UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

CASE NO. 1:11-CV-24438-GAYLES

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

STIEFEL LABORATORIES INC. and CHARLES W. STIEFEL,

Defendants.

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SECURITIES AND EXCHANGE COMMISSION'S REPLY TO OBJECTIONS TO DISTRIBUTION PLAN BY FOUR OBJECTORS (DE 250)

I. Introduction

The Securities and Exchange Commission has proposed equitably distributing the $37 million Fair Fund in this case to defrauded shareholders based on an expert valuation of Stiefel Laboratories share prices as of March 31, 2006, 2007, and 2008, respectively. Nonetheless, by cherry picking facts and misrepresenting the law governing Commission distribution plans, four former Stiefel Laboratories shareholders ("the Objectors") ask this Court in their objections (DE 250) to ignore the standards and equitable distribution principles the Commission used in its Distribution Plan to treat all defrauded shareholders equally.

Instead, based on their subjective and false claim that the fraud Defendants Stiefel Laboratories ("Stiefel Labs") and Charles W. Stiefel ("Stiefel") perpetrated on them was worse than the fraud the Defendants perpetrated on other shareholders, the Objectors ask the Court to arbitrarily favor them in the Distribution Plan at the expense of other defrauded shareholders. They do so using a legally unsound and factually unsupported methodology to calculate the Distribution

Payments they should receive. In addition, two of the Objectors ignore a directly on-point federal statute by claiming the Fair Fund should subsidize attorneys' fees and costs they paid in private settlements, which will reduce the amount of recoveries all other shareholders will receive. For the reasons set forth in the rest of this Reply, the Court should deny the objections.

The Objectors present two objections to the Commission's Distribution Plan. First, all four object to the expert's valuation of the March 31, 2008 Stiefel Labs share price the Commission used to calculate Distribution Payments to shareholders who sold stock to the company in late 2008 and early 2009. They claim the Court instead should arbitrarily choose a higher share price based on a damages award received by one shareholder in a private lawsuit, and ignore the law on disgorgement and the expert valuations the Commission used to determine Distribution Payments to all harmed shareholders. Second, two of the four Objectors claim the Commission wrongly excluded them from receiving Distribution Payments because the Commission did not give them credit for attorneys' fees and costs paid out of recoveries they received from the Defendants years ago in private lawsuits. Neither objection has merit.

The Court should deny the first objection for three primary reasons: (1) the Commission's Distribution Plan easily meets the "fair and reasonable" standard the Court must use to evaluate it; (2) the Objectors' proposed higher share price (based on a change-of-control transaction that took place months later) to calculate Distribution Payments is a legally incorrect measure of Stiefel Labs' disgorgement in this case; and (3) the factual premise of the Objectors' claim – that the fraud committed on them was worse than the fraud committed on other former shareholders – is wrong and legally irrelevant. In contrast, the evidence supporting the Commission's Distribution Plan – including an attached declaration from the Commission's expert Marc Brown – shows the Distribution Plan is legally sound and factually supported.

Second, with regard to the attorneys' fee objections, the Objectors failed to disclose to the Court there is a federal law specifically prohibiting the Commission from considering attorneys' fees in its distribution fund calculations. *See* Section 21(d)(4) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. 78(u)(d)(4)]. The statute is dispositive, and mandates denying this objection. Furthermore, even if the Commission subtracted attorneys' fees and costs from the private lawsuit recoveries, the two Objectors still received more in the private lawsuits than they would receive under the Commission's Distribution Plan. Thus, their objection is moot unless the Court sustains the first objection. Finally, other than the four Objectors represented by the same attorney, not a single shareholder in the 2008-2009 group objected to the Distribution Plan.

II. Factual And Procedural Background

The Objectors claim the fraud committed on them was somehow worse, or "the more sinister of the frauds" (Objections, DE 250, at 12), than the fraud committed on shareholders who sold to the company in earlier time periods. Therefore, the Objectors claim their group of shareholders should be compensated differently than other groups. However, this theory is directly contrary to the allegations of the Commission's Complaint.[1] Those allegations show the Complaint alleges virtually identical fraud by the Defendants against all harmed shareholders.

A. The Commission's Complaint

The Commission filed suit against Stiefel Labs and Stiefel in December 2011, alleging that from late 2006 through April 2009, they engaged in a fraudulent scheme to purchase shares of Stiefel Labs stock, primarily from current and former employees, at severely undervalued prices. Complaint, DE 1 at ¶1. The Defendants failed to disclose to shareholders and a third party valuing

[1] The Court should disregard the Objectors' inclusion of allegations from private lawsuits against the Defendants. Only the allegations of the Commission's Complaint are relevant to the Commission's Distribution Plan.

the shares material information crucial to valuing the stock. *Id.* at ¶3.

