



UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

DIVISION OF
CORPORATION FINANCE

April 4, 2019

Bradley J. Bondi
Cahill Gordon & Reindel LLP
Eighty Pine Street
New York, NY 10005-1702

Re: ***SEC v. Salix Pharmaceuticals, Ltd.*** (Civil Action No. 1:18-cv-08886) (S.D.N.Y.) (Sept. 28, 2018) - **Waiver of disqualification pursuant to Rule 506(d)(2)(ii) of Regulation D and Rule 262(b)(2) of Regulation A**

Dear Mr. Bondi:

This letter responds to your letter dated September 27, 2018 (“Waiver Letter”), written on behalf of Salix Pharmaceuticals, Ltd., (“Salix”) and constituting an application for a waiver of disqualification under Rule 506(d)(2)(ii) of Regulation D and Rule 262(b)(2) of Regulation A under the Securities Act of 1933 (“Securities Act”). In the Waiver Letter, you requested relief from any disqualification that will arise as to Salix under Rule 506 of Regulation D and Regulation A under the Securities Act as a result of the entry of a judgment (“Final Judgment”) on April 4, 2019 in the United States District Court for the Southern District of New York relating to the complaint filed by the Commission on September 28, 2018 against Salix.

Based on the facts and representations in the Waiver Letter and assuming Salix complies with the Final Judgment, we have determined that Salix has made a showing of good cause under Rule 506(d)(2)(ii) of Regulation D and Rule 262(b)(2) of Regulation A that it is not necessary under the circumstances to deny reliance on Rule 506 of Regulation D and Regulation A by reason of the entry of the Final Judgment. Accordingly, the relief requested in the Waiver Letter regarding any disqualification that may arise as to Salix under Rule 506 of Regulation D and Regulation A by reason of the entry of the Final Judgment is granted on the condition that Salix fully complies with the terms of the Final Judgment. Any different facts from those represented or failure to comply with the terms of the Final Judgment would require us to revisit our determination that good cause has been shown and could constitute grounds to revoke or further condition the waiver. The Commission reserves the right, in its sole discretion, to revoke or further condition the waiver under those circumstances.

For the Commission, by the Division of Corporation Finance, pursuant to delegated authority.

Sincerely,

/s/

Elizabeth M. Murphy
Associate Director
Division of Corporation Finance

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*ADMITTED IN DC ONLY

September 27, 2018

VIA EMAIL

Timothy B. Henseler, Esq.
Chief, Office of Enforcement Liaison
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Re: In the Matter of Salix Pharmaceuticals, Ltd. and Trading in
its Securities

Dear Mr. Henseler:

We write on behalf of Salix Pharmaceuticals, Ltd. ("Salix"), a subsidiary of Valeant Pharmaceuticals International, Inc. ("Valeant"), in connection with the settlement and entry of final judgment (the "Judgment") relating to *In the Matter of Salix Pharmaceuticals, Ltd. and Trading in its Securities*. Salix understands that the entry of the Judgment will disqualify it from relying on certain exemptions under Regulation A and Regulation D promulgated under the Securities Act of 1933 (the "Securities Act"). On behalf of Salix, we hereby respectfully request a waiver of any disqualification from these exemptions that will result from the entry of the Judgment. We respectfully submit that relief from disqualification is appropriate in this case for the reasons given below.

BACKGROUND

The staff of the Division of Enforcement (the "Staff") has engaged in settlement discussions with Salix in connection with the above-captioned investigation. As a result of these discussions, Salix submitted a Consent of Defendant Salix Pharmaceuticals, Ltd. (the "Consent"), which the Staff presented to the United States District Court for the Southern

District of New York in connection with a complaint (the “Complaint”) against Salix related to the investigation captioned above.

In the Consent, solely for the purpose of proceedings brought by or on behalf of the Commission or to which the Commission is a party, Salix consents to the entry of a final judgment permanently restraining and enjoining it from violations of Section 10(b) of the Securities Exchange Act of 1934 (the “Exchange Act”) [15 U.S.C. § 78j(b)] and Rule 10b-5(b) thereunder [17 C.F.R. § 240.10b-5(b)], Section 17(a)(2) of the Securities Act [15 U.S.C. § 77q(a)(2)], and Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Rule 13a-13 thereunder [17 C.F.R. § 240.13a-13], without admitting or denying the assertions contained therein (other than those relating to the jurisdiction of the Commission, which are admitted). The Complaint alleges that Salix’s violative conduct occurred from about 2013 to 2014, prior to Salix being acquired by Valeant.

