee to obtain approval to issue a total of 182,000 stock options, including

100,000 to Mueller, at the July 28 closing price of \$22.19. On October 9, 2004, the Compensation Committee authorized these option grants. Because Mueller's option grant was awarded on October 9, 2004, but was backdated to July 28, Mueller received option grants that were in-the-money by \$6.26 per share, which gave him an illicit benefit of approximately \$626,000.

51. At the time, Mueller knew, or was reckless in not knowing, that he and other SafeNet employees had been awarded backdated option grants to take advantage of a historically low closing price for SafeNet's stock, and that the grants were "in-the-money" when awarded. Mueller further knew, or was reckless in not knowing, that SafeNet was required to recognize a substantial compensation expense for the in-the-money portion of these option grants. Again, SafeNet did not record a compensation expense for these option awards.

#### The February 2005 Grants

52. In February 2005, SafeNet again awarded in-the-money options to certain employees. During or shortly after the first quarter of 2005, SafeNet's Auditor, while performing certain procedures, learned that the Company had issued option grants to SafeNet employees using historical dates from 2004 and 2005. In response, the Auditor discussed with various members of SafeNet's accounting staff, including Mueller, the need to recognize a compensation charge for the issuance of these in-the-money options. Consequently, SafeNet recognized a compensation charge for the granting of these in-the-money options.

53. Despite the fact that Mueller knew, or was reckless in not knowing that: (i) he and others had received substantial in-the-money option grants in the past; and (ii) although the requisite compensation expense for previous grants had not been recorded, he failed to take any remedial steps.



### The June 1, 2005 Grants

54. On May 31, 2005, an assistant to Argo (“Administrative Assistant”) sent an e-mail to Caputo, Argo, and Mueller. In the e-mail, the Administrative Assistant stated: “I was able to pick a price at the end of the quarter that was very low for almost all grants.” The e-mail included a list (the “List”) reflecting numerous option grants that were to be approved by SafeNet’s Board at a meeting scheduled for June 1, 2005. The List contained each contemplated option recipient, proposed grant dates (which ranged from September 2004 through March 2005), and a column reflecting the historical closing prices of SafeNet’s stock for each proposed grant date. The proposed exercise prices reflected on the List were more favorable than the price for SafeNet’s stock at the time the list was circulated.

55. At a Board meeting held on June 1, 2005, the Board approved option grants to the employees included on the List that was attached to the email that had been sent to Caputo, Argo, and Mueller on the previous day. These option grants were awarded to SafeNet employees, including Argo, using favorable historical grant dates that were from September 2004 through March 2005. Based upon SafeNet’s closing stock price on June 1, 2005, these option grants were in-the-money at the time they were awarded.

56. During July 2005, an assistant to a controller in SafeNet’s accounting department (“Assistant Controller”), learned that these in-the-money options had been awarded, and as a result, determined that a compensation expense of approximately \$1 million would need to be recorded over the vesting period of the options, beginning in the second quarter of 2005. The Assistant Controller then recorded in SafeNet’s books the appropriate expense for the second quarter of 2005.

57. In light of the large compensation expense, the Assistant Controller and the Administrative Assistant subsequently met with Mueller to advise him that SafeNet was required to record a compensation expense of approximately \$1 million. During the meeting, Mueller expressed that he did not want SafeNet to recognize a large compensation charge, and discussed ways to avoid the requirement to record the expense, including whether Caputo could change the grant date in order to avoid recording the charge. At the end of the meeting, Mueller instructed the Administrative Assistant to inform Caputo of the large compensation expense.

58. During a subsequent meeting with Caputo, the Administrative Assistant told him that the company needed to record a compensation expense of approximately \$1 million because the options awarded on June 1 had used historical grant dates. In response, Caputo stated that SafeNet would not record the \$1 million expense. Instead, Caputo told the Administrative Assistant to change all of the grant dates to June 1, which was the date when the options had actually been awarded by the Board, except for a grant to Argo. At the time he made this decision, Caputo did not have the legal authority to change the terms of option grants, including the grant dates.

59. Subsequently, Mueller and others were informed about Caputo's decision. The grant dates were then changed to June 1, and the compensation expense that had been previously recorded for these option grants was reversed.

60. At the time, based on the facts alleged in paragraphs 22 through 59, Caputo knew or should have known that (i) as a result of SafeNet's practice of backdating options grants, it was required to record compensation expense, but had failed to do so, and (ii) as a result of not recording these expenses, SafeNet's financial statements were materially misstated.

61. Also, at the time, based on the facts alleged in paragraphs 22 through 25, 33 through 39, and 51 through 59, Mueller knew or was reckless in not knowing, that (i) as a result of SafeNet's practice of backdating options grants, SafeNet was required to record compensation expense but had failed to do so, and (ii) SafeNet's financial statements were materially misstated as a result of not recording these expenses.

**SafeNet's Materially False and Misleading Statements and Disclosures**

62. As a result of the backdating scheme, from the fourth quarter of 2000 through May 2006, SafeNet's periodic reports, proxy statements, registration statements, and press releases contained materially misstated financial results and materially false and misleading information concerning SafeNet's financial condition and options granting practices. For example, during fiscal years 2000 through 2005, SafeNet's annual net income or loss was materially misstated for each year by approximately 5 percent, 26 percent, 30 percent, 26 percent, 246 percent, and 111 percent, respectively.

63. At various times during the relevant period, Mueller and Caputo prepared, reviewed and/or signed SafeNet's securities filings and press releases. Mueller knew, or was reckless in not knowing, that these securities filings and press releases contained materially false and misleading financial results as well as inaccurate disclosures. Caputo knew, or should have known, that that these securities filings and press releases contained materially false and misleading financial results as well as inaccurate disclosures.

64. During the relevant periods, Caputo and Mueller also signed certifications in connection with SafeNet's securities filings. Both Caputo and Mueller inaccurately certified that the respective filings did not contain any material misstatements or omit material information

and that the reports fairly presented in all material respects SafeNet's financial condition and results of operations.

