

1 Co-Lead Plaintiffs Evan Warsh and Stephen Neville (“Plaintiffs”), derivatively on
2 behalf of Maxwell Technologies, Inc. (“Maxwell” or the “Company”), submit this
3 Verified Consolidated Shareholder Derivative Complaint against:

- 4 (a) the eight members of Maxwell’s Board of Directors (the “Board”) and two
5 Maxwell officers (collectively, the “Individual Defendants”) for breaches of
6 fiduciary duties (Count I), gross mismanagement (Count II), abuse of
7 control (Count III), unjust enrichment (Count IV), and breach of duty of
8 honest services (Count V); and
- 9 (b) McGladrey LLP, Maxwell’s former outside auditor, for professional
10 negligence and accounting malpractice (Count VI) and aiding and abetting
11 breaches of fiduciary duty (Count VII).

12 In support of these derivative claims, Plaintiffs allege as follows:

13 **NATURE OF THE ACTION**

- 14 1. This is a shareholder derivative action brought to remedy the wrongdoing
15 committed by Maxwell’s directors and officers and by Maxwell’s outside auditor
16 between April 28, 2011 and the present (the “Relevant Period”).
- 17 2. Headquartered in San Diego, California, Maxwell is a Delaware
18 corporation that develops, manufactures, and markets: (a) energy-storage and power
19 delivery products for transportation, industrial use, telecommunications, and other
20 applications; and (b) microelectronic products for space and satellite applications.
- 21 3. During the Relevant Period, the Individual Defendants breached their
22 fiduciary duties as Maxwell’s officers and directors by causing Maxwell to issue false and
23 misleading statements regarding its financial condition. The Individual Defendants also
24 breached their fiduciary duties by falsely representing that Maxwell maintained
25 adequate internal controls when, in fact, they knew that such controls were materially
26 deficient. The lack of adequate internal controls caused Maxwell to misrepresent its
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1 revenues and income, thereby violating the Generally Acceptable Accounting Principles
2 (“GAAP”) and Maxwell’s internal accounting standards.

3 4. The Individual Defendants completely abdicated their duties to ensure
4 adequate internal controls over Maxwell’s financial reporting. Specifically, the members
5 of Maxwell’s Audit Committee were responsible for, among other things, reviewing and
6 approving Maxwell’s financial statements, after discussing the statements with
7 Maxwell’s management and its outside auditor, McGladrey LLP. But the Audit
8 Committee members failed to perform such duties, or performed them in such cursory
9 and perfunctory manner as to constitute bad faith and a complete abdication of their
10 fiduciary duties as directors. As a result, Maxwell was forced to:

- 11 (a) conduct an internal investigation regarding, among other things, its
12 improper revenue recognition;
- 13 (b) announce that its financial statements issued in 2011 and 2012
14 should not be relied upon;
- 15 (c) appoint BDO USA, LLP to replace McGladrey LLP as Maxwell’s new
16 auditor; and
- 17 (d) ultimately restate the financial statements for 2011 and 2012.

18 5. The Individual Defendants’ breaches of their fiduciary duties have
19 subjected Maxwell to multiple lawsuits and have already cost, and will continue to cost,
20 Maxwell millions of dollars.

21 6. The Individual Defendants’ misconduct is particularly glaring in light of
22 the fact that in January 2011, Maxwell entered into a deferred prosecution agreement
23 with the United States Department of Justice, paying \$8 million to settle criminal
24 charges that Maxwell violated the Foreign Corrupt Practices Act (“FCPA”). *See United*
25 *States v. Maxwell Techs., Inc.*, No. 11cr0329 JM (S.D. Cal.), Dkt. No. 2. In addition,
26 Maxwell paid \$6.3 million in disgorgement to resolve civil charges by the U.S. Securities
27

1 and Exchange Commission (“SEC”). These charges arose from, among other things,
2 Maxwell’s lack of internal controls and the falsification of its books and records.

3 7. Similarly, during the Relevant Period, the Individual Defendants caused
4 Maxwell to (a) overstate its revenues because of false accounting entries in Maxwell’s
5 books and records; and (b) issue materially false and misleading statements regarding
6 its financial performance and business prospects. As a result, Maxwell stock traded at
7 artificially-inflated prices, reaching a high of \$21.20 per share on November 4, 2011.

8 8. On March 7, 2013, the Individual Defendants caused Maxwell to issue a
9 press release disclosing that the Company would be restating previously-issued financial
10 statements for 2011 and most of 2012 due to errors related to the timing of recognition
11 of revenue from sales to certain distributors. Maxwell further disclosed that the
12 financial statements should no longer be relied upon. The release stated:¹

13 ***Maxwell Technologies, Inc. announced today that***
14 ***on March 1, 2013, the audit committee of its board***
15 ***of directors concluded that the previously issued***
16 ***financial statements*** contained in its annual report on
17 Form 10-K for the year ended December 31, 2011, and all
18 unaudited quarterly reports on Form 10-Q in 2011 and 2012
(collectively, the “Prior Periods”), as well [as] its selected
19 financial data for the related periods, ***should no longer be***
20 ***relied upon because of errors in those financial***
21 ***statements.*** The errors relate to the timing of recognition
22 of revenue from sales to certain distributors.

23 In addition to the financial statements for the Prior Periods,
24 related press releases furnished on current reports on Form
25 8-K, reports and stockholder communications describing its
26 financial statements for the Prior Periods and the report of
27 its independent registered public accounting firm,
28 McGladrey LLP (formerly McGladrey & Pullen, LLP), related
to the year ended December 31, 2011, should no longer be
relied upon.

The conclusion that the financial statements for the Prior
Periods cannot be relied upon is the result of an investigation
by Maxwell’s audit committee, with the assistance of
independent outside counsel and forensic accountants. The
investigation commenced following receipt of information

1 All emphasis added unless otherwise noted.

1 concerning potential recognition of revenue prior to the
2 satisfaction of certain of the criteria required to be met to
3 recognize revenue.

4 ***The investigation discovered arrangements with***
5 ***certain distributors regarding the payment terms***
6 ***for sales to such distributors with respect to certain***
7 ***transactions.*** These arrangements had not been
8 communicated to Maxwell's finance and accounting
9 department and, therefore, had not been considered when
10 recording revenue on shipments to these distributors. Based
11 on the terms of the agreements with these distributors as
12 they were known to the finance and accounting department,
13 it had been the policy to account for revenue related to
14 shipments to these distributors as title passed to the
15 distributor at either shipment from Maxwell's facilities or
16 receipt at the distributor's facility, assuming all other
17 revenue recognition criteria had been achieved. ***As a result***
18 ***of the arrangements discovered during the***
19 ***investigation, Maxwell does not believe that a fixed***
20 ***or determinable sales price existed at the time of***
21 ***shipment to these distributors,*** nor was collection
22 reasonably assured, at least with respect to certain
23 transactions. ***Therefore, the revenue from such sales***
24 ***should not have been recognized at the time of***
25 ***shipment to these distributors.***

26 Maxwell believes that the impact to the Prior Periods of
27 correcting the errors in revenue recognition related to sales
28 transactions to these distributors will be to decrease
previously reported revenues and profits for 2011 and the
first three quarters of 2012, and to increase revenue and
profits by the same amounts in subsequent periods.

Maxwell believes that the restatement of revenue
related to these distributors will decrease
previously reported revenues for fiscal year 2011
by approximately \$6.5 million and decrease
revenues in the first three quarters of 2012 by
approximately \$5.5 million in the aggregate.

Maxwell also believes that the restatement of revenue related
to these distributors will result in shipments to these
distributors for which title has passed to the distributor, but
for which the revenue recognition criteria has not been fully
achieved, of approximately \$12.0 million as of September 30,
2012. Of the shipments to these distributors that had not
been collected as of September 30, 2012, and therefore not
recognized as revenue, Maxwell collected \$4.6 million in the
fourth quarter of 2012 and \$3.0 million to date in the first
quarter of 2013, leaving \$4.4 million outstanding that will be
recognized as revenue as Maxwell receives payments in the
future.

1 Maxwell is in the process of evaluating deficiencies in its
2 internal controls over financial reporting and [has]
3 preliminarily concluded that it has material weaknesses in its
4 internal controls over financial reporting related to the
5 identification and evaluation of revenue transactions which
6 deviate from contractually established payment terms and
7 therefore has preliminarily concluded that its internal
8 controls over financial reporting and disclosure are not
9 effective. Maxwell intends to design and implement controls
10 to remediate these deficiencies.

11 As a result of the investigation, certain employees were
12 terminated and Maxwell's Sr. Vice President of Sales and
13 Marketing resigned.

14 9. On this news, Maxwell's stock price closed at \$8.10 per share, with a one-
15 day decline of 11% on volume of 1.7 million shares.

16 10. On April 2, 2013, Maxwell announced that it appointed BDO USA, LLP to
17 replace Defendant McGladrey as Maxwell's new independent auditor, causing Maxwell's
18 stock to drop further to \$4.98 per share.

19 11. On August 1, 2013, Maxwell restated its financial results for fiscal years
20 2011 and 2012, revealing the extent of its overstatement in revenues. Overall, the
21 Company admitted that it had misrepresented a total of \$19.2 million in revenues: \$10
22 million in 2011 and \$9.2 million for the first three quarters of 2012. This exceeded by
23 60% the \$12 million estimate the Company initially provided (\$6.5 million for 2011 and
24 \$5.5 million for the three quarters in 2012).

25 12. In its 2012 Form 10-K, filed the same day, the Company explained that it
26 had been regularly, improperly pulling revenue forward at quarter's end starting from
27 the first quarter 2011 through the third quarter 2012, and that the recognition of such
28 revenue violated GAAP because: (1) no fixed or determinable price existed at the time of
shipment of certain goods, given the existence of certain profit margin protection
agreements and the potential for customer credit offsets; (2) collection of such revenue
was not sufficiently certain, given the existence of certain return periods; (3) the
transaction involved extended payment terms; and/or (4) title had not yet passed to the
customer concerning goods for which revenue was improperly recognized.

1 13. In its 2012 Form 10-K, Maxwell identified the following material
2 weaknesses as contributing to the restatement:

- 3 • ***[W]e did not maintain adequately designed***
4 ***controls to ensure accurate recognition of***
5 ***revenue in accordance with GAAP.*** Specifically,
6 controls were not effective to ensure that deviations
7 from contractually established sales terms were
8 authorized, communicated, identified and evaluated
9 for their potential effect on revenue recognition.
10 Further, we did not adequately train and supervise
11 sales personnel to ensure that such personnel were
12 appropriately conscious of the requirement to
13 communicate deviations from contractually
14 established sales terms to finance and accounting
15 personnel in order for revenue recognition in our
16 financial statements to be accurately recorded.
- 17 • ***We did not perform a robust fraud risk***
18 ***assessment taking into consideration the***
19 ***various ways that fraud may be perpetrated***
20 ***to misappropriate assets or facilitate***
21 ***fraudulent financial reporting.*** We failed to
22 identify controls specifically designed to prevent and
23 detect fraud risks relating to revenue recognition.

24 14. An opinion letter provided by independent accountants hired by the
25 Company in connection with the restatement specifically found:

26 In our opinion, Maxwell Technologies, Inc. and subsidiaries
27 did not maintain, in all material respects, effective internal
28 control over financial reporting as of December 31, 2012,
based on criteria established in Internal Control—Integrated
Framework issues by the Committee of Sponsoring
Organizations of the Treadway Commission.

29 15. The true facts, which were known by the Individual Defendants but
30 concealed from the investing public and omitted from Maxwell's filings with the SEC
31 during the Relevant Period, included:

- 32 (a) Maxwell had overstated its revenues and earnings in 2011 and 2012
33 in violation of GAAP;
- 34 (b) Maxwell had reported revenues for sales prior to the time the sales
35 price was fixed or collection was reasonably assured; and

1 (c) Maxwell's internal accounting controls were deficient and
2 permitted the premature recognition of revenue, leading to materially misstated
3 financial results.

4 16. The Individual Defendants' misconduct caused Maxwell's common stock
5 to trade at artificially-inflated prices during the Relevant Period. After the foregoing
6 revelations of the true, but undisclosed, facts seeped into the market, the Company's
7 common stock experienced exorbitant selling pressure sending its price down nearly
8 62% from its Relevant Period high. As a result, Maxwell's market capitalization has
9 been severely diminished and its prospect of raising equity in the future is questionable.

10 JURISDICTION AND VENUE

11 17. This Court has jurisdiction over the action under Article VI, Section 10 of
12 the California Constitution.

13 18. Jurisdiction over all defendants is proper because they conduct business in
14 California, including, but not limited to, the misconduct alleged in this complaint, and
15 because they have sufficient minimum contacts with California to render the exercise of
16 jurisdiction by the California courts permissible under the traditional notions of fair
17 play and substantial justice.

18 19. Venue is proper in this Court because the events and conduct at issue took
19 place and have effect in the County of San Diego, and because Maxwell's headquarters
20 are located 3888 Calle Fortunada, San Diego, California 92123.

21 20. Plaintiffs have complied with all of the requirements under Section 800 of
22 the California Corporations Code.

23 THE PARTIES

24 I. Plaintiffs

25 21. Plaintiff Evan Warsh is a shareholder of Maxwell and has been at all
26 relevant times.

1 22. Plaintiff Stephen Neville is a shareholder of Maxwell. Plaintiff Neville has
2 continuously held Maxwell stock during the Relevant Period.

3 **II. Nominal Defendant**

4 23. Nominal Defendant Maxwell Technologies, Inc. is a Delaware corporation
5 with its principal place of business located at 3888 Calle Fortunada, San Diego,
6 California 92123.

7 **III. The Individual Defendants**

8 **A. The Director Defendants**

9 24. Defendant José L. Cortes has been a Class I director of Maxwell since
10 2002.

11 25. Defendant Roger Howsmon has been a Class I director of Maxwell since
12 2008. Howsmon is a member of Maxwell's Compensation Committee.

13 26. Defendant Burkhard Goeschel has been a Class II director of Maxwell
14 since 2007. Goeschel is a member of Maxwell's Governance and Nominating
15 Committee.

16 27. Defendant Jean Lavigne has been a Class II director of Maxwell since
17 1999. Lavigne is a member of Maxwell's Compensation Committee and Nominating
18 Committee.

19 28. Defendant Mark Rossi has been a Class II director of Maxwell since 1997.
20 Rossi was elected Chairperson of the Board in May 2011. Rossi is a member of
21 Maxwell's Audit Committee and Governance and Nominating Committee; Rossi is the
22 Chairperson of Maxwell's Compensation Committee.

23 29. Defendant Robert Guyett has been a Class III director of Maxwell since
24 2000. Between May 2010 and May 2011, Guyett served as the Chairperson of the Board.
25 Guyett is a member of Maxwell's Compensation Committee and Governance and
26 Nominating Committee; Guyett is the Chairperson of Maxwell's Audit Committee.

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1 30. Defendant Yon Yoon Jordan has been a Class III director of Maxwell since
2 2008. Jordan is a member of the Audit Committee and the Chairperson of the
3 Governance and Nominating Committee.

4 31. Defendant David J. Schramm has been a Class III director, President, and
5 Chief Executive Officer (“CEO”) of Maxwell since 2007.

6 32. Defendants Cortes, Howsmon, Goeschel, Lavigne, Rossi, Guyett, Jordan,
7 and Schramm are collectively referred to as the “Director Defendants.”