Valeant is a publicly traded company with its common stock listed on the New York Stock Exchange and is a reporting company under the Exchange Act. Salix is a subsidiary of Valeant. Valeant acquired Salix on April 1, 2015.

DISCUSSION

Salix understands that, absent a waiver, the entry of the Judgment will disqualify it, its affiliated entities, and other issuers from relying on certain exemptions under Regulation A and Regulation D promulgated under the Securities Act. Salix is concerned that, should it or any of its affiliated entities be deemed to be an issuer, predecessor of the issuer, affiliated issuer, general partner or managing member of the issuer, promoter, underwriter of securities, or be deemed to serve in any other relevant capacity, then Salix, its issuer affiliates, and other issuers with which it is associated in one of those listed capacities and which rely upon or may rely upon these offering exemptions when issuing securities, would be prohibited from doing so. The Commission may waive Regulation A or Regulation D disqualifications upon a showing of good cause that it is not necessary under the circumstances that the exemptions be denied.

Based on the factors set forth by the Division of Corporation Finance for considering waiver requests¹ and the facts and circumstances set forth below, Salix requests that the Commission waive any disqualifying effects that the Judgment will have under Regulation A or under Regulation D.

1. *Whether the Conduct Involved the Offer and Sale of Securities*

The Complaint alleges that Salix made misrepresentations and omissions in connection with the offer and sale of securities. The Complaint alleges that over a period of three months

¹ See Division of Corporation Finance, *Waivers of Disqualification under Regulation A and Rules 505 and 506 of Regulation D* (Mar. 13, 2015).

(June 2014 to August 2014), Salix obtained money or property by means of the allegedly fraudulent statements when it sold common stock to five employees as part of the employees' exercise of Salix options pursuant to a compensation plan. As described below, Valeant has taken substantial steps to ensure that the conduct alleged in the Complaint does not recur.

2. *Whether the Conduct Involved a Scier-er-Based Violation or a Criminal Conviction*

The Division of Corporation Finance's statement on "bad actor" waivers states that the Division of Corporation Finance will "consider whether the conduct involved a criminal conviction or scier-er based violation, as opposed to a civil or administrative non-scier-er based violation."² That statement also indicates that "where there is a . . . scier-er based violation involving the offer and sale of securities, the burden on the party seeking the waiver to show good cause that a waiver is justified would be significantly greater."³

The Complaint alleges that Salix violated Section 10(b) of the Exchange Act and Rule 10b-5(b) thereunder. These are scier-er-based claims. The Complaint also alleges that Salix violated Section 17(a)(2) of the Securities Act, Section 13(a) of the Exchange Act, and Rule 13a-13 under Section 13(a) of the Exchange Act. These are not scier-er-based claims. The Complaint relates only to civil causes of action, and no criminal charges were filed against Salix or any of its directors, officers, or other employees. As mentioned above, Salix neither admits nor denies the allegations in the Complaint (other than those relating to the jurisdiction of the Commission, which are admitted).

As discussed in this letter, Salix satisfies the higher burden to show good cause that is applicable to the scier-er-based claims in the Complaint. First, as discussed in further detail below, Salix satisfies the Commission's criteria for granting a waiver after a change in control because Valeant acquired Salix on April 1, 2015 and then promptly removed the entire Salix management team. None of the individuals allegedly responsible for the conduct alleged in the Complaint is employed by, or exercises any influence over, Salix or Valeant.⁴ Second, as discussed below, Salix and its successor, Valeant, took substantial remedial steps to address Salix's prior alleged conduct.