Beginning in approximately 1975, Stiefel Labs' employees began acquiring Stiefel Labs common stock as part of the company's Employee Stock Bonus Plan ("Plan"). *Id.* at ¶13. Each year from 1975 to 2008, Stiefel Labs made discretionary contributions to the Plan with Stiefel Labs stock. *Id.* at ¶14. Stiefel Labs allocated contributions to employee accounts based on length of employment and compensation. *Id.* Prior to November 2008, only Plan shareholders who retired, were terminated, or left Stiefel Labs could sell their stock back to the company. *Id.* at ¶32.

To determine the price Stiefel Labs would pay Plan shareholders for stock buybacks (and other Plan purposes), Stiefel Labs engaged a third-party accountant to value the stock who relied on the company's financial statements and other information Stiefel Labs gave him. *Id.* at ¶18. The accountant valued the stock price as of March 31 of each year. *Id.* Stiefel communicated the results of those valuations to shareholders later each calendar year. *Id.* However, this third-party accountant used a flawed methodology and was not qualified to perform the valuations. *Id.* Also, the Defendants failed to disclose to the accountant crucial information about offers and valuations the company received from investment firms. *Id.* at ¶19.

The Complaint goes on to allege the Defendants defrauded shareholders selling shares back to the Company in three different time periods – those shareholders selling following the as of March 31, 2006 valuation, the as of March 31, 2007 valuation, and the as of March 31, 2008 valuation. *Id.* at ¶¶21-36. The allegations of fraud in each year follow an identical pattern – the third-party accountant undervalued Stiefel Labs shares because Stiefel and the company failed to disclose to him (and subsequently to shareholders) significant financial events involving outside parties' interest and investment in Stiefel Labs. *Id.*

For example, the Complaint alleges that in 2006, prior to the as of March 31, 2006 share price being valued and communicated to shareholders, Stiefel Labs engaged a financial advisor to explore interest from private equity firms in investing in the company. *Id.* at ¶21. Shortly after the $13,012 share value was announced, five private equity firms offered to acquire $200 million of Stiefel Labs preferred shares at valuations 50 to 200 percent higher than $13,012 per share. *Id.* at ¶23. The Defendants failed to disclose this crucial information to shareholders selling stock back to the company at $13,012 per share in late 2006 and for much of 2007. *Id.* at ¶24.

Similarly, before the as of March 31, 2007 price was announced, a subsidiary of one of the private equity firms, Blackstone Healthcare Partners, offered first to buy Stiefel Labs and later invested approximately $500 million in the company. *Id.* at ¶¶25-26. For this, Blackstone received preferred shares valued at amounts far higher than the $14,517 valuation price as of March 31, 2007. *Id.* at ¶¶26-27. The Defendants did not disclose to the accountant and to most shareholders selling stock back to the company in late 2007 and for most of 2008 the offers from the five equity firms in 2006, Blackstone's offer to buy Stiefel Labs, the valuation Blackstone placed on the Company when it purchased 19 percent of the company, and other information. *Id.* at ¶¶28-29.

Finally, after the as of March 31, 2008 share price of $16,469 was announced in October 2008, the Defendants failed to disclose to numerous selling shareholders in December 2008 and the first three months of 2009 that Stiefel and Stiefel Labs were actively trying to sell the company – in direct contravention of statements Stiefel and other family members had made over the years that they intended to keep Stiefel Labs a private company. *Id* at ¶¶30-36. As the Objectors note, there were more selling shareholders during this time than in previous years because in November 2008, Stiefel Labs began an "optional diversification" program encouraging then-current employees to sell their Plan stock back to the company. *Id.* at ¶32. But as discussed in more detail in Section III.C below, the fact that there were more selling shareholders during this time than in previous years is irrelevant to whether the Distribution Plan is fair and reasonable.

Thus, the Complaint's detailed factual allegations make it clear that the fraud committed against Stiefel Labs shareholders followed an identical pattern each year and was egregious in each year. *Id.* at ¶¶21-36. Furthermore, the Complaint alleges that the Defendants should have disclosed the events in question *each year* to shareholders and should have updated their annual valuations *each year*. *Id.* at ¶¶42-47.

Moreover, the Commission's Complaint alleges the factual basis for the Commission's disgorgement remedy: "The Defendants benefitted greatly from their scheme. Each time Stiefel Labs purchased stock back, *it saved considerable money by not paying the shareholders the fair market value of their stock under the Plan.*" *Id.* at ¶4 (emphasis added).

