



IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

THE POLICE AND FIRE
RETIREMENT SYSTEM OF THE
CITY OF DETROIT, derivatively on
behalf of TESLA, INC.,

Plaintiff,

v.

ELON MUSK, BRAD BUSS, ROBYN
M. DENHOLM, IRA EHRENPREIS,
LAWRENCE J. ELLISON, ANTONIO
J. GRACIAS, STEPHEN T.
JURVETSON, LINDA JOHNSON
RICE, JAMES MURDOCH, KIMBAL
MUSK, KATHLEEN WILSON-
THOMPSON, and HIROMICHI
MIZUNO,

Defendants,

-and-

TESLA, INC., a Delaware Corporation,
Nominal Defendant.

**REDACTED - PUBLIC VERSION
FILED SEPTEMBER 8, 2023**

C.A. No. 2020-0477-KSJM

**AFFIDAVIT OF CARL S. SABA IN SUPPORT OF
SETTLEMENT AND AWARD OF ATTORNEYS' FEES AND EXPENSES**

STATE OF CALIFORNIA)
) ss:
COUNTY OF SANTA CLARA)

Carl Saba, being duly sworn, deposes and states as follows:

1. I have personal knowledge of the matters stated in this declaration and, if called as a witness, would competently testify to them.

2. I am a partner at the forensic & financial consulting firm Hemming Morse, LLP. My CV is attached to this declaration as Exhibit F, and sets forth my qualifications.

3. Hemming Morse, LLP was retained by Bleichmar, Fonti & Auld, LLP and Fields Kupka & Shukurov LLP (collectively “Plaintiff’s Counsel”), as Counsel for The Police and Fire Retirement System of the City of Detroit, derivatively on behalf of Tesla, Inc. (“Plaintiff”) to calculate the presumed grant date fair value of a list of option grants provided by Plaintiff’s Counsel, which would have been granted under pre-existing Tesla’s director compensation policy in fiscal years 2021, 2022 and 2023 (“Foregone Options”).¹ I was also asked by Plaintiff’s Counsel to calculate the fair value and intrinsic value for each of the challenged options and Foregone Options as of June 16, 2023. The intrinsic value of a grant as of June 16, 2023, is calculated as the difference between the closing price of Tesla stock on June 16, 2023 and the exercise price of that same grant.

4. In order to prepare these calculations, I applied the Black-Scholes-Merton Option Pricing Model (the “Black Scholes Model”) to derive the fair value of the grants on their presumed issuance dates as well as on June 16, 2023.

5. The Black Scholes Model is a widely used method to value call and put options, which are the right to either purchase or sell the underlying security by paying or receiving the contractual exercise price associated with the options. The Black Scholes Model is discussed in AICPA guidance and practice aids as an accepted method for determining the fair value of compensatory option grants and reporting the resulting period expense in the financial statements of the company that granted the awards.² The Black Scholes Model is also widely cited in

¹ Capitalized terms not otherwise defined herein have the meaning ascribed to them in the Stipulation and Agreement of Compromise and Settlement Between Plaintiff and Settling Defendants (Trans. ID 70397017).

² *Accounting Standards Codification (ASC) 718-10-55-16* states that “a closed-form model (for example, the Black-Scholes-Merton formula) are among the valuation techniques that meet the criteria required by this Topic for estimating the fair values of share options and similar instruments granted in share-based payment transactions.” ASC 718 provides guidance under U.S. Generally Accepted Accounting Principles on determining grant date fair value and expensing of fair value of compensatory option and stock grants in a company’s financial statements.

valuation and finance textbooks as a method to value call and put options.³

6. Each Black Scholes model calculation requires the following five key inputs: (i) the underlying stock price as of the valuation date, (ii) a volatility estimate over the term of the option, (iii) the risk-free interest rate, (iv) the exercise price of the option, and (v) a time to maturity assumption.

Challenged Options

7. For the challenged options' ***fair value as of June 16, 2023*** calculations, I applied the following inputs:

- a. *Stock price:* Tesla's closing stock price on June 16, 2023 as reported by S&P CapitalIQ (www.capitaliq.com).
- b. *Volatility:* Selected volatility equal to the trailing 5-year equity volatility for Tesla as of June 16, 2023 of 66.8%.
- c. *The risk-free rate:* Valuation date U.S. Treasury Constant Maturity Rate for a term matching the time to maturity estimate for the option. This rate is used as an approximation of the riskless rate of return in the market.
- d. *The exercise price:* The exercise price was as stated per the terms in the contractual option grant agreement for each grant.
- e. *Time to maturity:* Assuming a contractual term of 7 years, the remaining expected term is conservatively estimated as the midpoint of the remaining contractual term. The majority of these options had exceeded their initial grant date expected term as disclosed by Tesla.