3. *Responsibility for the Conduct*

The Complaint alleges that former officers of Salix are responsible for Salix's conduct alleged in the Complaint. As a result of an Audit Committee investigation of Salix's inventory levels, Salix's Board of Directors forced Salix's former CFO to resign in November 2014 and forced Salix's former CEO to retire in January 2015. Additionally, promptly after Valeant

² *Id.*

³ *Id.*

⁴ See Securities and Exchange Commission, *Disqualification of Felons and Other "Bad Actors" From Rule 506 Offerings*, SEC Release No. 33-9414, 2013 WL 3817311, at *13 (July 10, 2013).

acquired Salix on April 1, 2015, Valeant removed the entire Salix management team. None of the officers or directors who were employed by Salix or who were on the Board of Salix before Valeant's acquisition has any current role with or influence over Salix or Valeant. Consistent with the Division of Corporation Finance's statement on "bad actor" waivers, Salix and Valeant's removal or termination of individuals associated with the alleged misconduct weighs in favor of Salix's waiver request.⁵

4. *Duration of the Conduct*

The Complaint states that the duration of the alleged conduct was limited to approximately May 2013 to October 2014. All of the alleged conduct occurred prior to Valeant's April 1, 2015 acquisition of Salix.

5. *Remedial Steps*

The Commission has expressed its intention that waivers of Rule 506 disqualification be issued "upon a proper showing that there has been a change of control and the persons responsible for the activities resulting in a disqualification are no longer employed by the entity or exercise influence over such entity."⁶ In this case, both elements are satisfied. First, there has been a change of control: Valeant acquired Salix on April 1, 2015, and Salix became subject to Valeant's management and Board of Directors. Second, none of the individuals allegedly responsible for the conduct alleged in the Complaint is employed by Salix or Valeant or exercises influence over either entity—eliminating any prospect of those individuals repeating the alleged conduct at Valeant. Before the acquisition, Salix's Board of Directors forced the resignation or retirement of certain officers that the Complaint alleges are responsible for the alleged conduct. After the acquisition, Valeant promptly removed the entire remaining Salix management team.

Salix and Valeant have taken additional remedial steps to address the conduct alleged in the Complaint. Upon learning of allegations involving its inventory levels, Salix's internal and external counsel immediately took action to determine if those allegations had any merit. After initial inquiries, all such advisors recommended to the Audit Committee of Salix's Board of Directors that the Audit Committee should hire counsel to conduct a thorough and independent investigation. In response to these recommendations, the Audit Committee promptly engaged counsel (as well as an independent forensic accounting firm to work with counsel) to investigate the allegations in more detail, and to ascertain whether any additional problems existed. Audit

⁵ See Division of Corporation Finance, *Waivers of Disqualification under Regulation A and Rules 505 and 506 of Regulation D* (Mar. 13, 2015) ("[I]f misconduct committed by one or more individuals resulted in the waiver applicant's disqualification, and the applicant removes or terminates its association with those individuals, the Division would generally view such actions taken as favorable to the waiver request.").

⁶ See Securities and Exchange Commission, *Disqualification of Felons and Other "Bad Actors" From Rule 506 Offerings*, SEC Release No. 33-9414, 2013 WL 3817311, at *13 (July 10, 2013).

Committee counsel was engaged formally in mid-October 2014, and in a matter of days Salix reported the conduct to the SEC on October 29, 2014.

As mentioned above, Salix's Board of Directors forced the resignation or retirement of certain officers. At that time, Salix's bylaws required it to advance these officers' attorneys' fees. To ensure their cooperation in the investigation, Salix's Board persuaded each of these officers to sign agreements requiring, *inter alia*, that they cooperate with Salix in connection with any internal investigation or any external investigation or proceeding relating to Salix, including by agreeing to provide truthful statements or testimony as a declarant or witness in connection with any such investigation. Those agreements also contained a provision that permitted the Board to claw back any unvested shares if the Board found that a relevant officer intentionally engaged in conduct detrimental to Salix. Such a clawback was not previously available under these officers' then-existing employment agreements.

Subsequently, in March 2015, after reviewing the findings of the Audit Committee's independent investigation and at Valeant's request, the Board executed the clawback provisions in those officers' agreements, and clawed back \$38.7 million in equity compensation from them. In addition, Salix eliminated or reduced bonuses for many high-level executives with knowledge of the alleged conduct.

Additionally, after Valeant acquired Salix, Valeant's own internal controls became effective with respect to Salix's products. Unlike Salix, which had no inventory management agreements prior to the acquisition, Valeant immediately applied its wholesaler distribution agreements to the Salix products. Currently, Valeant has distribution agreements with the three largest wholesalers in the United States.⁷ Pursuant to these agreements, Valeant receives actual on-hand inventory and sales data on a daily basis and receives inventory demand data on a weekly basis, enabling all relevant parties to access accurate data. To limit the amount of inventory at Valeant's wholesalers, the distribution agreements contain target inventory levels between half a month and two months of Valeant's products, based on historical demand.⁸ Valeant's management reviews these inventory levels on a weekly, monthly, and quarterly basis.