#### **SafeNet's Materially False and Misleading Proxy Statements**

65. During the period of the improper conduct, SafeNet, issued proxy statement filings that contained materially false and misleading statements and material omissions concerning SafeNet's stock option granting practices. In connection with their duties as officers of the Company, Caputo and Mueller prepared and/or reviewed SafeNet's proxy statements that contained materially false and misleading statements and material omissions concerning SafeNet's stock option grants made to themselves and other SafeNet employees.

#### **Caputo and Mueller Failed to File Section 16 Ownership Reports**

66. During the relevant period, Caputo and Mueller, as senior officers of a public company, were required to disclose option grants within two days of the date of grant, by filing with the Commission reports on Forms 4. Caputo and Mueller failed to file reports on Form 4 with the Commission to disclose the option grants that they each received from SafeNet.

### **B. The Earnings Management Scheme**

#### **Background**

67. During the relevant period, SafeNet disseminated financial results in press releases and during quarterly conference calls with analysts and investors. At the end of each quarter, SafeNet also provided investors and analysts with "earnings guidance" for net income and EPS for the upcoming quarter and the full year. SafeNet provided its financial results and earnings guidance with respect to its GAAP earnings and its non-GAAP earnings.

68. SafeNet's non-GAAP earnings excluded the impact of certain expenses that were reflected in its GAAP earnings. For example, SafeNet routinely excluded expenses that it claimed were attributable to the costs of integrating acquired companies into its current operations ("integration expense").

69. Based in part on SafeNet's quarterly guidance, Wall Street analysts estimated what they believed would be SafeNet's non-GAAP EPS for each quarter. The average of these estimates was commonly referred to as the "consensus estimate," and as with many public companies, was used by investors as a measure of SafeNet's financial performance on a quarterly basis. The terms "consensus estimates" and "earnings guidance" will hereinafter collectively be referred to as "earnings targets."

70. Meeting or exceeding earnings targets was a very high priority for SafeNet. Consequently, SafeNet's senior management exerted tremendous pressure on SafeNet's accounting and finance staff to meet earnings targets. As described below, during the period of the misconduct, when SafeNet could not meet these earnings targets through normal business operations, it engaged in illegitimate practices to meet earnings targets.

71. In March 2003, the Commission promulgated Regulation G to ensure that the use of non-GAAP performance measures by issuers was not misleading to investors and that investors clearly understood the difference between a company's GAAP and non-GAAP financial results. Toward that end, Regulation G prohibited issuers from providing investors with false or misleading presentations of non-GAAP financial measures including non-GAAP earnings results. Regulation G also required issuers who disclose non-GAAP earnings to investors to provide, in their public releases, reconciliations from the non-GAAP earnings to the

GAAP earnings by identifying each category of expenses that was excluded from the non-GAAP amounts.

72. During the relevant period, SafeNet's press releases for quarterly earnings announcements included financial results on a GAAP and non-GAAP basis, along with a reconciliation between the GAAP and non-GAAP financial results. From the second quarter of 2003, on a quarterly basis, SafeNet furnished to the Commission its quarterly earnings announcements on Forms 8-K.

73. As described below, as a result of the earnings management scheme, SafeNet violated Regulation G by disseminating false and misleading non-GAAP financial results beginning with the third quarter of 2004 and continuing through the second quarter of 2005, and for the year ended 2004.

#### **Overview of the Earnings Management Scheme**

74. From the third quarter of 2004 through the second quarter of 2005, SafeNet's senior management was under tremendous pressure to meet earnings targets. At the end of each of these quarters, Caputo and Mueller were aware that SafeNet's business operations had been insufficient to meet the earnings targets for each of these quarters. As a result, Caputo and Mueller took actions to ensure that SafeNet would meet its earnings targets. In response, Mueller requested that his subordinates make improper accounting entries in order to meet these targets. Specifically, based on Mueller's requests, Greenman, Wilroy, and Pasko made, or caused others to make, improper accounting adjustments to various expenses including: (i) the improper classification of ordinary operating expenses as integration expenses; (ii) the improper reduction of accruals for certain professional fees; and (iii) the improper reduction of inventory

reserve accruals. These inappropriate adjustments were then recorded in SafeNet's books and records.

75. Greenman, Wilroy, and Pasko knew, or should have known, that these adjustments were improper because they: (i) were made solely for the purpose of meeting or exceeding earnings targets; (ii) were made without any support or as a result of unsupported assumptions, (iii) created the false and misleading appearance that SafeNet had met or exceeded its quarterly earnings targets through its normal business operations; and (iv) in a number of instances, resulted in SafeNet not complying with GAAP.

76. As SafeNet's CFO, Mueller knew, or was reckless in not knowing, that these adjustments were improper because they: (i) were made solely for the purpose of meeting or exceeding earnings targets; (ii) were made without any support or as a result of unsupported assumptions, (iii) created the false and misleading appearance that SafeNet had met or exceeded its quarterly earnings targets through its normal business operations; and (iv) in a number of instances, resulted in SafeNet not complying with GAAP.

77. Through his role as CEO, and based on information that he received through his interactions with Mueller and others, Caputo knew or should have known that, during the relevant period, quarterly earnings targets had been met through the use of improper accounting adjustments.

78. During the course of the improper conduct, SafeNet, through the actions of Caputo, Mueller, Greenman, Wilroy, and Pasko, failed to disclose to investors that its quarterly earnings results had been materially inflated due to these accounting improprieties.

79. The following sections of the Complaint describe the facts surrounding the improper adjustments in each of the primary areas involved in the misconduct. Although each area is discussed separately, these and other improper adjustments were used collectively by SafeNet to meet or exceed quarterly earnings targets.

**Misclassification of Ordinary Operating Expenses as Integration Expenses**

80. By the end of the fourth quarter of 2004, after realizing that SafeNet would not meet its earnings target for that quarter, Mueller requested that Greenman and Wilroy identify ordinary operating expenses related to advertising and marketing (collectively, "advertising"), and reclassify them, without support, as integration expenses. By eliminating these and other expenses, SafeNet's non-GAAP earnings results were significantly inflated.

81. Specifically, acting on Mueller's instructions, Greenman, without any support, asked a subordinate to classify one hundred percent of SafeNet's advertising expenses for its U.S. operations as an integration expense. In addition, at Mueller's direction, Greenman also caused certain advertising expenses that had been recorded in previous quarters during 2004 to be reclassified as integration expenses for the fourth quarter of 2004, even though these expenses had not been incurred in that quarter.