8 33. Defendants Guyett, Jordan, and Rossi are collectively referred to as the
9 “Audit Committee Defendants.”

10 **B. The Officer Defendants**

11 34. Defendant Kevin S. Royal is the Chief Financial Officer (“CFO”) of
12 Maxwell. Royal signed Maxwell’s SEC filings and participated in conference calls with
13 analysts and investors during the Relevant Period.

14 35. Defendant Van M. Andrews was Maxwell’s Senior Vice President, Sales
15 and Marketing during the Relevant Period, until his resignation on March 1, 2013.

16 36. Defendants Schramm, Royal, and Andrews are collectively referred to as
17 the “Officer Defendants.”

18 **C. McGladrey**

19 37. Defendant McGladrey LLP (“McGladrey”) (formerly known as McGladrey
20 & Pullen, LLP) is an accounting firm with 75 offices across the United States. Upon
21 information and belief, McGladrey maintains several offices in California, including one
22 in this County (located at 1455 Frazee Road, Suite 600, San Diego, California 92108).
23 McGladrey was Maxwell’s outside auditor during the Relevant Period, until its
24 resignation on March 19, 2013. McGladrey audited Maxwell’s financial results stated in
25 its Form 10-K dated February 16, 2012 and its Form 10-Qs issued in 2011 and 2012, all
26 of which were subject to Maxwell’s restatement.

1 (b) conduct the affairs of the Company in an efficient, business-like
2 manner so as to make it possible to provide the highest quality performance of its
3 business, to avoid wasting the Company's assets, and to maximize the value of the
4 Company's stock;

5 (c) remain informed as to how Maxwell conducted its operations, and,
6 upon receipt of notice or information of imprudent or unsound conditions or
7 practices, to make reasonable inquiry in connection therewith, and to take steps
8 to correct such conditions or practices;

9 (d) establish and maintain systematic and accurate records and reports
10 of the business and internal affairs of Maxwell and procedures for the reporting
11 of the business and internal affairs to the Board and to periodically investigate, or
12 cause independent investigation to be made of, said reports and records;

13 (e) maintain and implement an adequate and functioning system of
14 internal legal, financial, and management controls, such that Maxwell's
15 operations would comply with all laws and its financial statements filed with the
16 SEC and disseminated to the public and Maxwell's shareholders would be
17 accurate;

18 (f) exercise reasonable control and supervision over the public
19 statements made by the Company's officers and employees and any other reports
20 or information that the Company was required by law to disseminate; and

21 (g) examine and evaluate any reports of examinations, audits, or other
22 financial information concerning the financial affairs of the Company and to
23 make full and accurate disclosure of all material facts concerning, among other
24 things, each of the subjects and duties set forth above.

25 43. As senior executive officers and directors of a publicly-traded company
26 whose common stock was registered with the SEC pursuant to the Securities Exchange
27 Act of 1934 (the "Exchange Act") and traded on NASDAQ, the Individual Defendants
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1 had a duty to disseminate accurate and truthful information with respect to the
2 Company's financial condition and performance, growth, operations, financial
3 statements, business, products, management, earnings, and present and future business
4 prospects; and to correct any previously-issued statements that had become materially
5 misleading or untrue, so that the market price of the Company's common stock would
6 be based upon truthful and accurate information. The Individual Defendants'
7 misrepresentations and omissions during the Relevant Period violated these specific
8 requirements and obligations. Thus, the Individual Defendants breached their fiduciary
9 duties by causing or recklessly permitting violations of the federal securities laws.

10 **II. Compliance with GAAP**

11 44. In issuing its financial statements, Maxwell was required to comply with
12 GAAP – a common set of accounting principles, standards, and procedures recognized
13 by the accounting profession and used to compile financial statements.

14 45. In fact, Maxwell stated in its Forms 10-K dated March 6, 2010 and
15 February 16, 2012 that “[t]he accompanying consolidated financial statements include
16 the accounts of Maxwell Technologies, Inc. and its subsidiaries and have been prepared
17 in accordance with [GAAP].”

18 46. In reality, however, the Individual Defendants failed to ensure that
19 Maxwell adhered to GAAP during the Relevant Period.

20 **III. Compliance with Maxwell's Revenue-Recognition Policy**

21 47. Maxwell's Form 10-K dated March 10, 2011 stated the following with
22 respect to Maxwell's "Revenue Recognition":

23 Revenue is derived primarily from the sale of
24 manufactured products directly to customers. For certain
25 long-term contracts, revenue is recognized at the time costs
26 are incurred. Product revenue is recognized, according to the
27 guidelines of the [SEC] Staff Accounting Bulletin ("SAB")
28 Numbers 101, Revenue Recognition in Financial Statements,
and 104, Revenue Recognition, when all of the following
criteria are met: (1) persuasive evidence of an arrangement
exists (upon contract signing or receipt of an authorized
purchase order from a customer); (2) title passes to the

1 customer at either shipment from the Company's facilities or
2 receipt at the customer facility, depending on shipping
3 terms; (3) customer payment is deemed fixed or
4 determinable and free of contingencies or significant
5 uncertainties; and (4) collectability is reasonably assured. If
6 a volume discount is offered, revenue is recognized at the
7 lowest price to the customer. This method has been
8 consistently applied from period to period and there is no
9 right of return.

6 Revenue generated from fixed price contracts is
7 recognized on a percentage of completion basis measured by
8 the percentage of cost incurred to date to the estimated costs
9 for each contract, as required by the Construction-Type and
10 Production-Type Contracts Subtopic of the Financial
11 Accounting Standards Board Accounting Standards
12 Codification ("FASB ASC"), and is limited by the funding of
13 the prime contractor. Provisions for estimated losses on
14 incomplete contracts are made in the period in which such
15 losses are determined.

11 From time to time the Company has entered into
12 multiple-element contractual arrangements with elements of
13 software that are essential to the functionality of the
14 delivered elements. Additionally, the Company has contracts
15 where all the elements of the agreement need to be delivered
16 and accepted by the customer prior to any revenue being
17 recognized for the agreement. The Company recognizes
18 revenue on the delivered elements when vendor-specific
19 objective evidence ("VSOE") of the fair value of the
20 undelivered elements exists in accordance with the Software
21 Revenue Recognition Subtopic of the FASB ASC. In 2007,
22 the Company entered into a contract whereby the Company
23 delivered certain elements and VSOE of fair value of the
24 undelivered elements did not exist at the time certain
25 elements were delivered. During the year ended December
26 31, 2010, the Company recorded \$3.0 million of revenue that
27 had previously been deferred related to this contract.

20 48. Similarly, Maxwell's Form 10-K dated February 16, 2012 stated the
21 following with respect to Maxwell's "Revenue Recognition":

22 Revenue is derived primarily from the sale of
23 manufactured products directly to customers. Product
24 revenue is recognized, according to the guidelines of the
25 Securities and Exchange Commission ("SEC") Staff
26 Accounting Bulletin ("SAB") Numbers 101, Revenue
27 Recognition in Financial Statements, and 104, Revenue
28 Recognition, when all of the following criteria are met: (1)
persuasive evidence of an arrangement exists (upon contract
signing or receipt of an authorized purchase order from a
customer); (2) title passes to the customer at either shipment
from the Company's facilities or receipt at the customer
facility, depending on shipping terms; (3) customer payment

1 is deemed fixed or determinable and free of contingencies or
2 significant uncertainties; and (4) collectability is reasonably
3 assured. If a volume discount is offered, revenue is
4 recognized at the lowest price to the customer. This method
5 has been consistently applied from period to period and
6 there is no right of return.

7 Revenue generated from certain long-term, fixed price
8 contracts is recognized either on a percentage of completion
9 basis or on a milestone basis, depending on which method
10 management determines best reflects the progress of
11 performance under the contract. Under the milestone
12 method, revenue is recognized for the contractual
13 consideration that is contingent upon achievement of a
14 milestone in its entirety as revenue in the period the
15 milestone is achieved if the milestone is determined to be
16 substantive. Under the percentage of completion basis,
17 revenue is measured by the percentage of cost incurred to
18 date to the estimated costs for each contract, as required by
19 the Construction-Type and Production-Type Contracts
20 Subtopic of the Financial Accounting Standards Board
21 Accounting Standards Codification ("FASB ASC"), and is
22 limited by the funding of the prime contractor. Provisions for
23 estimated losses on incomplete contracts are made in the
24 period in which such losses are determined.

25 **IV. Regulation S-X's Presumption of Inaccuracy**

26 49. Regulation S-X, 17 C.F.R. § 210.4-01(a)(1), provides that financial
27 statements filed with the SEC that are not prepared in accordance with GAAP "will be
28 presumed to be misleading or inaccurate." During the Relevant Period, the Individual
29 Defendants failed to ensure that Maxwell's financial statements complied with GAAP.

30 50. Specifically, under GAAP, as set forth in the Statement of Financial
31 Accounting Standards ("SFAS") 48 issued by the Financial Accounting Standards Board
32 ("FASB"), revenue can only be recognized and booked in the period in which it is
33 substantially earned.

34 51. Similarly, FASB's Statement of Financial Accounting Concepts No. 5
35 ("FASB CON No. 5") provides that for revenue to be recognizable, it must be: (1) realized
36 or realizable; and (2) earned.

37 52. Likewise, the SEC's Staff Accounting Bulletin No. 104 on "Revenue
38 Recognition," which establishes guidelines regarding the timing of revenue recognition

1 based on factors such as passage of title, installation, payments, and client acceptance,
2 states:

3 [R]evenue should not be recognized until it is realized or
4 realizable and earned. . . . [Concepts Statement 5,
5 Paragraph 84(a) [states that] “the two conditions (being
6 realized or realizable and being earned) are usually met by
7 the time product or merchandise is delivered or services are
8 rendered to customers, and revenues from manufacturing
9 and selling activities and gains and losses from sales of other
10 assets are commonly recognized at time of sale (usually
11 meaning delivery).” . . .

12 The staff believes that revenue generally is realized or
13 realizable and earned when all of the following criteria are
14 met:

- 15 • Persuasive evidence of an arrangement exists,
- 16 • Delivery has occurred or services have been
17 rendered,
- 18 • The seller’s price to the buyer is fixed or
19 determinable, and
- 20 • Collectibility is reasonably assured.

21 Some revenue arrangements contain multiple revenue-
22 generating activities. The staff believes that the
23 determination of the units of accounting within an
24 arrangement should be made prior to the application of the
25 guidance in this SAB Topic by reference to the applicable
26 accounting literature.

27 53. By causing the Company to record non-existent revenue and to record
28 revenue before it was earned, the Individual Defendants not only violated the
29 Company’s own internal policy regarding revenue recognition, but they also violated
30 GAAP by not complying with the following: (1) the SFAS 48, (2) the FASB CON No. 5,
31 and (3) the SEC’s Staff Accounting Bulletin No. 104.

32 54. Because the Company’s financial statements filed with the SEC were not
33 prepared in accordance with GAAP, they are “presumed to be misleading or inaccurate”
34 under Regulation S-X.

35 **V. Compliance with the Code of Business Conduct and Ethics**

36 55. The Code of Business Conduct and Ethics “describes the core values and
37 beliefs of Maxwell and provides the foundation for all business conduct. Our guidelines
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1 for conducting Maxwell business are consistent with the highest standards of business
2 ethics.” The code applies to Maxwell’s directors, officers and other employees, and
3 requires them to “follow specific guidelines in managing its records.” The Code of
4 Ethics states that all employees “must adhere to the Company’s business and legal
5 requirements in managing records, including all recorded information regardless of
6 medium or characteristics.”

7 56. With regard to “Financial Responsibility and Authorization,” the code
8 provides:

9 Maxwell employee[s] must ensure that no false or
10 intentionally misleading entries are made in Maxwell’s
11 accounting records. Intentional misclassification of
12 transactions regarding accounts, departments, or accounting
13 periods violate the law and the Code. **All transactions
must be supported by accurate documentation in
reasonable detail, recorded in the proper account
and in the proper accounting period.**

14 **If any employee has concerns or complaints
regarding questionable accounting, auditing or
15 other financial records, he or she must report those
concerns to the Audit Committee of the Board of
16 Directors, the Compliance Department or the Maxwell
Ethics Hotline.**

17 Employees must act with absolute financial and record-
18 keeping integrity in processing travel and expense reports
19 and other financial transactions. Employees must follow
20 requirements regarding responsibility and approval for
21 committing Maxwell financial or other resources. Cash or
22 other assets must not be maintained in any unrecorded or
23 “off-the-books” fund for any purpose. **Compliance with
Generally Accepted Accounting Principles (GAAP)
and the Company’s system of internal controls is
required at all times.** Proper justification is required
when alternative accounting treatment is possible under
GAAP.

24 VI. The Audit Committee Charter

25 57. During the Relevant Period, Defendants Guyett, Jorden, and Rossi were
26 members of the Audit Committee. Thus, they were obligated to ensure that Maxwell
27 maintained adequate internal controls.

1 obtained Statement on Auditing Standards No. 50 letters;
2 and (d) other material written communications between the
3 independent auditors and management.

4 **5. Discuss with management and the**
5 **independent auditors the adequacy and**
6 **effectiveness of the Company's financial staff and**
7 **accounting and financial controls,** including the
8 Company's systems to monitor and manage business risk,
9 and the Company's legal and ethical compliance programs.

10 6. Review with management and the independent
11 auditors the effect of regulatory and accounting initiatives as
12 well as off-balance sheet structures on the Company's
13 financial statements.

14 7. Discuss with the independent auditors the matters
15 required to be discussed by Statement on Auditing Standards
16 No. 114 relating to the conduct of the audit and any other
17 matters required to be communicated to the Audit
18 Committee by the independent auditors under generally
19 accepted auditing standards.

20 8. Discuss with the independent auditors significant
21 matters with respect to which they consulted their national
22 office, and, if so determined by the Audit Committee, discuss
23 such matters with the national office of the independent
24 auditors.

25 **9. Meet with the chief financial officer and the**
26 **independent auditors in separate executive**
27 **sessions to discuss issues relating to the quarterly**
28 **unaudited and annual audited financial**
statements. At least annually, inquire of the
independent auditors as to whether any director,
officer or employee of the Company has attempted
to fraudulently influence, coerce, manipulate or
mislead the auditors.

10. Review any disclosures made to the Audit
Committee by the chief executive officer and/or
chief financial officer during their certification
process for the Form 10-K and Form 10-Q regarding
any significant deficiencies in the design or
operation of internal controls or material
weaknesses therein and any fraud involving
management or other employees who have a
significant role in the Company's internal controls.

11. Obtain confirmation from the independent auditors
12 that Section 10A of the Securities Exchange Act of 1934 has
13 not been implicated.

14 12. Review with the independent auditors any problems
15 or difficulties the auditors may have encountered and any

1 management letter provided by the auditors and the
2 Company's response to that letter. Such review should
3 include any difficulties encountered in the course of the audit
4 work, including any restrictions on the scope of activities or
5 access to required information, and any disagreements with
6 management.

7 13. Based upon its reviews and discussions, the Audit
8 Committee shall recommend to the Board of Directors as to
9 whether the annual audited financial statements should be
10 included in the Company's Annual Report on Form 10-K.

11 14. Prepare the report required by the rules of the
12 Securities and Exchange Commission to be included in the
13 Company's annual proxy statement.

14 15. Review the content and clarity of communications
15 with the public regarding annual and quarterly operating
16 results prior to their release.