Valeant also has specific policies and procedures, to which Salix is subject, which will prevent the alleged misconduct at issue from recurring in the future. For example, product returns are processed in accordance with an established return policy, and Valeant only grants credit for products that are returned within six months before the expiration date of the product or within 12 months after the expiration date. The return policy does not allow credit for returns of saleable product, such as a wholesaler's overstock. Any credit for a return outside of the policy's criteria requires approval pursuant to a matrix that is based on the dollar value of the product to be returned. Valeant also has an enterprise resource planning system that ensures delivery of products to wholesalers is booked in the quarter in which the sale contractually occurred. This system will not allow a shipment to be recorded in a period after the period has

⁷ See Valeant Pharmaceuticals International, Inc., Annual Report (Form 10-K), at 90 (Feb. 28, 2018).

⁸ See *id.*

ended. In addition, Valeant performs proof-of-delivery testing on shipments to wholesalers to ensure proper revenue recognition.

6. *Impact If the Waiver Is Denied*

The disqualification of Salix from relying on the exemptions under Regulation A and Regulation D would have an adverse impact on third parties, namely innocent Salix and Valeant shareholders who did not benefit in any way from the alleged misconduct at Salix. While Salix is currently a wholly owned subsidiary of Valeant, in the future it may be independent and need to raise capital to finance its operations. For example, in November 2016, Valeant was in discussions with third parties concerning divesting Salix,⁹ and Valeant may divest Salix or pursue other options in the future.

A disqualification would have an unfair, disproportionate, and prejudicial impact on Valeant's shareholders. Valeant's ability to divest Salix, to spin it off in an initial public offering, or to merge it with another company for the benefit of Valeant's shareholders could be thwarted by the uncertainty of Salix's future eligibility to avail itself of exemptions under Regulation A and Regulation D. In particular, Valeant's inability to represent that Salix will be eligible to rely on such exemptions could chill potential acquirers' interest in Salix as an acquisition target or depress the price a potential acquirer is willing to pay for Salix. These uncertainties unfairly prejudice Valeant's innocent shareholders because all of the alleged misconduct occurred prior to Valeant acquiring Salix and Valeant's shareholders did not benefit in any way from the alleged misconduct at Salix. Denying the waiver requests and hindering Valeant's efforts to pursue a transaction involving Salix for the benefit of Valeant's shareholders imposes disproportionate harm on Valeant's shareholders.

Furthermore, if Valeant divests or spins off Salix and Salix is prohibited from availing itself of the exemptions under Regulation A or Regulation D, then the innocent shareholders of Salix, who did not benefit in any way from the alleged conduct at Salix, would be harmed.

CONCLUSION

For the reasons stated above, Salix respectfully requests that the Commission (or the Division of Corporation Finance pursuant to delegated authority) waive, effective as of the date

⁹ See Valeant Pharmaceuticals International, Inc., *Valeant Pharmaceuticals Comments on Press Report Regarding Its Gastroenterology Business Unit* (Nov. 1, 2016), available at <http://ir.valeant.com/news-releases/2016/11-01-2016-213619928> ("We are currently in discussions with third parties for various divestitures including but not limited to Salix.").

of entry of the Judgment, any disqualification under Regulation A or Regulation D with regard to Salix arising as a result of such entry.¹⁰

Please let us know if you have any questions.

Sincerely,



Bradley J. Bondi

cc: Johanna Losert (SEC)
Michael Kaplan (Davis Polk & Wardwell LLP)
Sophia Hudson (Davis Polk & Wardwell LLP)

¹⁰ The Commission has granted relief under Rule 262 of Regulation A and Rules 505(b)(2)(iii)(C) and 506(d)(2)(ii) of Regulation D for similar reasons or in similar circumstances. *See, e.g.*, Diamond Foods, Inc., SEC No-Action Letter (Mar. 6, 2014) (waiver after violation of Section 17(a) of the Securities Act and Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11, and 13a-13).