82. Based on these instructions, SafeNet's accounting personnel made improper and incorrect entries in SafeNet's books and records with respect to the fourth quarter of 2004. These entries increased SafeNet's non-GAAP EPS by approximately six cents per share.

83. Prior to these entries being recorded, Mueller, Greenman, and Wilroy failed to perform any analysis or research to determine whether any of the reclassified advertising expenses were actually related to the integration of any acquired companies. Pasko learned of



these accounting entries, which were improper, by the end of the first quarter of 2005, or by early in the second quarter of 2005.

84. Even with these improper entries, SafeNet still could not meet its quarterly non-GAAP earnings target for the fourth quarter of 2004. As a result, Mueller requested that Greenman and Wilroy reclassify one hundred percent of foreign advertising expenses, and fifty percent of the travel, meals, and entertainment expenses of SafeNet's international subsidiaries. As with the other entries, no research or analysis was performed prior to these entries being made in SafeNet's books and records.

85. On or about January 19, 2005, SafeNet's accounting department reclassified approximately \$1.1 million of expenses, which consisted of one hundred percent of advertising, fifty percent of travel, and fifty percent of the meals and entertainment expenses for SafeNet's international subsidiaries. These entries increased SafeNet's non-GAAP EPS for the fourth quarter 2004 by approximately three cents per share.

86. As a result of the improper entries, for the fourth quarter of 2004, SafeNet misclassified approximately 104 percent of its total advertising expenses as an integration expense. Consequently, SafeNet's non-GAAP EPS was materially overstated for the fourth quarter of 2004.

87. Also, during the conference call to discuss SafeNet's fourth quarter and year end 2004 financial results, Caputo and Mueller made materially inaccurate statements, and omitted material information, concerning SafeNet's integration expenses, and specifically, with respect to the nature of the advertising costs that had been treated as integration expenses. For example, during the conference call, an analyst questioned why marketing expenses had been treated as an integration expense. In response, Caputo asserted that these costs were "one-time in nature" and

related to the cost of SafeNet changing marketing materials (such as signage) of an acquired company to reflect that it was now part of SafeNet. At the time, Caputo knew or should have known that this information was misleading because he was aware that the majority of these costs actually had been incurred for advertising SafeNet products.

### **Other Improperly Classified Integration Expenses**

88. In order to meet quarterly earnings targets, SafeNet also improperly reclassified ordinary expenses related to compliance with certain requirements imposed by the Sarbanes-Oxley Act of 2002 ("SOX") as integration expenses. From the fourth quarter of 2004 through the second quarter of 2005, SafeNet improperly characterized approximately sixty-six percent of the company's SOX expenses as integration expenses.

89. As with the advertising expenses, SafeNet did not perform any analysis to determine whether the SOX expenses had been incurred as a result of the integration of an acquired company. Instead, SafeNet, at Mueller's direction, made unsupported assumptions about the percentage of SOX costs that were purportedly incurred as a direct result of the integration of an acquired company. Specifically, Mueller told his accounting staff (including Greenman, Wilroy, and Pasko) they should inform the Auditors that, because a particular acquisition had increased SafeNet's size by sixty-six percent, SafeNet was justified in treating sixty-six percent of SafeNet's total SOX costs as integration expense. Subsequently, on a number of occasions, this misleading explanation was provided to the Auditors and SafeNet's Audit Committee.

90. At the time, Greenman, Wilroy and Pasko knew, or should have known, that the accounting entries related to the SOX costs were not proper because there was no support for these entries.

91. Neither SafeNet nor Mueller ever disclosed to investors that SafeNet had relied on unsupported assumptions, rather than the actual amount of expenses, to determine what percentage of SafeNet's SOX costs could be classified as an integration expense.

92. SafeNet also recorded as integration expenses certain unexpected expenses that would have adversely affected SafeNet's earnings. On or about March 4, 2005, SafeNet's Auditor discovered that, during the fourth quarter of 2004, SafeNet had not accrued an expense for an invoice for approximately \$301,000. In response, the Auditor advised SafeNet's accounting personnel that SafeNet would have to accrue this amount as an expense as part of both its fourth quarter and year ended 2004 results. Based on Mueller's directions, Greenman advised the Assistant Controller to classify as an integration expense as much of the approximately \$301,000 invoice as needed to enable SafeNet to meet its quarterly earnings targets. In an email dated March 3, 2005, the Assistant Controller advised Greenman, and Wilroy that she had accrued the approximately \$301,000, but "had to put \$100k into integration to keep the EPS." This email string was then forwarded to Pasko, and subsequently, to Mueller.

93. During the first and second quarters of 2005, SafeNet, through the actions of Mueller, Greenman, Wilroy, and Pasko continued to misclassify certain expenses as integration expenses in order to meet earnings targets.

**Misleading SafeNet's Audit Committee and Auditor Regarding Integration Expenses**

94. During the relevant period, Caputo, Mueller, Greenman, Wilroy, and Pasko, made, or caused others to make, misleading statements to the Audit Committee and SafeNet's Auditor regarding the nature of the integration expenses being claimed by SafeNet.

95. On March 14, 2005, SafeNet's Audit Committee held a meeting that was attended by, among others, Caputo, Mueller, Greenman, Wilroy, Pasko, and the Audit Partner for the Auditor. In commenting on SafeNet's integration expenses for the fourth quarter and year ended 2004, the Audit Partner stated that, "these costs should not be recurring and are subject to challenge." In response to the issues raised by the Audit Partner, the Audit Committee requested information from management regarding the nature of SafeNet's specific integration expenses.

96. In response to this request by the Audit Committee, Wilroy, with input from SafeNet's accounting department (including Greenman and Pasko), Caputo, and Mueller, drafted a detailed memorandum ("Integration Summary") summarizing the dollar amount and purported rationale for each category of expense that had been classified as an integration expense. Prior to the meeting, Wilroy confirmed with Caputo that the description of each area of integration expense was acceptable to Caputo. Subsequently, Wilroy provided the Integration Summary to the Audit Committee and SafeNet's Auditor. At the time the Integration Summary was provided to the Audit Committee and SafeNet's Auditor, Caputo, Wilroy, Greenman and Pasko knew or should have known that it contained false and misleading statements about the methodology that SafeNet purportedly used to determine the amount of its integration expenses.