17 62. With respect to oversight, the Audit Committee is required to:

18 **1. Review the content and clarity of all material**
19 **communications with the public regarding changes**
20 **in financial projections prior to their release.**

21 **2. At least annually, review the Company's**
22 **"critical accounting policies" with management**
23 **and the independent auditors.**

24 3. Review major changes to the Company's auditing and
25 accounting policies, principles and practices as suggested by
26 the independent auditors or management.

27 4. Obtain reports from management, and, if so
28 determined by the Audit Committee, from the independent
auditors that the Company's subsidiary/foreign affiliated
entities are in conformity with applicable accounting and
internal controls requirements and the Company's Code of
Business Conduct and Ethics pertaining to such matters,
including disclosures of insider and affiliated party
transactions.

5. Review with management and the independent
auditors any correspondence with regulators or
governmental agencies and any employee complaints or
published reports that raise material issues regarding the
Company's financial statements or accounting policies.

6. Review with counsel legal compliance matters
including corporate securities trading policies and other legal
matters that may have a material impact on the financial
statements, the Company's compliance policies and any
material reports or inquiries received from regulators or
governmental agencies.

1 7. Oversee establishment and implementation of
2 procedures for receiving, retaining and investigating reports
3 of illegal acts pertaining to accounting or internal control
4 matters involving the Company detected by the independent
5 accountants or others and, in accordance with such
6 procedures, supervise the investigation of such reports of
7 illegal acts, review the actions taken or to be taken by the
8 Company to remediate such illegal acts, and, if appropriate,
9 recommend further action by the Board of Directors.
10 Oversee establishment and implementation of procedures
11 for the confidential, anonymous submission by employees of
12 the Company and others of concerns or complaints regarding
13 accounting or internal control matters and investigate any
14 such concerns or complaints.

15 8. Review and approve all related party transactions (as
16 defined in Section 404 of Regulation S-K) involving the
17 Company.

18 9. Review and discuss with management and the
19 independent auditors new or proposed accounting rules or
20 pronouncements that may affect the Company.

21 **10. *Review and update periodically concepts***
22 ***pertaining to accounting and internal controls***
23 ***topics within the Code of Business Conduct and***
24 ***Ethics*** and communicate same to the Governance
25 Committee.

26 **VII. The Duty of Reasonable and Prudent Supervision**

27 63. The Individual Defendants are required to exercise reasonable and
28 prudent supervision over the management, policies, practices, and internal controls of
the Company. By virtue of such duties, the Individual Defendants are required to,
among other things:

(a) ensure that Maxwell maintains adequate internal controls over
financial reporting;

(b) refrain from acting upon material inside corporate information to
benefit themselves;

(c) ensure that Maxwell complies with its legal obligations and
requirements, including acting only within the scope of its legal authority and
disseminating truthful and accurate statements to the investing public;

1 (d) conduct the affairs of the Company in an efficient, business-like
2 manner so as to make it possible to provide the highest quality performance of its
3 business, to avoid wasting the Company's assets, and to maximize the value of the
4 Company's stock;

5 (e) properly and accurately guide investors and analysts as to the true
6 financial condition of the Company at any given time, including making accurate
7 statements about the Company's financial results;

8 (f) remain informed as to how Maxwell conducted its operations, and,
9 upon receipt of notice or information of imprudent or unsound conditions or
10 practices, make reasonable inquiry in connection therewith, and take steps to
11 correct such conditions or practices and make such disclosures as necessary to
12 comply with securities laws; and

13 (g) ensure that Maxwell was operated in a diligent, honest, and prudent
14 manner in compliance with all applicable laws, rules, and regulations.

15 **BREACHES OF FIDUCIARY DUTIES**

16 64. Each Individual Defendant owed to Maxwell and to its shareholders the
17 fiduciary duty of loyalty and good faith, and the exercise of due care and diligence in
18 managing and overseeing Maxwell's affairs, as well as in the use and preservation of its
19 property and assets. The Individual Defendants' misconduct involves a knowing and
20 culpable violation of their obligations as directors and officers of Maxwell, the absence
21 of good faith on their part, or a reckless disregard of their duties that they were aware or
22 should have been aware posed a risk of serious injury to Maxwell. Each Individual
23 Defendant ratified each other's misconduct because they collectively comprised
24 Maxwell's Board and management at all relevant times.

25 65. The Individual Defendants each breached their duties of loyalty and good
26 faith by allowing Defendants to cause, or by themselves causing, the Company to make
27 false and/or misleading statements and/or failing to disclose that:

1 (a) the Company was improperly recording revenue, including the
2 creation of non-existent revenue and booking revenue in an earlier period than
3 when it was earned;

4 (b) as a result, the Company's revenue and financial results were
5 overstated by nearly \$20 million;

6 (c) the Company's financial statements were not prepared in
7 accordance with GAAP;

8 (d) the Company lacked adequate internal and financial controls; and

9 (e) as a result of the foregoing, the Company's financial statements
10 were materially false or misleading at all relevant times.

11 66. In addition, as a result of the Individual Defendants' actions and course of
12 conduct, the Company is now the subject of class action lawsuits that allege violations of
13 federal securities laws. As a result, Maxwell has expended, and will continue to expend,
14 significant sums of money to rectify the Individual Defendants' wrongdoing.

15 **CONTROL, ACCESS, AND AUTHORITY**

16 67. The Individual Defendants, because of their positions of control and
17 authority, were able to and did, directly or indirectly, exercise control over the wrongful
18 acts complained of herein, as well as the contents of the various public statements
19 issued by Maxwell.

20 68. Because of their advisory, executive, managerial, and directorial positions
21 with Maxwell, each of the Individual Defendants had access to adverse, non-public
22 information about the financial condition, operations, and improper representations of
23 Maxwell.

24 69. Each of the Individual Defendants was the agent of each of the other
25 Defendants and of Maxwell, and was at all times acting within the course and scope of
26 such agency.

27

28

CONSPIRACY, AIDING AND ABETTING, AND CONCERTED ACTION

1
2 70. In committing the wrongful acts alleged herein, Defendants have pursued,
3 or joined in the pursuit of, a common course of conduct, and have acted in concert with
4 and conspired with one another in furtherance of their wrongdoing. Defendants further
5 aided and abetted and/or assisted each other in breaching their respective duties.

6 71. During all times relevant hereto, Defendants collectively and individually
7 initiated a course of conduct that was designed to and did conceal the fact that: (a)
8 Maxwell was improperly recording revenue, including the creation of non-existent
9 revenue and booking revenue in an earlier period than when it was earned; (b) as a
10 result, Maxwell's revenue and financial results were overstated; (c) Maxwell's financial
11 statements were not prepared in accordance with GAAP; (d) Maxwell lacked adequate
12 internal and financial controls; and (e) as a result of the foregoing, Maxwell's financial
13 statements were materially false or misleading at all relevant times. In furtherance of
14 this plan, conspiracy, and course of conduct, Defendants collectively and individually
15 took the actions set forth herein.

16 72. Defendants engaged in a conspiracy, common enterprise, and/or common
17 course of conduct. During this time, Defendants caused Maxwell to issue false or
18 misleading financial results based upon non-existent revenue or based on revenue that
19 was improperly recorded in an earlier period than when it was earned.

20 73. The purpose and effect of the Individual Defendants' conspiracy, common
21 enterprise, and/or common course of conduct was, among other things, to: (a) disguise
22 the Individual Defendants' violations of law, including breaches of fiduciary duties, and
23 unjust enrichment; and (b) disguise and misrepresent the Company's future business
24 prospects.

25 74. Defendants accomplished their conspiracy, common enterprise, and/or
26 common course of conduct by causing Maxwell to falsely represent that Maxwell had
27 adequate internal controls in place, and by purposefully, recklessly, or negligently
28 causing Maxwell to release improper statements. Because the actions described herein

1 occurred under the authority of the Board, each of the Individual Defendants was a
2 direct, necessary, and substantial participant in the conspiracy, common enterprise,
3 and/or common course of conduct complained of herein.

4 75. Each Defendant aided and abetted and rendered substantial assistance in
5 the wrongs complained of herein. In taking such actions to substantially assist the
6 commissions of the wrongdoing complained of herein, each Defendant acted with
7 knowledge of the primary wrongdoing, substantially assisted the accomplishment of
8 that wrongdoing, and was aware of his (or her or its) overall contribution to and
9 furtherance of the wrongdoing.

10 **FACTUAL ALLEGATIONS**

11 76. Maxwell develops, manufactures, and markets energy-storage, power
12 delivery and microelectronic products worldwide. Maxwell offers ultracapacitors, which
13 are energy storage devices that provide energy storage and power delivery solutions for
14 applications in the transportation, automotive, information technology, renewable
15 energy, and industrial electronics industries; and CONDIS high-voltage capacitors
16 comprising grading and coupling capacitors, and capacitive voltage dividers used to
17 ensure the safety and reliability of electric utility infrastructure and other applications
18 involving transport, distribution, and measurement of high-voltage electrical energy.
19 Maxwell also provides radiation-hardened microelectronic products, including single-
20 board computers and components, such as high-density memory and power modules for
21 satellites and spacecraft applications. Maxwell markets and sells its products through
22 direct and indirect sales for integration by original equipment manufacturers into a
23 range of end products. Founded in 1965, Maxwell was listed and traded on the
24 NASDAQ global market under the ticker "MXWL" during the Relevant Period.

25 77. Maxwell's revenue was primarily derived from the sales of products. In
26 Maxwell's 2010 Form 10-K, the Company represented that its revenue recognition
27 policy for product sales was as follows:

1 *Assumptions and Approach Used.* Product revenue is
2 recognized when all of the following criteria are met: (1)
3 persuasive evidence of an arrangement exists (upon contract
4 signing or receipt of an authorized purchase order from a
5 customer); (2) title passes to the customer at either shipment
6 from our facilities or receipt at the customer facility,
7 depending on shipping terms; (3) price is deemed fixed or
8 determinable and free of contingencies or significant
9 uncertainties; and (4) collectability is reasonably assured.
10 Customer purchase orders and/or contracts are generally
11 used to determine the existence of an arrangement. Shipping
12 documents are used to verify product delivery. We assess
13 whether a price is fixed or determinable based upon the
14 payment terms associated with the transaction. If a volume
15 discount is offered, revenue is recognized at the lowest price
16 offered to the customer. We assess the collectability of
17 accounts receivable based primarily upon creditworthiness
18 of the customer as determined by credit checks and analysis,
19 as well as the customer's payment history.

20 **I. The False and Misleading Statements**

21 78. The statements set forth below regarding Maxwell's financial condition
22 and business prospects were false and misleading. And the Individual Defendants were
23 responsible for the issuance of these false and misleading statements.

24 79. On April 28, 2011, the Individual Defendants caused Maxwell to issue a
25 press release announcing its first quarter 2011 financial results. Maxwell reported net
26 income of \$196,000, or \$0.01 diluted earnings per share ("EPS"), and revenue of \$35.3
27 million for the first quarter ended March 31, 2011. Schramm stated the following about
28 Maxwell's business prospects:

 "Energy storage solutions for wind turbine blade pitch
 systems and hybrid and electric transit vehicle drive systems
 continued to be primary drivers of ultracapacitor sales
 growth, along with increasing contributions from automotive
 stop-start idle elimination systems and various backup
 power applications," said David Schramm, Maxwell's
 president and chief executive officer. "This strong top line
 growth and ongoing cost reduction and efficiency
 improvements also enabled the company to continue
 improving operating results."

 * * *

 "***We expect sequential top line growth of five to
 seven percent in the second quarter," Schramm
 said. "For the full year, we continue to expect top
 line growth of more than 20 percent over 2010, and***

1 ***steadily improving operating performance should***
2 ***enable the company to generate cash from***
3 ***operations and be profitable on a non-GAAP basis***
4 ***going forward.***”

5 80. On May 5, 2011, the Individual Defendants caused Maxwell to file its first
6 quarter 2011 Form 10-Q with the SEC. Defendants Schramm and Royal signed the
7 Form 10-Q, which referenced Maxwell’s Form 10-K for the year ended December 31,
8 2010, as well as to the Company’s accounting policies. Schramm and Royal each signed
9 internal control certifications as required by the Sarbanes–Oxley Act of 2002 (“SOX”),
10 affirming that they were responsible for designing “such internal control over financial
11 reporting, or [causing] such internal control over financial reporting to be designed
12 under [their] supervision, to provide reasonable assurance regarding the reliability of
13 financial reporting and the preparation of financial statements for external purposes in
14 accordance with generally accepted accounting principles,” and that they had reported
15 to the board and auditors “[a]ll significant deficiencies and material weaknesses in the
16 design or operation of internal controls over financial reporting which are reasonably
17 likely to adversely affect the registrant’s ability to record, process, summarize and report
18 financial information.”

19 81. Before approving the issuance of Maxwell’s quarterly financial reports, the
20 Audit Committee Defendants – Guyett, Jorden, and Rossi – were required to “[r]eview
21 with management and the independent auditors”:

- 22 (a) “the results of the independent auditors’ reviews of the quarterly
23 unaudited financial statements and annual audited financial
24 statements”; and
25 (b) the “Quarterly Reports on Form 10-Q including, but not limited to,
26 management’s discussion and analysis of financial condition and
27 results of operations, and related disclosure topics, prior to the
28 filing of such reports.”

1 ongoing operating performance improvement should enable
2 the company to be profitable on a non-GAAP basis going
3 forward.”

4 88. On November 4, 2011, Maxwell reached its Relevant Period high of \$21.20
5 per share.

6 89. On November 7, 2011, the Individual Defendants caused Maxwell to file its
7 third quarter 2011 Form 10-Q with the SEC. Defendants Schramm and Royal signed the
8 Form 10-Q, which referred to Maxwell’s Form 10-K for the year ended December 31,
9 2010, as well as to the Company’s accounting policies. The Form 10-Q was also
10 reviewed and approved by the Audit Committee Defendants. Like the previous Form
11 10-Qs, the November 7, 2011 Form 10-Q contained a certification by Schramm and
12 Royal as required by SOX.

13 90. Before approving the issuance of Maxwell’s quarterly financial reports, the
14 Audit Committee Defendants – Guyett, Jorden, and Rossi – were required to “[r]eview
15 with management and the independent auditors”:

16 (a) “the results of the independent auditors’ reviews of the quarterly
17 unaudited financial statements and annual audited financial
18 statements”; and

19 (b) the “Quarterly Reports on Form 10-Q including, but not limited to,
20 management’s discussion and analysis of financial condition and
21 results of operations, and related disclosure topics, prior to the
22 filing of such reports.”

23 91. In contravention of these duties, Guyett, Jorden, and Rossi either failed to
24 conduct the requisite reviews or conducted only a cursory, perfunctory review. As a
25 result, Guyett, Jorden, and Rossi acted in bad faith and abdicated their fiduciary duties
26 in approving the issuance of the false and misleading financial statements in Maxwell’s
27 November 7, 2011 Form 10-Q.