Foregone Options

8. For the Foregone Options' ***fair value as of June 16, 2023***

³ Ross, Westerfield, Jaffe, *Corporate Finance, Sixth Edition*, 2002, McGraw-Hill Irwin, p. 633. "It is no exaggeration to say that the Black-Scholes formula is among the most important contributions in finance. It allows anyone to calculate the value of an option given a few parameters."

calculations, I applied the following inputs:

- a. *Stock price*: Tesla's closing stock price on June 16, 2023 as reported by S&P CapitalIQ.
- b. *Volatility*: Selected volatility equal to the trailing 5-year equity volatility for Tesla as of June 16, 2023 of 66.8%.
- c. *The risk-free rate*: Valuation date U.S. Treasury Constant Maturity Rate for a term matching the time to maturity estimate for the option. This rate is used as an approximation of the riskless rate of return in the market.
- d. *The exercise price*: The exercise price was assumed to be set Tesla's closing stock price on the assumed grant date.
- e. *Time to maturity*: The remaining time to maturity was calculated assuming an initial grant date expected term of 4.3 years for the 2021 options, and 4.1 years for the 2022 options, as reported in Tesla's 2021 and 2022 10-K disclosures; and an estimated contractual term of 4.43 years for the 2023 options which represents the average of Tesla's grant date expected terms as disclosed in Form 10-K filings for fiscal years 2017 through 2022. The remaining expected term is estimated as the amount of the original grant date expected term that has not yet elapsed as of June 16, 2023.

9. For the Foregone Options' ***grant date fair value*** calculations, I applied the following inputs:

- a. *Grant date*: It is assumed that these options would be awarded according to the same schedule prior issuances of options were awarded under Tesla's pre-existing director compensation policy.
- b. *Stock price*: Tesla's closing stock price on the grant date as reported

by S&P CapitalIQ.

- c. *Volatility*: For the 2021 and 2022 options, the volatility input equal to the volatility reported by Tesla as per the company's public filing disclosures for ASC 718 compensatory grant date fair value in fiscal years 2021 and 2022. For the 2023 option grants, the selected volatility equals to the trailing 5-year equity volatility for Tesla as of June 16, 2023 of 66.8%.
- d. *The risk-free rate*: U.S. Treasury Constant Maturity Rate as of each relevant calendar year end (2021-2022) for a term matching the time to maturity estimate for the option. This rate is used as an approximation of the riskless rate of return in the market. For the 2023 grants, the U.S. Treasury Constant Maturity Rate was determined as of June 16, 2023.
- e. *The exercise price*: The exercise price was assumed to be set Tesla's closing stock price on the assumed grant date.
- f. *Time to maturity*: The expected term to maturity was selected at 4.3 years for the 2021 options and 4.1 years for the 2022 options, as reported in Tesla's 2021 and 2022 Form 10-K disclosures. The expected term to maturity for the 2023 options was set at 4.43 years, which represents the average of Tesla's grant date expected terms as disclosed in Form 10-K filings for fiscal years 2017 through 2022.

10. My calculations are detailed in **Exhibits A.1 through E** attached to this declaration. Exhibits A.1, B.1, C.1 and D.1 summarize the fair value of each grant as of June 16, 2023 and on the grant date with respect to Forgone Options, and present the intrinsic gain of all grants as of June 16, 2023. Exhibits A.2, B.2,

C.2 and D.2 document the Black Scholes Model calculations that support my conclusions.

11. Executed August 30, 2023 in Los Altos, California.

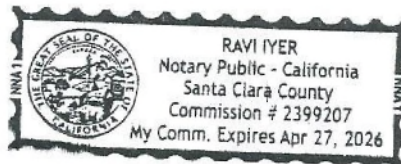


Carl S. Saba, MBA, CVA, ASA, ABV

SWORN AND SUBSCRIBED before me
this 30th day of August, 2023.



Notary Public



CERTIFICATE OF SERVICE

I hereby certify that on September 8, 2023, I caused a true and correct copy of the foregoing **Redacted – Public Version of Affidavit of Carl S. Saba in Support of Settlement and Award of Attorneys’ Fees and Expenses** to be served via File & ServeXpress on the following counsel of record:

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/s/ Sarah E. Delia

Sarah E. Delia (No. 5833)