97. As SafeNet's CFO, Mueller knew, or was reckless in not knowing, that the Integration Summary contained false and misleading statements about the methodology that SafeNet purportedly used to determine the amount of its integration expenses.

**SafeNet's Misleading Presentation of its Non-GAAP Earnings for the Second Quarter of 2005**

98. For the second quarter of 2005, SafeNet had planned to report in its earnings release that its quarterly integration expenses were approximately \$5 million, or approximately

\$.15 per share. This amount was extremely large in comparison to the total amount of SafeNet's non-GAAP EPS for that quarter.

99. During the Auditor's second quarter review, the Auditor determined that a large portion of these expenses should be reclassified as ordinary operating expenses. In particular, the Auditor concluded that SafeNet's use of integration costs during the second quarter was "abusive." The Auditor also found that SafeNet appeared to be using the integration expense category "as a means of meeting [non-GAAP] EPS guidance."

100. As a result, the Auditor required SafeNet to reclassify approximately \$3 million of the approximately \$5 million of proposed second quarter integration expenses as ordinary operating expenses. Notably, the remaining integration expenses of approximately \$2 million still included ordinary operating expenses, such as, approximately \$470,000 of SOX costs that SafeNet had improperly classified as an integration expense.

101. At the Auditor's insistence, SafeNet removed approximately \$2.6 million from the integration expense line item on its GAAP income statement for the second quarter of 2005. However, in order to meet its non-GAAP earnings targets, SafeNet, at the direction of Caputo and Mueller, continued to exclude approximately \$4.6 million dollars (e.g., approximately \$2.6 million that the Auditor had not allowed to be included in integration expense, plus the remaining \$2 million of purported integration expense to which the Auditor did not object) from its non-GAAP earnings results.

102. By excluding these very significant amounts, SafeNet hoped to be able to meet or exceed its earnings target for the second quarter of 2005. However, even if SafeNet excluded approximately \$2.6 million from its non-GAAP earnings, it still needed to explain in its earnings release how this excluded amount related to the GAAP income statement.

103. To address this disparity, SafeNet created certain categories in its reconciliation including: “Research and Development—non-recurring;” “Sales and Marketing—non-recurring;” and “General and Administrative—non-recurring.” The total of these three categories offset the approximately \$2.6 million in expenses that the Auditor had refused to allow SafeNet to treat as integration expenses because the Auditor had concluded they were ordinary and recurring operating expenses.

104. For example, approximately forty-six percent of the \$2.6 million consisted of the salaries of approximately sixty employees who purportedly were going to be terminated in upcoming fiscal quarters. In reality, no decisions had been made with respect to these employees prior to the end of the second quarter of 2005. In fact, some of these employees never were terminated by SafeNet, or were terminated six months to a year after the end of the second quarter of 2005.

105. During the quarterly conference call, both Caputo and Mueller discussed these purportedly “non-recurring” charges with the analysts. In describing these charges, Caputo and Mueller failed to disclose material information. For example, they failed to disclose that a large percentage of the charges consisted of ordinary salary expenses for the second quarter for employees that they purportedly planned to terminate in future quarters.

#### **Improper Reductions of Professional Fee Accruals**

106. Prior to the third quarter of 2004, SafeNet’s long standing practice was to estimate the total annual costs for professional services relating to the preparation and filing of periodic reports on Form 10-Q and Form 10-K. After determining SafeNet’s professional service fee estimates at the beginning of each year, SafeNet then recorded the estimated expense each month so that such expenses were spread over a twelve-month period.

107. From the third quarter of 2004 through the first quarter of 2005, SafeNet, through the conduct of its employees, reduced certain previously recorded professional fee accruals and reversed them into income. These adjustments were made without any support and for the purpose of creating the false appearance that SafeNet had met its quarterly earnings targets. Mueller, Greenman, Wilroy, and Pasko reduced, or were aware that others had reduced, these professional fee accruals, which were then reversed into income.

108. Similarly, for the fourth quarter of 2004 and first quarter of 2005, Mueller, Greenman, and Wilroy caused SafeNet to not record any further accruals for professional fees, even though SafeNet was required to do so under GAAP. For example, during the first quarter of 2005, as SafeNet received invoices for professional services that had been rendered, SafeNet did not record these invoiced amounts as expenses in its books and records, as required by GAAP. By the end of the first quarter 2005, or early in the second quarter of 2005, Pasko had learned about the aforementioned conduct relating to professional accruals.

109. By reversing these accruals and ceasing to record them in future quarters, SafeNet changed its long-standing method for accounting for professional fees. Under GAAP, SafeNet was required to disclose this change to investors, but failed to do so. Also, such a change required the issuance of a "preferability letter" from SafeNet's auditor, which was required to be filed with the company's next periodic filing with the Commission.

110. Mueller, Greenman, Wilroy, and Pasko failed to advise SafeNet's Auditors of this change, and failed to cause SafeNet to disclose this information to investors.

111. As a result of SafeNet's failure to properly accrue for professional fees during prior quarters, by the second quarter of 2005, SafeNet accumulated a substantial amount of out of period professional fee expenses that were due or past due for payment. For example, by mid-

May 2005, SafeNet had accumulated approximately one million dollars of out of period professional expenses.

112. During the second quarter of 2005, SafeNet was required to pay at least \$800,000 of the past due invoices, which should have been accrued in prior quarters. Upon paying these past due invoices, SafeNet recorded an expense of at least \$800,000 for these out of period expenses. As a result of the conduct of Mueller, Greenman, Wilroy and Pasko, SafeNet failed to disclose to investors or its Auditors that: (i) the second quarter results included these significant out of period expenses, and (ii) these expenses had not been accrued in prior quarters in order to create the false appearance that SafeNet had reached its earnings targets in prior quarters.

113. Also, at the end of the second quarter of 2005, Mueller told Pasko to continue to reduce accruals in order to inflate SafeNet's quarterly EPS. Pasko then asked the Assistant Controller to "drive down liabilities" in order to increase SafeNet's EPS for the second quarter of 2005.