28 92. On February 16, 2012, the Individual Defendants caused Maxwell to issue
a press release announcing its fourth quarter and fiscal year ended 2011 financial

1 results. Maxwell reported net income of \$1.6 million, or \$0.06 diluted EPS, and
2 revenue of \$42.5 million for the fourth quarter ended December 31, 2011. Further, the
3 Company reported net income of \$849,000, or \$0.03 diluted EPS, and revenue of
4 \$157.3 million for the fiscal year ended December 31, 2011. The release stated in part:

5 “Emerging ultracapacitor applications in backup power and
6 stop-start idle elimination systems in micro hybrid autos
7 augmented ongoing contributions from established customer
8 bases in wind energy and hybrid bus drive systems to drive
9 steadily increasing sales growth in 2011,” said David
10 Schramm, Maxwell’s president and chief executive officer.
11 “We have also introduced new products for the
12 uninterruptible power supply (UPS) and engine starting
13 markets that we expect to drive additional growth in the
14 coming year.”

15 * * *

16 “Considering the impact of the Chinese New Year holidays
17 and historic seasonality, we expect revenue to be lower by as
18 much as five percent sequentially in the current first quarter
19 compared with that reported in the fourth quarter,”
20 Schramm said. “However, ***as previously stated, for the
21 full year, we expect sales to grow at a rate similar
22 to that experienced in 2011, and steadily improving
23 operating performance should enable the Company
24 to continue to be profitable on a non-GAAP basis.***”

25 93. On February 16, 2012, the Individual Defendants caused Maxwell to file its
26 2011 Form 10-K with the SEC. The Form 10-K reported net income of \$849,000 or
27 \$0.03 diluted EPS, and revenue of \$157.3 million for fiscal year 2011. The Form 10-K
28 also stated:

Assumptions and Approach Used. Product revenue is
recognized when all of the following criteria are met: (1)
persuasive evidence of an arrangement exists (upon contract
signing or receipt of an authorized purchase order from a
customer); (2) title passes to the customer at either shipment
from our facilities or receipt at the customer facility,
depending on shipping terms; (3) price is deemed fixed or
determinable and free of contingencies or significant
uncertainties; and (4) collectability is reasonably assured.
Customer purchase orders and/or contracts are generally
used to determine the existence of an arrangement. Shipping
documents are used to verify product delivery. We assess
whether a price is fixed or determinable based upon the
payment terms associated with the transaction. If a volume
discount is offered, revenue is recognized at the lowest price

1 offered to the customer. We assess the collectability of
2 accounts receivable based primarily upon creditworthiness
3 of the customer as determined by credit checks and analysis,
4 as well as the customer's payment history.

5 94. Before approving the issuance of Maxwell's annual financial reports, the
6 Audit Committee Defendants – Guyett, Jorden, and Rossi – were required to “[r]eview
7 with management and the independent auditors”:

8 (a) “the results of the independent auditors’ reviews of the quarterly
9 unaudited financial statements and annual audited financial
10 statements”;
11 and

12 (b) the “annual audited financial statements to be included in the
13 Company’s Annual Report on Form 10-K . . . including, but not
14 limited to, management’s discussion and analysis of financial
15 condition and results of operations, and related disclosure topics,
16 prior to the filing of such reports.”

17 95. In contravention of these duties, Guyett, Jorden, and Rossi either failed to
18 conduct the requisite reviews or conducted only a cursory, perfunctory review. As a
19 result, Guyett, Jorden, and Rossi acted in bad faith and abdicated their fiduciary duties
20 in approving the issuance of the false and misleading financial statements in Maxwell’s
21 Form 10-K for 2011.

22 96. All Director Defendants and Royal signed Maxwell’s 2011 Form 10-K.

23 97. On March 30, 2012, the Individual Defendants caused Maxwell to file with
24 the SEC the Proxy Statement Form 14A, which “incorporate[d] by reference the
25 consolidated financial statements and the notes related thereto contained in the
26 Company’s 2011 Annual Report on Form 10-K.”

27 98. The Proxy Statement also contained a “Report of the Audit Committee,” in
28 which the Guyett, Jordan, and Rossi expressly approved the financial statements for
29 fiscal year 2011:

1 [T]he Audit Committee has met and held discussions with
2 management and the independent auditors. Management
3 represented to the Audit
4 Committee that the Company's consolidated financial
5 statements were prepared in accordance with accounting
6 principles generally accepted in the United States of
7 America, and the Audit Committee has reviewed and
8 discussed the consolidated financial statements and the
9 effectiveness of internal control over financial reporting with
10 management and the independent auditors. The Audit
11 Committee discussed with the independent auditors matters
12 required to be discussed by Statement on Auditing Standards
13 No. 61 (Codification of Statements on Auditing Standards),
14 as amended (AICPA, Professional Standards,
15 Vol. 1. AU Section 380), as adopted by the PCAOB in Rule
16 3200T.

17 The Company's independent auditors also provided to the
18 Audit Committee the written disclosures and the letters
19 required by Independence Standards
20 Board Standard No. 1 (Independence Discussions with Audit
21 Committees) and PCAOB Rule 3526 (Communication with
22 Audit Committees Concerning Independence), and the Audit
23 Committee discussed with the independent auditors the
24 firm's independence from the Company and its management.

25 Based on the Audit Committee's discussions with
26 management and the independent auditors as well as the
27 Audit Committee's review of the representations of
28 management and the report of the independent auditors to
the Audit Committee, the Audit Committee recommended
that the Board include the audited consolidated financial
statements for the year ended December 31, 2011 in the
Company's Annual Report on Form 10-K, filed with the SEC
on February 16, 2012.

99. On April 26, 2012, the Individual Defendants caused Maxwell to issue a
press release announcing disappointing first quarter 2012 financial results. Maxwell
reported net income of \$504,000, or \$0.02 diluted EPS, and revenue of \$39.2 million
for the first quarter ended March 31, 2012. The release stated in part:

"Ultracapacitor revenue was down sequentially from Q4, due
in part to seasonal factors, including the Chinese New Year
observance," said David Schramm, Maxwell's president and
chief executive officer. "Continued demand for
ultracapacitor-based energy storage systems to power hybrid
electric transit buses helped to offset softness in other
applications. That, along with ongoing order flow for backup
power applications and stop-start idle elimination systems in
micro hybrid autos enabled us to sustain year-over-year
growth."

1
2 “We expect revenue to increase by 4 to 7 percent sequentially
3 in the current second quarter compared with that reported in
4 the first quarter,” Schramm said. “On the basis of reduced
5 forecasts from customers in Europe and elsewhere, we now
6 anticipate top line growth for the full year to be in the range
7 of 15 to 20 percent, and continuing solid operating
8 performance should enable the company to be profitable on
9 a non-GAAP basis.”

10
11 100. Following this disclosure of disappointing results, Maxwell’s stock
12 declined from \$15.80 per share to as low as \$8.81 per share before closing at \$9.60 per
13 share, on volume of 7.29 million shares. However, Maxwell’s stock continued to trade at
14 artificially-inflated levels as the Individual Defendants concealed the Company’s
15 improper revenue recognition and deficient internal controls.

16
17 101. On April 26, 2012, the Individual Defendants caused Maxwell to file its
18 first quarter 2012 Form 10-Q with the SEC. Defendants Schramm and Royal signed the
19 Form 10-Q, which referred to Maxwell’s Form 10-K for the year ended December 31,
20 2011, as well as to the Company’s accounting policies. The Form 10-Q was also reviewed
21 and approved by the Audit Committee Defendants. Like the previous Forms 10-Q, the
22 April 26, 2012 Form 10-Q contained a certification by Schramm and Royal under SOX.

23
24 102. Before approving the issuance of Maxwell’s quarterly financial reports, the
25 Audit Committee Defendants – Guyett, Jorden, and Rossi – were required to “[r]eview
26 with management and the independent auditors”:

- 27
28
- (a) “the results of the independent auditors’ reviews of the quarterly unaudited financial statements and annual audited financial statements”; and
 - (b) the “Quarterly Reports on Form 10-Q including, but not limited to, management’s discussion and analysis of financial condition and results of operations, and related disclosure topics, prior to the filing of such reports.”

1 103. But Guyett, Jorden, and Rossi either failed to conduct the requisite
2 reviews or conducted only a cursory, perfunctory review. As a result, Guyett, Jorden,
3 and Rossi acted in bad faith and abdicated their fiduciary duties when they approved the
4 issuance of the false and misleading financial statements in Maxwell's April 26, 2012
5 Form 10-Q.

6 104. On August 2, 2012, the Individual Defendants caused Maxwell to issue a
7 press release announcing its second quarter 2012 financial results. Maxwell reported
8 net income of \$2.7 million, or \$0.09 diluted EPS, and revenue of \$40.9 million for the
9 second quarter ended June 30, 2012. The release stated in part:

10 “Slowing demand in Europe has impacted ultracapacitor
11 revenue growth through the first half of the year, and the
12 outlook there remains uncertain,” said David Schramm,
13 Maxwell's president and chief executive officer. “On the plus
14 side, careful expense controls, strong demand for
15 ultracapacitor products for hybrid electric transit buses and
16 wind turbine blade pitch systems in China and steady
17 performance by our high voltage and microelectronics
18 groups have enabled us to continue growing and improving
19 bottom line performance in a difficult economic
20 environment.”

16 * * *

17 “Based on current order flow and customer forecasts in our
18 core ultracapacitor market segments, we expect sequential
19 top line growth of seven to 10 percent in the third quarter,”
20 Schramm said. “That should keep us on track to achieve
21 growth in the range of 15 to as much as 20 percent for the
22 full year and support ongoing improvement in operating
23 performance.”

21 105. On August 2, 2012, the Individual Defendants caused Maxwell to file its
22 second quarter 2012 Form 10-Q with the SEC. Defendants Schramm and Royal signed
23 the Form 10-Q, which referred to Maxwell's Form 10-K for the year ended December 31,
24 2011, as well as to the Company's accounting policies. The Form 10-Q was also reviewed
25 and approved by the Audit Committee Defendants. Like the previous Forms 10-Q, the
26 August 2, 2012 Form 10-Q contained a certification by Schramm and Royal under SOX.

27

28

1 106. Before approving the issuance of Maxwell’s quarterly financial reports, the
2 Audit Committee Defendants – Guyett, Jorden, and Rossi – were required to “[r]eview
3 with management and the independent auditors”:

4 (a) “the results of the independent auditors’ reviews of the quarterly
5 unaudited financial statements and annual audited financial
6 statements”; and

7 (b) the “Quarterly Reports on Form 10-Q including, but not limited to,
8 management’s discussion and analysis of financial condition and
9 results of operations, and related disclosure topics, prior to the
10 filing of such reports.”

11 107. But Guyett, Jorden, and Rossi either failed to conduct the requisite
12 reviews or conducted only a cursory, perfunctory review. As a result, Guyett, Jorden,
13 and Rossi acted in bad faith and abdicated their fiduciary duties when they approved the
14 issuance of the false and misleading financial statements in Maxwell’s August 2, 2012
15 Form 10-Q.

16 108. On October 25, 2012, the Individual Defendants caused Maxwell to issue a
17 press release announcing its third quarter 2012 financial results. Maxwell reported net
18 income of \$5.4 million, or \$0.19 diluted EPS, and revenue of \$43.9 million for the
19 second quarter ended June 30, 2012.

20 109. On October 30, 2012, the Individual Defendants caused Maxwell to file its
21 third quarter 2012 Form 10-Q with the SEC. Defendants Schramm and Royal signed the
22 Form 10-Q, which referred to Maxwell’s Form 10-K for the year ended December 31,
23 2011, as well as to the Company’s accounting policies. The Form 10-Q further stated in
24 part:

25 We are committed to maintaining disclosure controls and
26 procedures designed to ensure that information required to
27 be disclosed in our periodic reports filed under the Securities
28 and Exchange Act of 1934 (the “Exchange Act”) is recorded,
processed, summarized and reported within the time periods
specified in the SEC’s rules and forms, and that such

1 information is accumulated and communicated to our
2 management, including our Principal Executive Officer and
Principal Financial Officer, as appropriate, to allow for
timely decisions regarding required disclosure.

3 Under the supervision and with the participation of our
4 management, including our Principal Executive Officer and
Principal Financial Officer, we conducted an evaluation of
5 the effectiveness of the design and operation of our
disclosure controls and procedures as of September 30,
6 2012, as such term is defined under Rule 13a-15(e)
promulgated under the Exchange Act. Based on this
7 evaluation, our Principal Executive Officer and Principal
Financial Officer concluded that our disclosure controls and
8 procedures were effective as of the end of the period covered
by this Quarterly Report on Form 10-Q.

9 110. Like the previous Forms 10-Q, the October 30, 2012 Form 10-Q contained
10 a certification by Schramm and Royal under SOX.

11 111. Before approving the issuance of Maxwell's quarterly financial reports, the
12 Audit Committee Defendants – Guyett, Jorden, and Rossi – were required to “[r]eview
13 with management and the independent auditors”:

14 (a) “the results of the independent auditors’ reviews of the quarterly
15 unaudited financial statements and annual audited financial
16 statements”; and

17 (b) the “Quarterly Reports on Form 10-Q including, but not limited to,
18 management’s discussion and analysis of financial condition and
19 results of operations, and related disclosure topics, prior to the
20 filing of such reports.”

21 112. But Guyett, Jorden, and Rossi either failed to conduct the requisite
22 reviews or conducted only a cursory, perfunctory review. As a result, Guyett, Jorden,
23 and Rossi acted in bad faith and abdicated their fiduciary duties when they approved the
24 issuance of the false and misleading financial statements in Maxwell’s October 30, 2012
25 Form 10-Q.

26 113. Each of the foregoing statements regarding Maxwell’s financial condition
27 and business prospects were false and misleading when made, as discussed below.

28

1 **II. The Emergence of the Truth**

2 114. On March 7, 2013, after the market closed, the Individual Defendants
3 caused Maxwell to issue a press release disclosing that the Company would be restating
4 previously-issued financial statements for 2011 and most of 2012 due to errors related to
5 the timing of recognition of revenue from sales to certain distributors. Maxwell further
6 disclosed that the financial statements should no longer be relied upon. The release
7 stated in part:

8 ***Maxwell Technologies, Inc. announced today*** that on
9 March 1, 2013, the audit committee of its board of directors
10 concluded that ***the previously issued financial***
11 ***statements contained in its annual report on Form***
12 ***10-K for the year ended December 31, 2011, and all***
13 ***unaudited quarterly reports on Form 10-Q in 2011***
14 ***and 2012 (collectively, the “Prior Periods”), as well***
15 ***[as] its selected financial data for the related***
16 ***periods, should no longer be relied upon because of***
17 ***errors in those financial statements. The errors***
18 ***relate to the timing of recognition of revenue from***
19 ***sales to certain distributors.***

20 In addition to the financial statements for the Prior Periods,
21 related press releases furnished on current reports on Form
22 8-K, reports and stockholder communications describing its
23 financial statements for the Prior Periods and the report of
24 its independent registered public accounting firm,
25 McGladrey LLP (formerly McGladrey & Pullen, LLP), related
26 to the year ended December 31, 2011, should no longer be
27 relied upon.

28 The conclusion that the financial statements for the Prior
Periods cannot be relied upon is the result of an investigation
by Maxwell’s audit committee, with the assistance of
independent outside counsel and forensic accountants. The
investigation commenced following receipt of information
concerning potential recognition of revenue prior to the
satisfaction of certain of the criteria required to be met to
recognize revenue.