B. Procedural History

The Complaint alleges the Defendants violated Section 10(b) and Rule 10b-5 of the Exchange Act, and sought, among other things, injunctions, disgorgement of ill-gotten gains, and civil penalties. *Id.* at pp. 19-22. After years of extensive litigation, the Defendants and the Commission mediated the case for a second time on February 26, 2020, and agreed on a proposed settlement that the Commission subsequently approved. As a result, on June 4, 2020, the Court created a Fair Fund and entered Final Judgments by consent against Stiefel Labs and Stiefel (DE 233, 234, and 235). Under terms of the Final Judgments, Stiefel Labs and Stiefel neither admitted nor denied the allegations of the Complaint and agreed to pay in the aggregate $37 million.[2] The

[2] The Objectors appear to question the settlement on Page 7 of their objections when they state "the SEC settled its $110 million disgorgement claim for $37 million, or approximately 33.6%." The first paragraph of the Complaint states the Defendants defrauded shareholders out of more than $110 million. However, that does not mean the $110 million was the Commission's disgorgement claim, and the Objectors' attempt to characterize it as such confuses damages investors may have suffered with the separate measure of disgorgement – the amount by which the Defendants illegally profited. As discussed in Section III.B below, the two concepts have separate legal meaning and are computed differently. Also, as explained in the Distribution Plan (DE 240-1 at 7-8) and in Section III.B, the Commission's expert witness' calculations

Final Judgment against Stiefel Labs orders the Company to pay disgorgement of $23 million, prejudgment interest on disgorgement of $2,210,000, and a civil penalty of $1.3 million. The Final Judgment against Stiefel orders him to pay disgorgement of $9.3 million, prejudgment interest on disgorgement of $930,000, and a civil penalty of $260,000.

Following entry of the Final Judgments and creation of the Fair Fund, the Court entered additional orders appointing undersigned Commission counsel as the Distribution Agents, a Tax Administrator, and a Third Party Fund Administrator for the Fair Fund (DE 237, 239). Then on September 24, 2020, the Commission moved the Court to approve its Distribution Plan (DE 240), leading to the current objections.

C. The Distribution Plan

The Commission proposes a Distribution Plan methodology that will distribute the $37 million Fair Fund to Eligible Shareholders based on the work of an independent third-party expert, who has determined the amounts by which Stiefel Labs undervalued its shares each year in the as of March 31 valuations. The Distribution Plan is thus based on objective evidence, proposes an equitable distribution to all three groups of harmed Plan shareholders[3] based on identical criteria, and is consistent with the allegations of the Complaint that Stiefel Labs undervalued its shares each year. Complaint at ¶¶1-4 and 21-36; Distribution Plan (DE 240-1) at Pages 6-9.

The Complaint alleges the Defendants benefitted from undervaluing the shares Stiefel Labs

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show Stiefel Labs' profits were approximately $40.8 million from purchases from Eligible Shareholders in the Distribution Plan. The Commission's settlement recovered more than 90 percent of that amount. In addition, the Objectors have no standing to question the settlement and the previously entered Final Judgments. *Official Committee of Unsecured Creditors of Worldcom, Inc. v. SEC*, 467 F.3d 73, 81-83 (2d Cir. 2006); *SEC v. Spence & Green Chemical Co.*, 612 F.2d 896 (5th Cir. 1980).

[3] There are 258 Eligible Shareholders in the Distribution Plan, 245 of whom sold through the Stiefel Labs Plan. The remaining 13 shareholders sold outside the Plan. In addition, there were 29 Excluded Shareholders, who were excluded for several reasons set forth in the Distribution Plan at Page 3.

purchased from employees "by not paying the shareholders the fair market value of their stock under the Plan." Complaint at ¶4. Consistent with those allegations, the Commission retained a valuation expert during the litigation of this matter to determine what the fair market value of the Plan stock actually was at each of the as of March 31 valuations because Stiefel Labs used the as of March 31 valuations to set the prices at which it repurchased stock from shareholders. Distribution Plan at 7-8. Marc Brown is a managing director of Alix Partners, a financial and operational consulting firm with more than 2,000 employees in 23 offices worldwide. Mr. Brown is Alix Partner's Valuation Services Practice Coordinator, has more than 20 years of professional experience in valuing public and private companies, and has extensive experience in valuing companies in the healthcare and pharmaceutical industries.[4]

Using several well-accepted valuation methods, Mr. Brown determined the true value of the Stiefel Labs Plan shares as of March 31, 2006, 2007, and 2008.[5] Mr. Brown's report found the following differences in price between what the Defendants paid Plan shareholders and what the shares were actually worth.