114. The Assistant Controller initially refused to make this adjustment because she knew it was not appropriate. However, after Pasko promised the Assistant Controller that this would be the last time that he would ask her to do this, the Assistant Controller reduced the accruals in order to increase SafeNet's quarterly EPS.

#### **Improper Inventory Reserve Reductions**

115. As part of the earnings management scheme, Mueller also requested that Greenman improperly reduce SafeNet's domestic, obsolete, inventory reserve ("inventory reserve") to inflate its quarterly EPS on both a GAAP and non-GAAP basis. Specifically, for the fourth quarter and year ended of 2004, SafeNet's level of inventory reserves was reduced by



approximately \$1.7 million. These improper adjustments increased SafeNet's quarterly EPS by approximately four cents per share.

116. Under GAAP, inventory must be recorded at the lower of either its cost or the market price, and any write-downs of inventory establish a new cost basis for the inventory. Once inventory is written-down, it cannot be valued at a higher price. By reducing the inventory reserve and consequently, increasing the recorded value of the inventory, SafeNet failed to comply with GAAP.

117. During the first quarter of 2005, SafeNet improperly reduced inventory reserves by approximately \$106,000. This entry, when combined with the other improper entries made during the first quarter, created the false appearance that SafeNet had met its quarterly earnings targets through its normal business operations.

118. At the time, Mueller knew, or was reckless in not knowing, about the GAAP violations that resulted from these inappropriate reserve reductions. Greenman, Wilroy, and Pasko knew, or should have known, about the GAAP violations that resulted from these inappropriate reserve reductions.

119. In April 2005, while conducting an interim review, the Auditor inquired about the rationale for SafeNet changing its level of inventory reserves. At the time, Mueller, Greenman, and Wilroy became aware that a SafeNet employee had provided an inaccurate and misleading explanation to the Auditor to make it appear that these reserve reductions were legitimate, but they did nothing to correct the information that had been given to the Auditor.

120. At the end of the second quarter of 2005, Mueller was informed by the Assistant Controller that SafeNet's inventory reserves needed to be increased to appropriate levels.

Specifically, she recommended that Mueller increase SafeNet's inventory reserves from one percent of the inventory balance to five percent of the inventory balance, because low reserve levels had been created by the improper reductions in prior quarters. Mueller responded that he did not want to record the reserve at five percent because the Auditor would notice that change. Mueller then directed that the inventory reserve be recorded at only two percent, which was far below the level at which it should have been recorded. Although the Assistant Controller disagreed with Mueller, she made the change in the general ledger but noted next to the entry, "Per CFO, bring inventory reserve to 2% of total inventory."

121. In connection with the review for the second quarter of 2005, the Auditor again questioned SafeNet's accounting for inventory reserves. In response to these questions, a SafeNet employee provided the Auditor with a misleading explanation for the changes to the inventory reserves. At the time, Mueller knew, or was reckless in not knowing, and Wilroy and Pasko knew, or should have known, that an inaccurate explanation had been provided to the Auditor.

#### **SafeNet's Materially False and Misleading Statements and Disclosures**

122. As a result of the earnings management scheme, SafeNet's financial results were materially misstated, on a GAAP and a non-GAAP basis, for the third quarter of 2004 through the second quarter of 2005 and for the year ended 2004. Specifically, SafeNet's GAAP net income or loss was misstated in financial statements by as much as 25 percent for the third quarter of 2004, 882 percent for the fourth quarter of 2004, 75 percent for the first quarter of 2005, 15 percent for the second quarter of 2005, and approximately 270 percent for the year ended 2004. SafeNet's non-GAAP net income was misstated by as much as 5 percent for the

third quarter of 2004, 50 percent for the fourth quarter of 2004, 13 percent for the first quarter of 2005, 7 percent for the second quarter of 2005, and 15 percent for the year ended 2004.

123. These misstatements were also qualitatively material to investors because they resulted from accounting entries that were made: (i) without any support, or on the basis of unsupported assumptions; and (ii) with the intent to artificially inflate SafeNet's earnings results.

124. During the relevant period, SafeNet, through the conduct of Mueller and Caputo, stated that SafeNet's integration expenses were "non-recurring" or "one time in nature." As described above, during the relevant period, a significant portion of the purported integration expenses consisted of ordinary and recurring expenses.

125. The improper classifications of operating expenses as integration expenses also resulted in certain line items on SafeNet's income statements being materially misstated. Specifically, these misclassifications resulted in SafeNet materially overstating the amount of its integration expense line item and understating the amount of several operating expense line items.

126. Throughout the period of the earnings management scheme, Caputo and Mueller reviewed, approved, and/or signed periodic securities filings, registration statements, and press releases, which included SafeNet's misstated financial results. Accordingly, Caputo and Mueller caused SafeNet to disseminate materially misstated financial results and false and misleading information related to those financial results.

127. During the course of the improper conduct, Caputo and Mueller also signed certifications in connection with SafeNet's public filings on Forms 10-K and Forms 10-Q. Both Caputo and Mueller inaccurately certified that the relevant filings did not contain any material misstatements or omit material information and that the reports fairly presented in all material

respects SafeNet's financial condition and results of operations. SafeNet's financial statements filed for those years did not fairly present SafeNet's financial condition because SafeNet had misstated its financial results due to the illicit accounting adjustments, described above.

128. At various times during the earnings management scheme, Greenman, Wilroy, and Pasko assisted in the preparation of SafeNet's financial statements that were included in periodic securities filings, registration statements, and press releases. At the time, Greenman, Wilroy, and Pasko knew, or should have known, that SafeNet's financial statements were materially misleading as a consequence of the improper accounting adjustments. Accordingly, Greenman, Wilroy, and Pasko caused SafeNet to disseminate materially false and misleading financial statements.

129. In addition, during the relevant period, Caputo, Mueller, Greenman, Wilroy, and Pasko, each signed management representation letters to SafeNet's Auditor that contained inaccurate representations.