The investigation discovered arrangements with
certain distributors regarding the payment terms
for sales to such distributors with respect to certain
transactions. These arrangements had not been
communicated to Maxwell’s finance and accounting
department and, therefore, had not been considered when
recording revenue on shipments to these distributors. Based
on the terms of the agreements with these distributors as
they were known to the finance and accounting department,
it had been the policy to account for revenue related to

1 shipments to these distributors as title passed to the
2 distributor at either shipment from Maxwell's facilities or
3 receipt at the distributor's facility, assuming all other
4 revenue recognition criteria had been achieved. **As a result
5 of the arrangements discovered during the
6 investigation, Maxwell does not believe that a fixed
7 or determinable sales price existed at the time of
8 shipment to these distributors, nor was collection
9 reasonably assured, at least with respect to certain
10 transactions. Therefore, the revenue from such
11 sales should not have been recognized at the time of
12 shipment to these distributors.**

7 Maxwell believes that the impact to the Prior Periods of
8 correcting the errors in revenue recognition related to sales
9 transactions to these distributors will be to decrease
10 previously reported revenues and profits for 2011 and the
11 first three quarters of 2012, and to increase revenue and
12 profits by the same amounts in subsequent periods.

11 Maxwell believes that **the restatement of revenue
12 related to these distributors will decrease
13 previously reported revenues for fiscal year 2011
14 by approximately \$6.5 million and decrease
15 revenues in the first three quarters of 2012 by
16 approximately \$5.5 million in the aggregate.**

14 Maxwell also believes that the restatement of revenue related
15 to these distributors will result in shipments to these
16 distributors for which title has passed to the distributor, but
17 for which the revenue recognition criteria has not been fully
18 achieved, of approximately \$12.0 million as of September 30,
19 2012. Of the shipments to these distributors that had not
20 been collected as of September 30, 2012, and therefore not
21 recognized as revenue, Maxwell collected \$4.6 million in the
22 fourth quarter of 2012 and \$3.0 million to date in the first
23 quarter of 2013, leaving \$4.4 million outstanding that will be
24 recognized as revenue as Maxwell receives payments in the
25 future.

21 Maxwell is in the process of evaluating deficiencies in its
22 internal controls over financial reporting and [has]
23 preliminarily concluded that it has material weaknesses in its
24 internal controls over financial reporting related to the
25 identification and evaluation of revenue transactions which
26 deviate from contractually established payment terms and
27 therefore has preliminarily concluded that **its internal
28 controls over financial reporting and disclosure
are not effective. Maxwell intends to design and
implement controls to remediate these deficiencies.**

26 **As a result of the investigation, certain employees
27 were terminated and Maxwell's Sr. Vice President
28 of Sales and Marketing resigned.**

The Company, including the audit committee, has discussed the foregoing matters with Maxwell's independent registered public accounting firm, McGladrey LLP. The audit committee has authorized and directed the officers of the Company to take the appropriate and necessary actions to restate its financial statements for the Prior Periods. Maxwell intends to file restated financial statements for the Prior Periods as soon as reasonable[y] practicable.

115. Maxwell further disclosed in its March 7, 2013 Form 8-K that Andrews had resigned, effective March 1, 2013, as a direct result of the ongoing investigation being performed by the audit committee and Maxwell's Board.

116. On this news, Maxwell's stock price dropped \$1.01 per share on March 8, 2013 to close at \$8.10 per share, a one-day decline of 11% on volume of 1.7 million shares.

117. On April 2, 2013, Maxwell announced that it appointed BDO USA, LLP to replace Defendant McGladrey as Maxwell's new independent auditor. On that day, Maxwell's stock price dropped to \$4.98 per share.

118. On August 1, 2013, Maxwell filed restated financial results with the SEC which were included in the Company's belated Form 10-K for fiscal year 2012. As noted above, the restatement totaled nearly \$20 million:

| | Nine Months Ended September 30, 2012 (in thousands, except per share data) | | | Fiscal Year Ended December 31, 2011 (in thousands, except per share data) | | |
|--|--|-------------------------|------------|---|-------------------------|------------|
| | As previously reported | Restatement Adjustments | Restated | As previously reported | Restatement Adjustments | Restated |
| Revenue | \$ 123,993 | \$ (9,238) | \$ 114,755 | \$ 157,311 | \$ (10,135) | \$ 147,176 |
| Cost of revenue | 72,503 | (5,571) | 66,932 | 95,254 | (5,148) | 90,106 |
| Gross profit | 51,490 | (3,667) | 47,823 | 62,057 | (4,987) | 57,070 |
| Income (loss) from operations | 10,648 | (4,312) | 6,336 | 1,783 | (2,287) | (504) |
| Net income (loss) | 8,565 | (4,258) | 4,307 | 849 | (2,287) | (1,438) |
| Diluted net income (loss) per share | \$ 0.30 | \$ (0.15) | \$ (0.15) | \$ 0.03 | \$ (0.08) | \$ (0.05) |

1 119. Concerning the restatement, the Company explained:

2 **Note 2—Restatement of Previously Issued Financial**
3 **Statements and Financial Information**

4 **Background on the Restatement**

5 *Audit Committee's Investigation*

6 In January 2013, following receipt of information
7 concerning potential revenue recognition issues, the Audit
8 Committee of the Board of Directors engaged independent
9 legal counsel and forensic accountants to conduct an
10 investigation concerning the potential issues and to work
11 with management to determine the potential impact on
12 accounting for revenue. In February 2013, as a result of the
13 findings of the Audit Committee's investigation to date, the
14 Company determined that certain of its employees had
15 engaged in conduct which resulted in revenue being
16 recorded in periods prior to the criteria for revenue
17 recognition under U.S. generally accepted accounting
18 principles being satisfied.

19 The investigation revealed arrangements with three of
20 the Company's distributors regarding extended payment
21 terms, and with one of the Company's distributors regarding
22 return rights and profit margin protection, for sales to such
23 distributors with respect to certain transactions. In addition,
24 arrangements were revealed with one non-distributor
25 customer to honor transfer of title at a date later than the
26 customer's purchase orders indicated. Based on the results
27 of its investigation, the Audit Committee determined that
28 these arrangements had not been communicated to the
company's finance and accounting department, or to the
Company's CEO, and therefore, had not been considered
when revenue was originally recorded. Based on the terms
of the agreements with these customers, as they were known
to the Company's finance and accounting department, it had
been the Company's policy to record revenue related to
shipments as title passed at either shipment from the
Company facilities or receipt at the Company's facility,
assuming all other revenue recognition criteria had been
achieved. In addition to the arrangements noted above, the
investigation uncovered an error on an individual
transaction where a customer was given extended payment
terms but those terms were not considered when revenue
was originally recognized.

As a result of the arrangement discovered during the
investigation, the Company does not believe that a fixed or
determinable sales price existed at the time of shipment, nor
was collection reasonably assured, at least with respect to
certain transactions. In addition, revenue related to certain
shipments to the one non-distributor customer was recorded

1 before the actual transfer of title and the satisfaction of the
2 Company's obligations to deliver the products. Therefore,
3 revenue from these sales should not have been recognized at
4 the time of shipment.

5 Based on the arrangements with customers revealed
6 in the investigation that were not considered when revenue
7 was originally recognized, the Company determined the
8 following:

- 9 • Beginning in the period in which the
10 investigation revealed arrangements regarding
11 extended payment terms for certain sales to
12 three distributors, the Company determined it
13 is appropriate to defer revenue recognition on
14 all sales to these distributors from the period of
15 shipment to the period of cash receipt. For
16 these distributors, revenue recognition in the
17 period of cash receipt was determined to be
18 appropriate beginning in the fourth quarter of
19 2011.
- 20 • Beginning in the period in which the
21 investigation revealed return rights and profit
22 margins protection for one distributor, the
23 Company determined it appropriate to defer
24 revenue recognition until the Company
25 determines that the distributor is not entitled
26 to any further returns or credits. For this
27 distributor, the deferral of revenue until the
28 Company determines that the distributor is not
entitled to any further returns or credits was
determined to be appropriate beginning in the
fourth quarter of 2011. At such time as this
determination is made, which is currently
anticipated to occur in the second half of the
fiscal year 2013, previous sales for which
revenue has been deferred, net of any credits or
returns that may be made by the distributor,
will be recognized as revenue.
- For the arrangement with the non-distributor
customer to honor transfer of title at a date
later than the customer's purchase order
indicated, the Company determined its
appropriate to defer revenue recognition to the
period in which the Company agreed to honor
transfer of title.

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- 2
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- For the individual transaction where a customer was given extended payment terms which were not considered when revenue was originally recognized in the first quarter of 2011, revenue recognition when the cash was received, which was in the second quarter of 2011, was determined to be appropriate.

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Management's Subsequent Internal Review

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Once the audit committee investigation was complete, the Company conducted a review beginning with the first quarter of 2009 through the first quarter of 2013 to ensure that all sales arrangements had been detected and accounted for appropriately. During this review, the Company noted that there were a number of quarter and revenue cut-off errors wherein revenue was recorded prior to the transfer of title to the customer and the satisfaction of the Company's obligation to deliver the products. The Company has corrected these errors occurring in the first quarter of 2011 through the third quarter of 2012 by moving the revenue recognition for these items to the period in which delivery actually occurred.

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Results of the Audit Committee's investigation and Management's Internal Review

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Based on the findings of the investigation, as previously reported in the Company's current report on Form 8-K dated March 7, 2013, the Audit Committee, in consultation with management and the Board of Directors, concluded that the Company's previously issued financial statements contained in its annual report on Form 10-K for the year ended December 31, 2011, and the quarterly reports on Form 10-Q for the quarters ended March 31, 2011, June 30, 2011, September 30, 2011, March 31, 2012, June 30, 2012 and September 30, 2012 should no longer be relied upon. Accordingly, the accompanying consolidated financial statements for the first three quarters of the fiscal year ended December 31, 2012, for the fiscal year ended December 31, 2011, and for each of the interim periods within the fiscal year ended December 31, 2011, have been restated in this Annual Report on Form 10-K.

26

27

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As a result of the Audit Committee's investigation, certain employees were terminated and the Company's Sr. Vice President of Sales and Marketing resigned as reported

1 in the Company's current report on Form 8-K dated March 7,
2013.

2
3 In connection with the errors identified during the
4 investigation resulting in the restatement of previously
5 reported financial statements, the Company identified
6 control deficiencies in its internal control over financial
7 reporting that constitute material weaknesses. For a
8 discussion of our disclosure controls and procedures and the
9 material weaknesses identified, see Part II, Item 9A, Controls
10 and Procedures, of this Annual Report on Form 10-K.

11
12 The Company previously filed annual report on Form
13 10-K for the fiscal year ended December 31, 2011, and its
14 quarterly reports on Form 10-Q for the periods affected by
15 the restatements, have not been amended. Accordingly,
16 investors should no longer rely upon the Company's
17 previously released financial statements for any quarterly or
18 annual periods after and including March 31, 2011, and any
19 earnings releases or other communications relating to these
20 periods. See Note 15, *Unaudited Quarterly Financial*
21 *Information*, of the Notes to the Consolidated Financial
22 Statements, in this Annual Report for the impact of these
23 adjustments for the full fiscal year ended December 31, 2011,
24 and the first three quarters of the fiscal year ended December
25 31, 2012 and each of the quarterly periods in the fiscal year
26 ended December 31, 2011, respectively.

17 **Restatement Adjustments**

18 *Restatement Adjustments Related to Sales Arrangements*

19 Several adjustments were made to the Company's
20 previously filed consolidated financial statements as a result
21 of the restatement in order to reflect revenue recognition in
22 the appropriate periods as discussed above. Accordingly, for
23 the subject sales transactions, revenue and accounts
24 receivable balances were reduced by an equivalent amount in
25 the period that the sale was originally recorded as revenue,
26 and revenue was increased in the subsequent period in which
27 the criteria for revenue recognition were met. Further, for
28 the subject sales transactions, cost of revenue was reduced,
and inventory was increased, in the period that the sale was
originally recorded as revenue, and cost of revenue was
increased, and inventory was reduced, in the period the sale
was ultimately recorded as revenue. However, for sales to
one distributor in which revenue is being deferred until the
Company determines that the distributor is not entitled to

1 any further returns or credits, as discussed above, the
2 increase to revenue, and the related reduction to inventory
3 and increase to cost of revenue, will be recorded in a future
4 period when this determination is made.

5 The adjustments also reflect the impacts of adjusting
6 the Company's returns reserves for certain stock rotation
7 rights of the distributors, and adjusting the Company's
8 reserves for allowances for doubtful accounts, as well as
9 commissions expense, although these charges were not
10 material.

11 In addition to the adjustments to revenue, accounts
12 receivable, inventory and cost of revenue, inventory reserves
13 balances and cost of revenue were adjusted in related to the
14 adjustments to inventory discussed above, in order to reflect
15 inventory ultimately recorded on our balance sheets at its
16 lower of cost or market value.

17 *Other Restatement Adjustments*

18 Since the Company's determination to restate its
19 previously issued financial statements constituted an event
20 of default under the terms of its credit facility, the bank had
21 the right to require immediate payment of the outstanding
22 borrowings. As a result, restatement adjustments were
23 recorded to reclassify amounts outstanding under the credit
24 facility from long-term debt to current liabilities as of each
25 respective balance sheet date. In addition, an insignificant
26 amount of debt issuance costs were reclassified from a long-
27 term asset to a short-term asset, consistent with the
28 classification of the related debt. In June 2013, the Company
entered into a forbearance agreement with the bank wherein
the bank agreed to forbear from further exercise of its rights
and remedies to call our outstanding debt under the credit
facility in connection with the events of default for a period
terminating on the earlier of September 30, 2013 or the
occurrence of any additional events of default.

Further, a restatement adjustment was made to
reclassify a legal settlement with a customer from selling,
general and administrative expense to contra-revenue in the
second quarter of 2011 in the amount of \$2.6 million.
Certain other immaterial adjustments were made in
connection with the restatement, which resulted in a
\$153,000 decrease to the net loss recorded for the year
ended December 31, 2011, and a \$170,000 decrease to net
income/loss for the nine-months ended September 30, 2012.

1 The restatement adjustments did not impact the
2 Company's previously reported tax provision or benefit in
3 any of the affected periods, other than a \$54,000 decrease in
4 the income tax provision for the quarter ended September
5 30, 2012, as all of the restatement adjustments were related
6 to our U.S. operations, for which we have significant net
7 operating loss carry forward and have not recorded an
8 income tax expense or benefit in any period to date.
9 However, the restatement adjustments did impact the
10 composition of our deferred tax assets and liabilities as of
11 December 31, 2011 as presented in Note 10, Income Taxes, of
12 the Notes to the Consolidated Financial Statements included
13 in this Annual Report.

14 **Effects of Restatement**

15 For the fiscal year ended December 31, 2011, the
16 restatement of adjustments decreased revenue by \$10.1
17 million and decreased previously reported net income by
18 \$2.3 million or \$-0.08 per diluted share, to a net loss of \$1.4
19 million. As of June 30, 2013, we had collected the related
20 accounts receivable on all sales transactions that were
21 subject to restatement for the year ended December 31, 2011,
22 with the exception of an insignificant amount that was
23 subsequently credited to certain customers.

24 120. The Company also admitted that it had material weaknesses in its internal
25 financial controls that were a cause of the previously misrepresented earnings:

26 **Management's Annual Report on Internal Control 27 over Financial Reporting**

28 Our management is responsible for establishing and
maintaining adequate control over financial reporting, as
such term is defined in Exchange Act Rule 13a-15(f). Under
the supervision and the participation of our management,
including our principal executive officer and principal
financial officer, we conducted an evaluation of the
effectiveness of our internal control over financial reporting
based on the framework in *Internal Control—Integrated
Framework* issued by the Committee of Sponsoring
Organizations of the Treadway Commission.