**FIRST CLAIM**  
**Violations of Securities Act Section 17(a)(1)**  
**(As to Defendants SafeNet and Mueller)**

130. The Commission realleges and incorporates by reference each and every allegation contained in Paragraphs 1 through 129 above.

131. Defendants SafeNet and Mueller directly or indirectly, knowingly or recklessly in the offer or sale of SafeNet securities, by use of the means or instruments of transportation or communication in interstate commerce, or by use of the mails, employed devices, schemes or artifices to defraud.

132. By engaging in the conduct alleged above defendants SafeNet and Mueller violated Securities Act Section 17(a)(1) [15 U.S.C. § 77q(a)(1)].

**SECOND CLAIM**  
**Violations of Securities Act Sections 17(a)(2) and 17(a)(3)**  
**(As to Defendants SafeNet, Caputo, and Mueller)**

133. The Commission realleges and incorporates by reference each and every allegation contained in Paragraphs 1 through 132 above.

134. Defendants SafeNet, Caputo, and Mueller directly or indirectly, knowingly, recklessly or negligently, in the offer or sale of SafeNet securities, by use of the means or instruments of transportation or communication in interstate commerce, or by use of the mails: (a) obtained money or property by means of untrue statements of material fact or omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or (b) engaged in transactions, practices or courses of business which operated or would have operated as a fraud or deceit upon purchasers of SafeNet securities.

135. By engaging in the conduct alleged above, defendants SafeNet, Mueller, and Caputo violated Securities Act Sections 17(a)(2) and 17(a)(3) [15 U.S.C. §§ 77q(a)(2) and 77q(a)(3)].

**THIRD CLAIM**  
**Violations of Securities Act Sections 17(a)(2) and 17(a)(3)**  
**(As to Defendants Greenman, Wilroy, and Pasko)**

136. The Commission realleges and incorporates by reference each and every allegation contained in Paragraphs 1 through 21, and 67 through 129 above.

137. Defendants Greenman, Wilroy, and Pasko, directly or indirectly, knowingly, recklessly or negligently, in the offer or sale of SafeNet securities, by use of the means or

instruments of transportation or communication in interstate commerce, or by use of the mails:

(a) obtained money or property by means of untrue statements of material fact or omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or (b) engaged in transactions, practices or courses of business which operated or would have operated as a fraud or deceit upon purchasers of SafeNet securities.

138. By engaging in the conduct alleged above, defendants Greenman, Wilroy, and Pasko violated Securities Act Sections 17(a)(2) and 17(a)(3) [15 U.S.C. §§ 77q(a)(2) and 77q(a)(3)].

**FOURTH CLAIM**  
**Violations of Exchange Act Section 10(b) and**  
**Exchange Act Rule 10b-5 thereunder**  
**(As to Defendants SafeNet and Mueller)**

139. The Commission realleges and incorporates by reference each and every allegation contained in Paragraphs 1 through 138 above.

140. Defendants SafeNet and Mueller, directly or indirectly, by use of the means or instruments of interstate commerce, or of the mails, or of a facility of a national securities exchange, knowingly or recklessly: (a) employed devices, schemes, or artifices to defraud; (b) made untrue statements of a material fact or omitted to state a material fact, necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or (c) engaged in acts, transactions, practices, or courses of business which operated or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of securities.

141. By engaging in the conduct described above, defendants SafeNet and Mueller violated Exchange Act Section 10(b) [15 U.S.C. § 78j(b)] and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5].

142. In addition, by engaging in the conduct alleged above, defendant Mueller knowingly provided substantial assistance to SafeNet in its violations of the aforementioned provisions, thereby aiding and abetting SafeNet's violations of Exchange Act Section 10(b) [15 U.S.C. § 78j(b)] and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5].

**FIFTH CLAIM**  
**Violations of Exchange Act Section 14(a) and**  
**Exchange Act Rule 14a-9 thereunder**  
**(As to Defendants SafeNet, Mueller, and Caputo)**

143. The Commission realleges and incorporates by reference each and every allegation contained in Paragraphs 1 through 142 above.

144. Defendants SafeNet, Mueller, and Caputo, by the use of the mails or by any means or instrumentality of interstate commerce or of any facility of a national securities exchange or otherwise, solicited by means of a proxy statement, form of proxy, notice of meeting or other communication, written or oral, containing statements which, at the time and in light of the circumstances under which they were made, were false and misleading with respect to material facts, or omitted to state material facts necessary in order to make the statements therein not false or misleading or necessary to correct statements in earlier communications with respect to the solicitation of the proxy for the same meeting or subject matter which was false or misleading.

145. By engaging in the conduct alleged above, defendants SafeNet, Mueller, and Caputo violated Exchange Act Section 14(a) [15 U.S.C. § 78n(a)] and Exchange Act Rule 14a-9 [17 C.F.R. § 240.14a-9].

146. In addition, by engaging in the conduct alleged above, defendants Mueller and Caputo knowingly provided substantial assistance to SafeNet in its violations of the aforementioned provisions, thereby aiding and abetting SafeNet's violations of Exchange Act Section 14(a) [15 U.S.C. § 78n(a)] and Exchange Act Rule 14a-9 [17 C.F.R. § 240.14a-9].

**SIXTH CLAIM**  
**Violations of Exchange Act Section 13(b)(5) and Exchange Act Rule 13b2-1**  
**(As to Defendants Mueller and Caputo)**

147. The Commission realleges and incorporates by reference each and every allegation contained in Paragraphs 1 through 146 above.

148. Defendants Mueller and Caputo knowingly circumvented or knowingly failed to implement a system of internal accounting controls or knowingly falsified books, records or accounts subject to Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)].

149. Defendants Mueller and Caputo, directly or indirectly, falsified or caused to be falsified books, records or accounts subject to Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)].

150. By engaging in the conduct alleged above, defendants Mueller and Caputo violated Exchange Act Section 13(b)(5) [15 U.S.C. § 78m (b)(5)] and Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1].

**SEVENTH CLAIM**  
**Violations of Exchange Act Rule 13b2-1**  
**(As to Defendants Greenman, Wilroy, and Pasko)**

151. The Commission realleges and incorporates by reference each and every allegation contained in Paragraphs 1 through 21, and 67 through 129 above.



152. Defendants Greenman, Wilroy, and Pasko, directly or indirectly, falsified or caused to be falsified books, records or accounts subject to Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)].

153. By engaging in the conduct alleged above, defendants Greenman, Wilroy, and Pasko violated Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1].

**EIGHTH CLAIM**  
**Violations of Exchange Act Rule 13b2-2**  
**(As to Defendants Mueller and Caputo)**

154. The Commission realleges and incorporates by reference each and every allegation contained in Paragraphs 1 through 153 above.

155. Defendants Mueller and Caputo, directly or indirectly, (i) made, or caused to be made, materially false or misleading statements or (ii) omitted to state, or caused others to omit to state, material facts necessary in order to make statements made, in light of the circumstances under which they were made, not misleading, to an accountant in connection with an audit, review or examination of financial statements or the preparation or filing of a document or report required to be filed with the Commission.

156. By engaging in the conduct alleged above, defendants Mueller and Caputo violated Exchange Act Rule 13b2-2 [17 C.F.R. § 240.13b2-2].

**NINTH CLAIM**  
**Violations of Exchange Act Rule 13b2-2**  
**(As to Defendants Greenman, Wilroy, and Pasko)**

157. The Commission realleges and incorporates by reference each and every allegation contained in Paragraphs 1 through 21, and 67 through 129 above.

158. Defendants Greenman, Wilroy, and Pasko, directly or indirectly, (i) made, or caused to be made, materially false or misleading statements or (ii) omitted to state, or caused

others to omit to state, material facts necessary in order to make statements made, in light of the circumstances under which they were made, not misleading, to an accountant in connection with an audit, review or examination of financial statements or the preparation or filing of a document or report required to be filed with the Commission.

159. By engaging in the conduct alleged above, defendants Greenman, Wilroy, and Pasko violated Exchange Act Rule 13b2-2 [17 C.F.R. § 240.13b2-2].

**TENTH CLAIM**  
**Violations of Exchange Act Rule 13a-14**  
**(As to Defendants Mueller and Caputo)**

160. The Commission realleges and incorporates by reference each and every allegation contained in Paragraphs 1 through 159 above.

161. Defendant Mueller and Caputo signed false certifications in SafeNet's annual and quarterly reports.

162. By engaging in the conduct alleged above, defendants Mueller and Caputo violated Exchange Act Rule 13a-14 [17 C.F.R. § 240.13a-14].

**ELEVENTH CLAIM**  
**Violation of Exchange Act Section 16(a) and Rule 16a-3 Thereunder**  
**(As to Defendants Mueller and Caputo)**

163. The Commission realleges and incorporates by reference each and every allegation contained in Paragraphs 1 through 162 above.

164. Section 16(a) of the Exchange Act [15 U.S.C. § 78p(a)] and Rule 16a-3 thereunder [17 C.F.R. § 240.16a-3] require officers, directors and beneficial owners of more than ten percent of any class of equity security registered pursuant to Exchange Act Section 12 [15 U.S.C. § 78l] to file periodic reports disclosing any change of beneficial ownership of those securities.

165. Defendants Mueller and Caputo failed to file with the Commission Forms 4 to disclose their respective option grants within two days of the grant date.

166. By engaging in the conduct alleged above, defendants Mueller and Caputo violated Section 16(a) of the Exchange Act [15 U.S.C. § 78p (a)] and Exchange Act Rule 16a-3 [17 C.F.R. § 240.16a-3].

**TWELTH CLAIM**  
**SafeNet's Violations of Exchange Act Section 13(a)**  
**and Exchange Act Rules 12b-20, 13a-1, 13a-11, and 13a-13 thereunder,**  
**and Aiding and Abetting of These Violations**  
**(As to all Defendants)**

167. The Commission realleges and incorporates by reference Paragraphs 1 through 166 above.

168. Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)], and Rules 13a-1, 13a-11, and 13a-13 [17 C.F.R. §§ 240.13a-1, 240.13a-11, and 240.13a-13] thereunder, require issuers of registered securities to file with the Commission factually accurate annual, quarterly, and current reports. Exchange Act Rule 12b-20 [17 C.F.R. § 240.12b-20] further provides that, in addition to the information expressly required to be included in a statement or report, there shall be added such further material information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they were made, not misleading.

169. By engaging in the conduct alleged above, defendant SafeNet violated Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Exchange Act Rules 12b-20, 13a-1, 13a-11, and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, and 240.13a-13].

170. By engaging in the conduct alleged above, defendants Mueller and Caputo knowingly provided substantial assistance to SafeNet's violations of the aforementioned provisions, thereby aiding and abetting SafeNet's violations of the Exchange Act Section 13(a)

[15 U.S.C. § 78m(a)] and Exchange Act Rules 12b-20, 13a-1, 13a-11, and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, and 240.13a-13].

171. By engaging in the conduct alleged above in paragraphs 1 through 21, and 67 through 129, defendants Greenman, Wilroy, and Pasko knowingly provided substantial assistance to SafeNet's violations of the aforementioned provisions, thereby aiding and abetting SafeNet's violations of the Exchange Act Section 13(a) [15 U.S.C. § 78m(a)] and Exchange Act Rules 12b-20, 13a-1, 13a-11, and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, and 240.13a-13].

**THIRTEENTH CLAIM**  
**SafeNet's Violations of Exchange Act Sections 13(b)(2)(A) and 13(b)(2)(B),**  
**and Aiding and Abetting of These Violations**  
**(As to all Defendants)**

172. The Commission realleges and incorporates by reference Paragraphs 1 through 171 above.

173. Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)] requires issuers to make and keep books, records, and accounts which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of its assets. Section 13(b)(2)(B) of the Exchange Act [15 U.S.C. § 78m(b)(2)(B)] requires issuers to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that transactions were recorded as necessary to permit preparation of financial statements in conformity with GAAP and to maintain the accountability of assets.

174. By engaging in the conduct alleged above, defendant SafeNet violated Exchange Act Sections 13(b)(2)(A) and 13(b)(2)(B) [15 U.S.C. §§ 78m(b)(2)(A) and 78m(b)(2)(B)].