* * *

BDO USA LLP, the independent registered public
accounting firm that audited the consolidated financial
statements of Maxwell in this Annual Report on Form 10-K,
has issued an adverse opinion on the effectiveness of our

1 internal controls over financial reporting as of December 31,
2 2012 which is included in this Item under the heading
3 "Report of Independent Registered Public Accounting Firm."

4 *Material Weaknesses*

5 A material weakness is a deficiency, or a combination
6 of deficiencies, in internal control over financial reporting,
7 such that there is a reasonable possibility that a material
8 misstatement of our annual or interim financial statements
9 will not be prevented or detected on a timely basis.

10 For certain sales transactions, sales and other
11 personnel have entered into side arrangements with
12 customers for return rights, extended payment terms, profit
13 margin protection and transfer of title terms that were not
14 communicated to the finance and accounting department, or
15 to our CEO. As such, we did not maintain effective controls
16 over our revenues and accounts receivable balances as the
17 sales price was not fixed or determinable nor was
18 collectability reasonably assured at the time revenue was
19 originally recognized. As a result, we recognized revenue
20 prematurely. These errors resulted in the restatement of our
21 consolidated financial statement for each of the previously
22 reported interim and annual periods with the fiscal years
23 ended December 31, 2012 and 2011. These control
24 deficiencies could result in misstatements of revenues and
25 accounts receivable balances and related disclosures that
26 would result in material misstatement of the consolidated
27 financial statements that would not be prevented or
28 detected. Accordingly, our management has determined that
each of these control deficiencies constitutes a material
weakness. The specific material weaknesses are:

- we did not maintain adequately designed controls to ensure accurate recognition of revenue in accordance with GAAP. Specifically, controls were not effective to ensure that deviations from contractually established sales terms were authorized, communicated, identified and evaluated for their potential effect on revenue recognition. Further we did not adequately train and supervise sales personnel to ensure that such personnel were appropriately conscious of the requirement to communicate deviations from contractually established sales terms to finance and accounting personnel in order for revenue recognition in our financial statement to be accurately recorded; and
- We did not perform a robust fraud risk assessment taking into consideration the various ways that fraud may be perpetrated to misappropriate assets or facilitate fraudulent

1 financial reporting. We failed to identify
2 controls specifically designed to prevent and
3 detect fraud risks pertaining to revenue
4 recognition.

5 121. Finally, in its Form 10-K, the Company offered only vague promises as to
6 how it would remedy these material weaknesses in its internal financial controls.

7 122. The true facts, which were known by the Individual Defendants but
8 concealed from the investing public during the Relevant Period, included:

9 (a) Maxwell had overstated its revenues and earnings in 2011 and 2012
10 in violation of GAAP;

11 (b) Maxwell had reported revenues prior to the time the sales price was
12 fixed and/or collection was reasonably assured;

13 (c) Maxwell's internal accounting controls were deficient and
14 permitted the premature recognition of revenue, leading to materially misstated
15 financial results;

16 (d) Maxwell's internal controls were not effective to prevent deviations
17 from contractually-established sales terms; and

18 (e) the Company failed to perform a robust fraud risk assessment
19 pertaining to revenue recognition.

20 123. As a result of these false and misleading statements, Maxwell common
21 stock traded at artificially-inflated prices during the Relevant Period. However, after the
22 foregoing revelations of the true, but undisclosed, facts seeped into the market, the
23 Company's common stock experienced exorbitant selling pressure sending its price
24 down nearly 62% from its Relevant Period high.

25 **III. 2011 Compensation of Schramm, Royal, and Andrews**

26 124. While Maxwell's stock was trading at artificially-inflated prices, the
27 Individual Defendants awarded lavish compensation in 2011 to the Officer Defendants
28 (Schramm, Royal, and Andrews). Specifically, Defendants Howsmon, Lavigne, Rossi,

1 and Guyett, as members of Maxwell's Compensation Committee, approved and awarded
2 the unjust compensation as described below.

3 125. Pursuant to the Company's compensation program and policy, the
4 compensation paid to the Company's named executive officers "consists of base salary,
5 annual incentive bonuses, equity incentive awards, certain contractual severance and
6 change in control benefits, and certain perquisites."

7 126. For 2011, Defendants Schramm, Royal, and Andrews received the
8 following compensation as their base salaries:

| 9 | Name | Principal Position | 2011 Base Salary |
|----|-------------|--|-------------------------|
| 10 | Schramm | President, CEO, and Director | \$495,000 |
| 11 | Royal | Senior Vice President and CFO | \$311,100 |
| 12 | Andrews | Senior Vice President, Sales and Marketing | \$252,000 |

13
14 127. Defendant Schramm's base salary was, according to a compensation
15 consultant's study ordered by the Company, above the targeted 50th percentile of the
16 peer group data.

17 128. In addition to base salary, the Company uses annual performance-based
18 cash bonuses to compensate its executive officers. The purpose of those cash bonuses is
19 "to reward [the] executive officers for the achievement of Company performance goals."

20 129. For 2011, the Company had the following policy with regard to the Officer
21 Defendants' performance-based compensation:

22 The 2011 incentive bonus program for our named
23 executive officers consisted of three components related to
24 the achievement of certain operating metrics set forth in the
25 Company's 2011 operating plan as follows: **50% of the**
26 **target bonus amount related to the achievement of**
27 **revenue of \$157.6 million, 25% related to the**
28 **achievement of non-GAAP (explained below) gross**
profit of \$64.9 million, and 25% related to the
achievement of non-GAAP operating income of
\$12.1 million. Non-GAAP gross profit and operating
income are determined by excluding certain non-recurring
and non-cash items from actual financial results prepared
under U.S. Generally Accepted Accounting Principles

1 (“GAAP”). Specifically, these non-GAAP measures exclude
2 stock-based compensation expense, the impact of significant
3 legal settlements and the impact of significant legal expenses
4 related to legal matters that were not present or known when
5 the targets were set. **For 2011, annual cash bonuses
6 were to be paid at 100% of target if operating
7 metrics were achieved, and would be paid on a
8 sliding scale from zero to 150% of target if the
9 actual results achieved were higher or lower than
10 the target.**

11 Per the terms of their employment agreements, Mr.
12 Schramm was eligible to earn a target bonus of 100% of his
13 base salary, and Messrs. Royal and Kreigler were each
14 eligible to earn a target bonus of 50% of their respective base
15 salaries. Although Mr. Andrews does not have an
16 employment agreement with the Company, the
17 Compensation Committee determined his 2011 target bonus
18 eligibility to be 50% of his base salary.

19 130. As a result of the revenues achieved in 2011 (prior to the restatement), the
20 Company awarded substantial compensation to Schramm, Royal, and Andrews.
21 Specifically, the Company used the following methodology in calculating the amount of
22 performance-based compensation to award for 2011:

23 For 2011, the Company achieved revenues of \$157.3 million,
24 and after applying adjustments to arrive at the non-GAAP
25 financial measures described above, the Compensation
26 Committee determined 2011 non-GAAP gross profit of \$62.0
27 million and 2011 non-GAAP operating income of \$9.7
28 million. **Based on the application of the sliding scale
described above, the target bonus amount related
to the revenue metric was paid at 100%, the target
bonus amount related to non-GAAP gross profit
was paid at 70% and no amount was paid related to
the non-GAAP operating income target.**

131. As a result, Schramm, Royal, and Andrews received the following
“performance-based” compensation for 2011:

| Name | 2011 Performance-Based Compensation |
|---------|-------------------------------------|
| Schramm | \$ 336,600 |
| Royal | \$ 105,800 |
| Andrews | \$ 85,700 |

132. This compensation, however, was unjust and unearned because the
Company has now significantly restated its financial results for 2011.

1 133. The restatement reduced the revenues achieved for 2011 from \$157.3
2 million to \$147.2 million. Similarly, the restatement reduced the 2011 non-GAAP gross
3 profit from \$62 million to \$57 million. Utilizing the post-restatement financial results,
4 it is unlikely that the Officer Defendants would have been awarded any performance-
5 based compensation for 2011.

6 134. In addition to the above, Schramm, Royal, and Andrews also received the
7 following unearned cash bonuses and incentive-based stock awards in 2011:

| 8 | Name | Cash Bonus | Award of Restricted Shares |
|----|-------------|-------------------|-----------------------------------|
| 9 | Schramm | \$63,400 | 34,265 |
| 10 | Royal | \$30,000 | 14,233 |
| 11 | Andrews | \$30,000 | 10,121 |

12 **DAMAGES TO MAXWELL**

13 135. Maxwell has been, and will continue to be, severely damaged and injured
14 by the Individual Defendants' misconduct.

15 136. As a direct and proximate result of the Individual Defendants' misconduct,
16 Maxwell has expended and will continue to expend significant sums of money. Such
17 expenditures include, but are not limited to:

18 (a) legal fees associated with the lawsuits filed against the Company for
19 violations of the federal securities laws;

20 (b) loss of reputation and goodwill, and a "liar's discount" that will
21 plague the Company's stock in the future due to the Individual Defendants' false
22 statements and lack of candor to the marketplace;

23 (c) amounts paid to outside lawyers, accountants, and investigators in
24 connection with Maxwell's internal investigation;

25 (d) loss of revenues and profits due to the ensuing restatements;

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1 (e) costs relating to remediating the event of default of the Company's
2 credit facility, which occurred as a result of the Individual Defendants'
3 wrongdoing; and

4 (f) costs and fees associated with fixing the Company's materially
5 deficient internal controls.

6 **DERIVATIVE ALLEGATIONS**

7 137. Plaintiffs bring this action for the benefit of Maxwell to redress injuries
8 suffered as a result of the Individual Defendants' breaches of fiduciary duties and
9 violations of law, as well as the aiding and abetting thereof.

10 138. Maxwell is named solely as a nominal party in this action. This is not a
11 collusive action to confer jurisdiction on this Court that it would not otherwise have.

12 139. Plaintiffs are and have been Maxwell shareholders and have continuously
13 owned Maxwell common stock during the relevant times. Plaintiffs therefore will
14 adequately and fairly represent the interests of Maxwell in enforcing and prosecuting its
15 rights.

16 **DEMAND FUTILITY ALLEGATIONS**

17 140. Maxwell's Board at the time this action was initiated consisted of the
18 following eight directors: Cortes, Howsmon, Goeschel, Lavigne, Rossi, Guyett, Jorden,
19 and Schramm. Plaintiffs have not made any demand on the Board to institute this
20 action against the Individual Defendants and Defendant McGladrey because, for the
21 reasons set forth below, such demand would be a futile and useless act.

22 141. Where, as here, the board is comprised of an even number of directors, the
23 plaintiffs need only demonstrate that half of the board is interested or lacks
24 independence. Thus, Plaintiffs need only allege demand futility as to four of the eight
25 directors that were on the Board at the time this action was commenced.

1 142. As discussed in more detail below, Plaintiffs have adequately alleged that
2 demand would have been futile because all Director Defendants lack independence and
3 face a substantial likelihood of liability.

4 143. At the very least, Plaintiffs have adequately alleged that demand would
5 have been futile as to the following four directors:

6 (a) Defendant Schramm, the only inside director; and

7 (b) The Audit Committee Defendants (Guyett, Jordan, and Rossi).

8 **I. Demand Is Futile as to Schramm**

9 144. According to the Company's 2012 Proxy statement, Defendant Schramm is
10 not an independent director under NASDAQ listing standards. This decision as to
11 Schramm's lack of independence was made by the Board itself.

12 145. Schramm is also interested in this litigation for purposes of demand
13 futility because he faces a substantial likelihood of liability for his individual
14 misconduct. Schramm is a named defendant in the currently-pending federal class
15 actions, alleging that he violated § 10(b) of the Exchange Act and Rule 10b-5 when he
16 disseminated or approved the false and misleading statements set forth above.

17 146. If Schramm pursued these derivative claims, then that would expose his
18 own misconduct in the class action for violations of the federal securities laws. As such,
19 Schramm is fatally conflicted, and therefore, unable to render a disinterested decision as
20 to whether the Company should pursue these derivative claims. Thus, demand is futile.

21 147. Additionally, Schramm is interested because he issued many of the false
22 and misleading statements. In fact, Schramm signed the Company's SEC filings that
23 contained false and misleading statements, including the Form 10-K dated February 16,
24 2012 and the Forms 10-Q dated May 5, 2011, August 8, 2011, November 7, 2011, April
25 26, 2012, August 2, 2012, and October 30, 2012. Schramm authorized the issuance of
26 Maxwell's March 30, 2012 Proxy Statement, which incorporated the false and
27 misleading financial information from its Form 10-K. Schramm also participated in
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1 conference calls with analysts and investors during the Relevant Period. Schramm
2 therefore faces a substantial likelihood of liability for breaching his fiduciary duties.
3 Consequently, Schramm cannot disinterestedly consider a demand.

4 148. Notably, with regard to each of the above-mentioned Forms 10-Q,
5 Defendant Schramm signed internal control certifications as required by the Sarbanes-
6 Oxley Act of 2002 (“SOX”), affirming that he was responsible for designing “such
7 internal control over financial reporting, or [causing] such internal control over
8 financial reporting to be designed under [his] supervision, to provide reasonable
9 assurance regarding the reliability of financial reporting and the preparation of financial
10 statements for external purposes in accordance with generally accepted accounting
11 principles,” and that he had reported to the board and auditors “[a]ll significant
12 deficiencies and material weaknesses in the design or operation of internal controls over
13 financial reporting which are reasonably likely to adversely affect the registrant’s ability
14 to record, process, summarize and report financial information.”

15 149. As previously noted, however, the above representations were false and
16 misleading (and thereby violated SOX) because the Company has now admitted that it
17 lacked sufficient internal controls during the Relevant Period and that the following
18 significant material weaknesses existed during the Relevant Period:

- 19 • ***[W]e did not maintain adequately designed***
20 ***controls to ensure accurate recognition of***
21 ***revenue in accordance with GAAP.*** Specifically,
22 controls were not effective to ensure that deviations
23 from contractually established sales terms were
24 authorized, communicated, identified and evaluated
25 for their potential effect on revenue recognition.
26 Further, we did not adequately train and supervise
27 sales personnel to ensure that such personnel were
28 appropriately conscious of the requirement to
communicate deviations from contractually
established sales terms to finance and accounting
personnel in order for revenue recognition in our
financial statements to be accurately recorded.
- ***We did not perform a robust fraud risk***
assessment taking into consideration the
various ways that fraud may be perpetrated

1 ***to misappropriate assets or facilitate***
2 ***fraudulent financial reporting.*** We failed to
3 identify controls specifically designed to prevent and
4 detect fraud risks relating to revenue recognition.

5 Accordingly, Schramm faces a substantial likelihood of liability for violating his duties
6 under SOX and, therefore, demand as to him is futile.

7 150. Moreover, Schramm cannot render an independent decision because he is
8 a high-ranking officer of Maxwell. As his principal professional occupation, Schramm
9 has been the President and CEO of the Company since 2007. Schramm received total
10 compensation of \$1,310,800 in 2012, \$1,578,400 in 2011, \$1,160,600 in 2010, and
11 \$1,068,700 in 2009. Demand is futile as to Schramm because instituting any action
12 would jeopardize the lavish compensation Schramm is expected to receive in future
13 years from Maxwell, and could jeopardize his right to the bonus and incentive
14 compensation Schramm received for 2011 at a time when Maxwell stock was inflated by
15 the Individual Defendants' wrongdoing. Thus, demand is futile as to Schramm.