175. By engaging in the conduct alleged above, defendants Mueller and Caputo knowingly provided substantial assistance to SafeNet in its violations of the aforementioned

provisions, thereby aiding and abetting SafeNet's violations of Exchange Act Sections 13(b)(2)(A) and 13(b)(2)(B) [15 U.S.C. §§ 78m(b)(2)(A) and 78m(b)(2)(B)].

176. By engaging in the conduct alleged above in paragraphs 1 through 21, and 69 through 131, defendants Greenman, Wilroy, and Pasko knowingly provided substantial assistance to SafeNet in its violations of the aforementioned provisions, thereby aiding and abetting SafeNet's violations of Exchange Act Sections 13(b)(2)(A) and 13(b)(2)(B) [15 U.S.C. §§ 78m(b)(2)(A) and 78m(b)(2)(B)].

**FOURTEENTH CLAIM**  
**Violations of Regulation G**  
**by SafeNet, Mueller, and Caputo**

177. The Commission realleges and incorporates by reference Paragraphs 1 through 176 above.

178. Regulation G provides, among other things, that a registrant, or a person acting on its behalf, shall not make public a non-GAAP financial measure that, taken together with the information accompanying that measure and any other accompanying discussion of that measure, contains an untrue statement of a material fact or omits to state a material fact necessary in order to make the presentation of the non-GAAP financial measure, in light of the circumstances under which it is presented, not misleading.

179. By engaging in the conduct alleged above defendants SafeNet, Mueller, and Caputo violated Regulation G [17 C.F.R. § 244.100].

**PRAYER FOR RELIEF**

WHEREFORE, the Commission respectfully prays that this Court:

- a) permanently enjoin defendant SafeNet from violating Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Regulation G [17 C.F.R. § 244.100], Sections 10(b), 13(a),

13(b)(2)(A), 13(b)(2)(B), and 14(a) of the Exchange Act [15 U.S.C. §§ 78j(b), 78m(a), 78m(b)(2)(A), 78m(b)(2)(B), and 78n(a)], and Rules 10b-5, 12b-20, 13a-1, 13a-11, 13a-13, and 14a-9 thereunder [17 C.F.R. §§ 240.10b-5, 240.12b-20, 240.13a-1, 240.13a-11, 240.13a-13, and 240.14a-9];

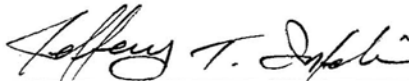
- b) permanently enjoin defendant Caputo from violating Sections 17(a)(2) and 17(a)(3) of the Securities Act [15 U.S.C. §§ 77q(a)(2) and 77q(a)(3)], Regulation G [17 C.F.R. § 244.100], Sections 13(b)(5), 14(a), and 16(a) of the Exchange Act [15 U.S.C. 78m(b)(5), 78n(a), and 78p(a)], and Rules 13a-14, 13b2-1, 13b2-2, 14a-9, and 16a-3 thereunder [17 C.F.R. §§ 240.13a-14, 240.13b2-1, 240.13b2-2, 240.14a-9, and 240.16a-3], and aiding and abetting violations of Exchange Act Sections 13(a), 13(b)(2)(A), 13(b)(2)(B), and 14(a) [15 U.S.C. §§ 78m(a), 78m(b)(2)(A), 78m(b)(2)(B), and 78n(a)], and Rules 12b-20, 13a-1, 13a-11, 13a-13, and 14a-9 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, 240.13a-13, and 240.14a-9].
- c) permanently enjoin defendant Mueller from violating Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Regulation G [17 C.F.R. § 244.100], and Sections 10(b), 13(b)(5), 14(a), and 16(a) of the Exchange Act [15 U.S.C. §§ 78j(b), 78m(b)(5), 78n(a), and §78p(a)], and Rules 10b-5, 13a-14, 13b2-1, 13b2-2, 14a-9, and 16a-3 thereunder [17 C.F.R. §§ 240.10b-5, 240.13a-14, 240.13b2-1, 240.13b2-2, 240.14a-9, and 240.16a-3], and aiding and abetting violations of Exchange Act Sections 10(b), 13(a), 13(b)(2)(A), 13(b)(2)(B), and 14(a) [15 U.S.C. §§ 78j(b), 78m(a), 78m(b)(2)(A), 78m(b)(2)(B), and 78n(a)], and Rules 10b-5, 12b-20, 13a-1, 13a-11,

13a-13, and 14a-9 thereunder [17 C.F.R. §§ 240.10b-5, 240.12b-20, 240.13a-1, 240.13a-11, 240.13a-13, and 240.14a-9].

- d) permanently enjoin defendants Greenman, Wilroy, and Pasko from violating Sections 17(a)(2) and 17(a)(3) of the Securities Act [15 U.S.C. §§ 77q(a)(2) and 77q(a)(3)], Exchange Act Rules 13b2-1 and 13b2-2 [17 C.F.R. §§ 240.13b2-1 and 240.13b2-2], and aiding and abetting violations of Exchange Act Sections 13(a), 13(b)(2)(A) and 13(b)(2)(B) [15 U.S.C. §§ 78m(a), 78m(b)(2)(A), and 78m(b)(2)(B)] and Rules 12b-20, 13a-1, 13a-11, and 13a-13 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, and 240.13a-13].
- e) order defendants Mueller, Caputo, and Greenman to disgorge, with prejudgment interest, all ill-gotten gains, compensation, and benefits derived as a result of their violations;
- f) pursuant to Securities Act Section 20(a) [15 U.S.C. § 77t(a)] and Exchange Act Section 21(d)(3) [15 U.S.C. § 78u(d)(3)], order defendants SafeNet, Caputo, Mueller, Greenman, Wilroy, and Pasko to pay civil money penalties;
- g) pursuant to Securities Act Section 20(e) [15 U.S.C. § 77t(e)] and Exchange Act Section 21(d)(2) [15 U.S.C. § 78u(d)(2)], prohibit defendant Mueller from acting as an officer or director of any issuer that has a class of securities registered pursuant to Exchange Act Section 12 [15 U.S.C. § 78l] or that is required to file reports pursuant to Exchange Act Section 15(d) [15 U.S.C. § 78o(d)]; and
- h) grant such other relief as the Court may deem just and appropriate.

Dated: November 10, 2009  
Washington, DC

Respectfully submitted,



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