16 151. Finally, according to Maxwell's 2012 Proxy statement, Schramm owned
17 363,164 shares of Maxwell stock, consisting of 1.25% of the total outstanding shares. As
18 a long-term officer and director and a large shareholder of Maxwell, Schramm
19 dominates and controls the other Board members.

20 **II. Demand Is Futile as to Guyett, Jorden, and Rossi**

21 152. The Audit Committee Defendants – Guyett, Jorden, and Rossi – were
22 responsible for reviewing and approving quarterly and annual financial statements,
23 earnings press releases, and Maxwell's internal controls over financial reporting. Each
24 Audit Committee Defendant breached his or her duty of candor and good faith by
25 approving the false financial statements, which, as Maxwell has admitted, should no
26 longer be relied upon and are subject to restatement.

27 153. For example, before approving the issuance of Maxwell's quarterly and
28 annual financial reports, the Audit Committee Defendants were required to "[r]eview
with management and the independent auditors":

- 1 (a) “the results of the independent auditors’ reviews of the quarterly
2 unaudited financial statements and annual audited financial
3 statements”; and
- 4 (b) “the annual audited financial statements to be included in the
5 Company’s Annual Report on Form 10-K and Quarterly Reports on
6 Form 10-Q including, but not limited to, management’s discussion
7 and analysis of financial condition and results of operations, and
8 related disclosure topics, prior to the filing of such reports.”

9 154. In breach of these specific obligations, the Audit Committee Defendants
10 either failed to conduct the requisite reviews or conducted only a cursory, perfunctory
11 review of the financial statements. As a result, the Audit Committee Defendants acted
12 in bad faith and abdicated their fiduciary duties when they approved the issuance of the
13 false and misleading financial statements in Maxwell’s Forms 10-Q and Form 10-K filed
14 in 2011 and 2012, with no meaningful review or independent scrutiny.

15 155. Moreover, the Audit Committee Defendants are responsible for ensuring
16 (a) adequate internal controls; (b) legal and regulatory compliance; and (c)
17 implementation of Maxwell’s accounting and reporting policies and procedures.

18 156. In a complete abdication of these responsibilities, however, the Audit
19 Committee Defendants failed to ensure that Maxwell had adequate internal controls
20 over its financial reporting. This failure is particularly glaring in light of the fact that the
21 Audit Committee Defendants were on notice that Maxwell’s internal controls were
22 lacking based on the Company’s January 2011 entry into the deferred prosecution
23 agreement with the government over the FCPA violations.

24 157. Accordingly, Defendants Guyett, Jorden, and Rossi face a sufficiently
25 substantial likelihood of liability for breaches of their fiduciary duties of loyalty, candor,
26 and good faith. Any demand upon Guyett, Jorden, and Rossi is futile.

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1 158. As members of the Audit Committee, Defendants Guyett, Jorden, and
2 Rossi were also responsible for (a) the integrity of Maxwell's financial statements; (b)
3 the Company's systems of internal controls regarding finance and accounting as
4 established by management; (c) the qualifications and independence of the independent
5 registered public accounting firm; (d) the performance of Maxwell's independent
6 registered public accounting firm; and (e) Maxwell's auditing, accounting, and financial
7 reporting processes generally. Defendants Guyett, Jorden, and Rossi reviewed and
8 approved Maxwell's false and misleading statements that misrepresented its business
9 and financial prospects. Defendants Guyett, Jorden, and Rossi, as members of
10 Maxwell's Board, each knew, or consciously disregarded, that the public statements
11 were materially false and misleading.

12 159. The Audit Committee Defendants also failed to correct the materially false
13 and misleading financial statements. The Audit Committee Defendants also signed the
14 report in Maxwell's March 30, 2012 Proxy Statement incorporating all the false and
15 misleading financial information. As such, the Audit Committee Defendants face a
16 substantial likelihood of liability. Demand is thus futile as to Guyett, Jorden, and Rossi.

17 **III. Demand Is Futile as to Cortes**

18 160. According to the Company's 2012 Proxy statement, Defendant Cortes is
19 not an independent director under NASDAQ listing standards. This decision as to
20 Cortes's lack of independence was made by the Board itself.

21 161. Defendant Cortes cannot render an independent decision because he has
22 been a director of Maxwell since 2002, receiving total compensation of \$110,000 in 2011
23 alone for his role on the Board. Demand is futile as to Cortes because instituting any
24 action would jeopardize the lavish compensation Cortes is expected to receive in future
25 years from Maxwell. Thus, demand is futile as to Cortes.

26 162. According to Maxwell's 2012 Proxy statement, Cortes owned 1,141,088
27 shares of Maxwell stock, consisting of 3.94% of the total outstanding shares. As a long-

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1 term director and large shareholder of Maxwell, Cortes dominates and controls the
2 other Board members. Thus, demand is futile as to Cortes.

3 **IV. Demand Is Futile as to All Director Defendants**

4 163. All Director Defendants – Cortes, Howsmon, Goeschel, Lavigne, Rossi,
5 Guyett, Jorden, and Schramm – face a substantial likelihood of liability for making and
6 approving the false and misleading statements set forth herein. Each of them signed
7 Maxwell’s February 16, 2012 Form 10-K, which contained the false and misleading
8 financial information that was subject to the restatement. Because all Director
9 Defendants face a substantial likelihood of liability, any demand upon them is futile.

10 164. Specifically, the Director Defendants have admitted that they permitted
11 the following material weaknesses to occur and exist during the Relevant Period:

- 12 • ***[W]e did not maintain adequately designed***
13 ***controls to ensure accurate recognition of***
14 ***revenue in accordance with GAAP.*** Specifically,
15 controls were not effective to ensure that deviations
16 from contractually established sales terms were
17 authorized, communicated, identified and evaluated
18 for their potential effect on revenue recognition.
19 Further, we did not adequately train and supervise
20 sales personnel to ensure that such personnel were
21 appropriately conscious of the requirement to
22 communicate deviations from contractually
23 established sales terms to finance and accounting
24 personnel in order for revenue recognition in our
25 financial statements to be accurately recorded.
- 26 • ***We did not perform a robust fraud risk***
27 ***assessment taking into consideration the***
28 ***various ways that fraud may be perpetrated***
to misappropriate assets or facilitate
fraudulent financial reporting. We failed to
identify controls specifically designed to prevent and
detect fraud risks relating to revenue recognition.

24 165. All Director Defendants also breached their fiduciary duties by allowing
25 Defendant Andrews, who was responsible for the improper revenue recognition, to
26 resign, instead of terminating and bringing claims against him.

27 166. Defendants Howsmon, Lavigne, Rossi, and Guyett also breached their
28 duties as members of the Compensation Committee by approving lavish compensation

1 packages for Defendants Schramm, Royal, and Andrews. This compensation included a
2 substantial performance-based component, which was both unjust and unearned in
3 light of the fact that Maxwell's financial results were inflated during the Relevant Period.

4 167. Moreover, all Director Defendants are subject to Maxwell's Code of
5 Business Conduct and Ethics. The code went well beyond the basic fiduciary duties
6 required by applicable laws, rules, and regulations. Specifically, the code required the
7 Director Defendants to "ensure that no false or intentionally misleading entries are
8 made in Maxwell's accounting records" and that all "transactions must be supported by
9 accurate documentation in reasonable detail, recorded in the proper account and in the
10 proper accounting period." The Director Defendants, however, failed to comply with
11 these requirements by causing the Company to make or allowing the Company to make
12 improper financial and business disclosures in its public press releases and filings with
13 the SEC. As a result, the Director Defendants face a substantial likelihood of liability for
14 breaching their fiduciary duties, and therefore demand upon them is futile.

15 168. If Maxwell's officers and directors are protected against personal liability
16 for their acts of mismanagement, abuse of control, and breaches of fiduciary duties
17 alleged in this complaint by D&O insurance, they caused the Company to purchase that
18 insurance for their protection with corporate funds, *i.e.*, monies belonging to the
19 shareholders. Upon information and belief, the D&O insurance policies covering the
20 Individual Defendants in this case contain provisions that eliminate coverage for any
21 action brought directly by Maxwell against the Individual Defendants, known as the
22 "insured versus insured exclusion." As a result, if the Director Defendants were to sue
23 themselves or certain of the officers of Maxwell, there would be no D&O insurance
24 protection. On the other hand, if the suit is brought derivatively, as this action is
25 brought, such insurance coverage exists and will provide a basis for the Company to
26 effectuate recovery. Therefore, the Board cannot be expected to file the claims asserted

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1 in this derivative lawsuit because such claims would not be covered under Maxwell's
2 D&O insurance policy.

3 169. Although Maxwell has been and will continue to be exposed to significant
4 losses due to the Individual Defendants' wrongdoing, the Board has not filed any
5 lawsuits against any directors or officers who were responsible for the losses. Thus, the
6 Director Defendants are breaching their fiduciary duties to the Company and face a
7 substantial likelihood of liability for their breaches. Indeed, the Director Defendants are
8 more interested in protecting themselves than they are in protecting Maxwell by
9 bringing this action. Thus, demand on the Board is futile.

10 **V. Demand Is Futile as to the Claims Against McGladrey**

11 170. The claims against Defendant McGladrey rely on the same facts as the
12 claims against the Director Defendants. Moreover, to show that McGladrey aided and
13 abetted breaches of fiduciary duties by such Defendants, the Company would first need
14 to show that the culpable directors breached their fiduciary duties.

15 171. Accordingly, in order to sue Defendant McGladrey, the Director
16 Defendants would be forced to demonstrate their own wrongdoing first, thus giving rise
17 to a "substantial likelihood of liability" and making demand futile.

18 * * *

19 172. In compliance with Section 800(b)(2) of the California Corporations Code,
20 Plaintiffs have caused a true and correct copy of this consolidated complaint to be
21 delivered to the Board before filing it with this Court.

22 **COUNT I**

23 **Breaches of Fiduciary Duties Against All Individual Defendants**

24 173. Plaintiffs incorporate by reference and re-allege each and every allegation
25 set forth above, as though fully set forth herein.

26 174. Each of the Individual Defendants owed to the Company the duty to
27 exercise candor, good faith, and loyalty in the management and administration of

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1 Maxwell's business and affairs, particularly with respect to issues regarding the
2 Company's financial reporting and internal controls.

3 175. Each of the Individual Defendants violated and breached his or her
4 fiduciary duties of candor, good faith, loyalty, and reasonable inquiry.

5 176. The Individual Defendants' misconduct set forth herein was characterized
6 by their intentional, reckless, or negligent breaches of the fiduciary duties they owed to
7 Maxwell to protect its rights and interests.

8 177. In breach of their fiduciary duties owed to Maxwell, the Individual
9 Defendants willfully participated in misrepresentation of the Company's financial
10 condition, failed to correct the Company's public statements, and failed to fully inform
11 themselves prior to making decisions as directors and officers, rendering them
12 personally liable to the Company for breaching their fiduciary duties.

13 178. The Individual Defendants had actual or constructive knowledge that they
14 had caused the Company to improperly misrepresent its financial condition and they
15 failed to correct the Company's public statements. Defendants had actual knowledge of
16 the misrepresentations and omissions of material facts set forth herein, or acted with
17 reckless disregard for the truth, in that they failed to ascertain and to disclose such facts,
18 even though such facts were available to them. Such material misrepresentations and
19 omissions were committed knowingly or recklessly and for the purpose and effect of
20 artificially inflating the price of Maxwell's securities.

21 179. These actions were not a good-faith exercise of prudent business judgment
22 to protect and promote the Company's corporate interests.

23 180. As a direct and proximate result of the Individual Defendants' breaches of
24 their fiduciary obligations, Maxwell has sustained and continues to sustain significant
25 damages. As a result of the misconduct alleged herein, Defendants are liable to the
26 Company.

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COUNT II

Abuse of Control Against All Individual Defendants

181. Plaintiffs incorporate by reference and re-allege each and every allegation set forth above, as though fully set forth herein.

182. The Individual Defendants' misconduct alleged herein constituted an abuse of their ability to control and influence Maxwell, for which they are legally responsible.

183. As a direct and proximate result of the Individual Defendants' abuse of control, Maxwell has sustained significant damages. As a direct and proximate result of the Individual Defendants' breaches of their fiduciary obligations of candor, good faith, and loyalty, Maxwell has sustained and continues to sustain significant damages. As a result of the misconduct alleged herein, the Individual Defendants are liable to the Company.

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COUNT III

Gross Mismanagement Against All Individual Defendants

184. Plaintiffs incorporate by reference and re-allege each and every allegation contained above, as though fully set forth herein.

185. By their actions alleged herein, the Individual Defendants, either directly or through aiding and abetting, abandoned and abdicated their responsibilities and fiduciary duties with regard to prudently managing the assets and business of Maxwell in a manner consistent with the operations of a publicly-held corporation.

186. As a direct and proximate result of the Individual Defendants' gross mismanagement and breaches of duties alleged herein, Maxwell has sustained and will continue to sustain significant damages.

187. As a result of the misconduct and breaches of duties alleged herein, the Individual Defendants are liable to the Company.

188. Plaintiffs, on behalf of Maxwell, have no adequate remedy at law.

COUNT IV

Unjust Enrichment Against Schramm, Royal, and Andrews

189. Plaintiffs incorporate by reference and re-allege each and every allegation set forth above, as though fully set forth herein.

190. During the Relevant Period, Defendants Schramm, Royal, and Andrews received performance-based compensation (in the form of cash bonuses and restricted shares) tied to the financial performance of Maxwell. Because Maxwell's financial results were inflated during the Relevant Period as a result of the wrongdoing alleged herein, Schramm, Royal, and Andrews received more compensation than they would have received had Maxwell's results not been inflated. Therefore, Schramm, Royal, and Andrews were unjustly enriched at the expense of and to the detriment of the Company.

191. Specifically, for 2011, Defendants Schramm, Royal, and Andrews received the following performance-based compensation – in addition to their base salaries of \$495,000, \$311,100, and \$252,000, respectively:

(a) \$336,600 (Schramm), \$105,800 (Royal), and \$87,700 (Andrews) received in performance-based bonuses;

(b) \$63,400 (Schramm), \$30,000 (Royal), and \$30,000 (Andrews) received in additional cash bonuses; and

(c) 34,265 (Schramm), 14,233 (Royal), and 10,121 (Andrews) restricted shares received.

192. The above compensation was both unjust and unearned because on August 1, 2013, the Company significantly restated its financial results for 2011.

193. During the Relevant Period, Defendants Schramm, Royal, and Andrews knew or should have known that the Company's financial results and performance were artificially inflated due to Defendants' wrongdoing.

194. By their wrongful acts and omissions, Defendants Schramm, Royal, and Andrews were unjustly enriched at the expense of, and to the detriment of, Maxwell.

1 195. To remedy these Defendants' unjust enrichment, the Court should order
2 Defendants Schramm, Royal, and Andrews to disgorge any cash bonuses, restricted
3 shares, and similar performance-based compensation that were received during, or as a
4 result of, acts performed during the Relevant Period because such compensation and
5 restricted shares were obtained by Schramm, Royal, and Andrews as a result of their
6 wrongful conduct and breaches of their fiduciary duties.

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8 **COUNT V**

9 **Breach of Duty of Honest Services Against Schramm, Royal, and Andrews**

10 196. Plaintiffs incorporate by reference and re-allege each and every allegation
11 contained above, as though fully set forth herein.

12 197. This claim is brought derivatively on behalf of the Company against the
13 Officer Defendants Schramm, Royal, and Andrews for breach of their undivided duty of
14 loyalty to their employer, Maxwell.

15 198. Schramm, Royal, and Andrews were employees of Maxwell.

16 199. As alleged above, Defendants Schramm, Royal, and Andrews breached
17 their duty of loyalty to Maxwell by not acting solely in Maxwell's interests in performing
18 their employment duties.

19 200. Those breaches of duty consisted of the conduct alleged throughout this
20 complaint including, without limitation, the Officer Defendants causing the Company to
21 make false and misleading statements to the market that misrepresented the Company's
22 business and financial prospects. Defendants Schramm, Royal, and Andrews benefitted
23 from their wrongdoing because they received performance-based compensation that
24 was directly tied to the Company's financial performance.

25 201. Maxwell was harmed by these Defendants' breaches of their undivided
26 duty of loyalty.

27 202. By reason of the foregoing, Maxwell was harmed and will continue to
28 suffer harm as described in greater detail above.

COUNT VI

Professional Negligence and Accounting Malpractice Against McGladrey

203. Plaintiffs incorporate by reference and re-allege each and every allegation set forth above as though fully set forth herein.

204. McGladrey issued “clean” or unqualified opinions on Maxwell’s financial statements for fiscal years 2011 and 2012, stating that those financial statements were presented in accordance with GAAP based on McGladrey’s audits which were performed in accordance with the Generally Accepted Auditing Standards (“GAAS”). GAAS, as approved and adopted by the American Institute of Certified Public Accountants (“AICPA”), governs the conduct of audit engagements.

205. The objective of audits of financial statements by an independent auditor is the expression of an opinion on the fairness with which they present, in all material respects, financial position, results of operations and cash flows in conformity with GAAP. The auditor’s report is the medium through which the auditor expresses his or her opinion or, if circumstances require, disclaims an opinion. In either case, the auditor states that the audit has been in accordance with GAAS. These standards required the auditor to state whether, in his or her opinion, the financial statements are presented in accordance with GAAP and to identify those circumstances in which such principles have not been consistently observed in the preparation of the financial statements of the current period in relation to those of the preceding period.

206. GAAS are comprised of ten general standards. The independent auditor is responsible for compliance with GAAS in an audit engagement. As set forth below, these standards to a great extent are interrelated and interdependent:

(a) General Standards

(i) The audit is to be performed by a person or persons having adequate technical training and proficiency as an auditor.

(ii) In all matters relating to the assignment, independence in mental attitude is to be maintained by the auditor or auditors.

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(iii) Due professional care is to be exercised in the performance of the audit and the preparation of the report.

(b) Standards of Fieldwork

(iv) The work is to be adequately planned and assistants, if any, are to be properly supervised.

(v) A sufficient understanding of the internal control structure is to be obtained to plan the audit and to determine the nature, timing, and extent of tests to be performed.

(vi) Sufficient competent evidential matter is to be obtained through inspection, observation, inquiries, and confirmations to afford a reasonable basis for an opinion regarding the financial statements under audit.

(c) Standards of Reporting

(vii) The report shall state whether the financial statements are presented in accordance with GAAP.

(viii) The report shall identify those circumstances in which such principles have not been consistently observed in the current period in relation to the preceding period.

(ix) Informative disclosures in the financial statements are to be regarded as reasonably adequate unless otherwise stated in the report.

(x) The report shall either contain an expression of opinion regarding the financial statements, taken as a whole, or an assertion to the effect that an opinion cannot be expressed. When an overall opinion cannot be expressed, the reasons therefore should be stated. In all cases where an auditor's name is associated with financial statements, the report should contain a clear-cut indication of the character of the auditor's work, if any, and the degree of responsibility the auditor is taking.

1 207. McGladrey's audits of Maxwell's financial statements issued between 2011
2 and 2012 violated each of the general standards set forth above.

3 208. McGladrey is the largest U.S. provider of assurance, tax and consulting
4 services focused on the middle market. McGladrey was the auditor of Maxwell's
5 financial statements during the Relevant Period, and was paid to review the quarterly
6 financial statements of Maxwell throughout this period. McGladrey audited Maxwell's
7 financial statements issued between 2011 and 2012, and issued the audit opinions
8 stating that those financial statements were fairly presented in accordance with GAAP,
9 and that McGladrey had audited those financial statements in accordance with GAAS.
10 Both of those statements were false. McGladrey either knew or should have been aware
11 of facts that undeniably precluded it from making those statements at the time they
12 were made. Maxwell's financial statements and McGladrey's opinions on them were
13 then used by Maxwell with McGladrey's consent to publicly disseminate Maxwell's
14 financial results in the filing of Maxwell's Form 10-K and Forms 10-Q with the SEC.

15 209. McGladrey was negligent in failing to comply with GAAS as Maxwell's
16 outside auditor. McGladrey issued unqualified opinions stating that the financial
17 statements of Maxwell were fairly presented in accordance with GAAP, when McGladrey
18 was aware of or should have been aware of facts and circumstances that undermined
19 such unqualified opinions and rendered them false and misleading.

20 210. In the course of performing audit services, McGladrey reasonably could
21 have obtained evidential matter revealing Maxwell's improper revenue recognition, but
22 improperly failed to require Maxwell to correct or adjust its financial statements or
23 make disclosure of such facts. As a result of its investigations and audit work,
24 McGladrey reasonably should have known that the reports and financial statements
25 described herein were materially false and misleading or negligently disregarded facts
26 that showed that all such statements were materially false and misleading.

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1 211. Because: (a) McGladrey spoke regularly with Maxwell's Board and Audit
2 Committee members who were knowledgeable about the undisclosed payments; and (b)
3 McGladrey attended certain of Maxwell's Board and Audit Committee meetings where
4 legal compliance was discussed, McGladrey knew or negligently disregarded facts that
5 indicated that McGladrey should have: (i) qualified its opinions on Maxwell's financial
6 statements for fiscal years 2011 and 2012; or (ii) required Maxwell to correct or adjust
7 its financial statements; or (iii) refused to give opinions in light of the materially adverse
8 effects of the undisclosed facts about Maxwell's financial condition. The failure to make
9 such qualification, correction, modification, or withdrawal was a violation of GAAS.

10 212. McGladrey also failed to require Maxwell to disclose material adverse facts
11 and allowed Maxwell to make material misrepresentations to its shareholders and to the
12 investing public.

13 213. McGladrey violated GAAS General Standard No. 3, which requires that
14 due professional care must be exercised by the auditor in performance of the
15 examination and the preparation of the audit report.

16 214. McGladrey violated GAAS Standard of Field Work No. 2, which requires
17 the auditor to make a proper study of existing internal controls, to determine whether
18 reliance thereon was justified, and if such controls are not reliable, to expand the nature
19 and scope of the auditing procedures to be applied. McGladrey reasonably should have
20 known that Maxwell's internal controls were insufficient yet still failed to expand the
21 auditing procedures.

22 215. McGladrey violated GAAS Standard of Field Work No. 3, which requires
23 sufficient competent evidential matter be obtained through inspection, observation,
24 inquiries and confirmations to afford a reasonable basis for an opinion to be issued on
25 the subject financial statements. McGladrey failed to obtain sufficient competent
26 evidential matter as to Maxwell's accounting and disclosure practices related to revenue
27 recognition.

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1 216. McGladrey violated GAAS Standard of Reporting No. 1, which requires the
2 audit report to state whether the financial statements are presented in accordance with
3 GAAP. McGladrey's opinions falsely represented that Maxwell's financial statements
4 complied with GAAP, when McGladrey knew or negligently disregarded that those
5 statements did not for the reasons herein alleged.

6 217. McGladrey violated GAAS Standard of Reporting No. 4, which requires,
7 when an opinion on the financial statements as a whole cannot be expressed, that the
8 reasons be stated. McGladrey should have either stated that no opinion could be issued
9 by them on Maxwell's financial statements or issued an adverse opinion stating that the
10 financial statements were not fairly presented.

11 218. McGladrey violated Standard of Field Work No. 1 and the standards set
12 forth in AU sections 310, 320 and 327 by, among other things, failing to adequately plan
13 its audit and properly supervise the work of its assistants so as to establish and carry out
14 procedures reasonably designed to search for and detect the existence of errors and
15 irregularities that would have a material effect upon the financial statements.

16 219. McGladrey violated SAS No. 16 in that it failed to perform its examination
17 with an attitude of professional skepticism and, in connection with the audits of
18 Maxwell's financials, ignored numerous "red flags" that would reasonably have led to
19 the discovery of the improper revenue recognition.

20 220. Defendant McGladrey violated AU section 316.20, which requires that
21 additional procedures should be performed when evaluation at the financial-statement
22 level indicates significant risk.

23 221. As a result of the foregoing, McGladrey's certification of Maxwell's
24 financial statements issued in 2011 and 2012 falsely represented that the statements
25 were audited pursuant to GAAS and that Maxwell's financial statements were presented
26 in conformity with GAAP. McGladrey knew that such certification was false and
27 misleading because, as detailed herein: (a) McGladrey knew or was negligent in not
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1 knowing that Maxwell's financial statements violated GAAP; and (b) McGladrey knew
2 those statements had not complied with GAAS.

3 222. As a result of the services rendered to Maxwell, McGladrey's personnel
4 were present or should have been present at Maxwell's corporate headquarters and
5 major operating offices and examined or participated, or should have examined and
6 participated, in reviews, investigations and audit procedures regarding the financial
7 condition, business operations and financial, accounting and management-control
8 systems of Maxwell. In the course of performing such services, McGladrey had virtually
9 unlimited access to substantial evidential matter revealing the adverse facts about the
10 Company's compliance with finance reporting requirements and laws and the finances
11 of Maxwell, but improperly failed to require adjustment for or disclosure of such facts.

12 223. McGladrey: (a) knew or was negligent in not knowing of the material,
13 adverse, non-public information about the financial statements of Maxwell, which was
14 not disclosed; and (b) participated in drafting, reviewing and/or approving the
15 misleading statements, releases, reports and other representations regarding Maxwell's
16 financial condition, including its Form 10-K for 2011 and Forms 10-Q for 2011 and 2012.

17 224. In performing auditing and accounting services on behalf of Maxwell and
18 engaging in the wrongful acts alleged herein, McGladrey knew or should have known
19 that its client would, and did, transmit false and misleading financial information to the
20 investing public. However, McGladrey failed to discharge its duties in adherence to
21 GAAP and GAAS to detect errors and irregularities and/or failed to require correction
22 and disclosure of these errors and irregularities.

23 225. In performing the auditing and accounting services to Maxwell in the
24 manner alleged herein, McGladrey owed a duty to Maxwell and its shareholders to use
25 such skill, care and diligence as other members of its profession commonly exercised.
26 McGladrey, however, breached such duty by committing the wrongful acts and conduct
27 alleged herein.

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1 226. Maxwell relied to its detriment on McGladrey and was damaged thereby.

2 227. As a direct, foreseeable, and proximate result of McGladrey's professional
3 negligence and accounting malpractice, Maxwell was damaged.

4 **COUNT VII**

5 **Aiding and Abetting Breaches of Fiduciary Duties Against McGladrey**

6 228. Plaintiffs incorporate by reference and re-allege each and every allegation
7 set forth above as though fully set forth herein.

8 229. McGladrey aided and abetted the Individual Defendants in breaching their
9 fiduciary obligations owed to Maxwell resulting in the wrongdoing and damages to the
10 Company. McGladrey knew or should have known that Maxwell's financial statements
11 for fiscal years 2011 and 2012 were materially false and misleading. McGladrey also
12 knew, or should have known, that the false and misleading information would be used,
13 in whole or in part, by Maxwell to prepare their publicly reported financial results and
14 financial statements. Nevertheless, McGladrey actively prepared the false and
15 misleading information and thereby aided and abetted the Individual Defendants'
16 breaches of fiduciary duties and their abuse of control, gross mismanagement and
17 violation of their duty of candor to Maxwell shareholders, complained of herein.

18 230. As a direct, foreseeable, and proximate result of McGladrey's aiding and
19 abetting of the Individual Defendants' breaches of fiduciary duties, Maxwell has been
20 damaged.

21 **PRAYER FOR RELIEF**

22 WHEREFORE, Plaintiffs pray for judgment in favor of Plaintiffs and Maxwell
23 and against all Defendants as follows:

24 A. Declaring that Plaintiffs may maintain this action on behalf of Maxwell
25 and that Plaintiffs are adequate representatives of Maxwell;

26 B. Declaring that the Individual Defendants have breached and/or aided and
27 abetted the breaches of their fiduciary duties to Maxwell, and that Defendant McGladrey
28

1 was negligent, committed accounting malpractice, and aided and abetted the Individual
2 Defendants' breaches of fiduciary duties;

3 C. Determining and awarding to Maxwell the damages sustained by it as a
4 result of the violations set forth above from each Defendant, jointly and severally,
5 together with pre-judgment and post-judgment interest thereon;

6 D. Directing Maxwell and the Individual Defendants to take all necessary
7 actions to reform and improve its corporate governance and internal procedures to
8 comply with applicable laws and to protect Maxwell and its shareholders from a repeat
9 of the damaging events described herein, including, but not limited to, putting forward
10 for shareholder vote the following resolutions for amendments to the Company's Bylaws
11 or Articles of Incorporation and the following actions as may be necessary to ensure
12 proper corporate governance policies:

- 13 (1) a proposal to strengthen the Audit Committee's review and
14 approval of financial reporting and internal controls over financial reporting;
15 (2) a provision to permit the shareholders of Maxwell to nominate at
16 least two candidates for election to the Board;
17 (3) a proposal to strengthen the Board's supervision of Maxwell's CEO;
18 (4) a provision to appropriately test and then strengthen the internal
19 audit and control functions; and
20 (5) a proposal to ensure the establishment of effective oversight of
21 compliance with applicable laws, rules, and regulations.

22 E. Awarding Maxwell restitution from the Individual Defendants and
23 Defendant McGladrey, and each of them, and ordering them to disgorge all profits,
24 benefits, and other compensation;

25 F. Awarding Plaintiffs the costs and disbursements of this action, including
26 reasonable attorneys' and experts' fees, costs, and expenses; and

27 G. Granting such other and further relief as the Court deems just and proper.
28

DEMAND FOR JURY TRIAL

Plaintiffs demand a trial by jury on all issues so triable.

Dated: September 27, 2013

Respectfully submitted,

BOTTINI & BOTTINI, INC.
Francis A. Bottini, Jr. (SBN 175783)
Yury A. Kolesnikov (SBN 271173)

/s/ Francis A. Bottini, Jr.
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Co-Lead Counsel for Plaintiffs

VERIFICATION

I, Stephen Neville, verify that I am a shareholder of Nominal Defendant Maxwell Technologies, Inc., and that I have continuously owned Maxwell stock since 2008. I have reviewed the allegations in this Verified Consolidated Shareholder Derivative Complaint. As to those allegations of which I have personal knowledge, I believe them to be true; as to those allegations of which I lack personal knowledge, I rely upon my counsel and counsel's investigation, and believe them to be true. Having received a copy of the complaint and reviewed it with counsel, I authorize its filing.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct. Executed on September 26, 2013.



Stephen Neville