Year	**Price Per Share Paid**	**Expert Valuation Per Share**	**Difference Per Share**
As of March 31, 2006	$13,012	$34,300	$21,288
As of March 31, 2007	$14,517	$56,800	$42,283
As of March 31, 2008	$16,469	$40,600	$24,131

[4] Mr. Brown's additional qualifications and experience are set forth in his CV in his report, which is attached as Exhibit 1 to Exhibit A to this Reply. The Objectors do not present any expert valuation to contradict Mr. Brown's opinion.

[5] Mr. Brown's report adopted the report of Bruce Den Uyl, the Commission's original expert from Alix Partners. Mr. Den Uyl passed away during the litigation and Mr. Brown, who had worked with Mr. Den Uyl, substituted for him. Mr. Brown's report has not previously been filed, but it is identical to Mr. Den Uyl's report, which was filed (DE 145-15) and which the Objectors cited in their objections.

The Commission used those values to calculate the amount of ill-gotten gains Stiefel Labs realized from undervaluing its shares in the buybacks at issue, i.e., for Stiefel Labs' Plan shareholders $21,288 per share in 2006, $42,283 per share in 2007, and $24,131 per share in 2008. The Commission also used those values to determine Stiefel Labs' ill-gotten gains from sales to non-Plan shareholders, as described in more detail in the Distribution Plan at page 9. The Commission then calculated each harmed shareholder's *pro rata* share of the Total Net Loss as described in the Distribution Plan at Page 9. Under the Distribution Plan each shareholder will receive approximately 90.5 percent of his or her Net Loss using the share prices set forth above.

III. Memorandum Of Law

A. The Fair And Reasonable Standard

The Objectors correctly state that the Court must determine whether the Commission's Distribution Plan is fair and reasonable, and that under that standard the Court should give deference to the Commission's plan. Objections at 11. However, the Objectors then essentially ask the Court to ignore that standard and assert that the District Court has unbridled discretion to evaluate Commission distribution plans against other proposed plans. *Id.* at 11, 13. This is not the case.

As the two courts that adopted the fair and reasonable standard stated, while District Courts always have discretion to determine how disgorged funds will be distributed,[6] the fair and reasonable standard does not give the Court open-ended discretion. Under that standard, "once the district court satisfies itself that the distribution of proceeds in a proposed SEC disgorgement plan is fair and reasonable, its review is at an end." *Worldcom*, 467 F.3d at 82, quoting *SEC v. Wang*, 944 F.2d 80, 85 (2d Cir. 1991). Because the Commission is charged by statute with

[6] *Worldcom*, 467 F.3d at 81.

enforcing the securities laws, courts should "defer to its 'experience and expertise' in determining how to distribute the funds." *Worldcom*, 467 F.3d at 82, quoting *Wang*, 944 F.2d at 88.

Under the fair and reasonable standard, District Courts should not weigh competing plans and decide which is the most fair and reasonable. *SEC v. J.P. Morgan Securities, Inc.*, 266 F. Supp. 3d 225, 227 (D.D.C. 2017) ("when the Securities and Exchange Commission devises a settlement distribution plan, a court does not consult a looking glass and ask whether it is the fairest of them all. The only question is whether such a plan is sufficiently fair and reasonable"); *Worldcom*, 467 F.3d at 84 ("limits are inevitable because the government did not recoup some endless wellspring of funds . . . when funds are limited, hard choices must be made"); *SEC v. CR Intrinsic Investments*, 164 F. Supp. 3d 433, 435 (S.D.N.Y. 2016) ("The standard of review for a proposed Fair Fund distribution plan 'fairly and reasonably distributes the limited Fair Fund proceeds among the potential claimants . . . nearly every plan to distribute funds obtained in an [SEC] enforcement action requires choices to be made regarding the allocation of funds between and among potential claimants within the parameters of the amounts recovered").

Courts routinely approve Commission Fair Fund distribution plans over the objections of claimants, particularly when, as here, the Commission's goal is to achieve an equitable and *pro rata* distribution of limited recovered funds. *Intrinsic Investments*, 164 F. Supp. 3d at 435-36 (denying investors' objections and approving a Commission distribution plan "because the SEC provides a reasonable and detailed justification for doing so in the interest prioritizing equitable distribution to injured investors"); *J.P. Morgan*, 266 F. Supp. 3d at 231 (denying objections because "[e]ven if the Objector's alternative makes some sense, the Amended Plan's proportional scheme is still a fair and reasonable one. Courts have favored *pro rata* distribution of assets where, as here . . . victims were similarly situated with respect to their relationship to the defrauders");

Worldcom, 467 F.3d at 84 ("It is clear that the SEC considered carefully how best to apportion investors"). As set forth in the following sections, the Commission's Distribution Plan more than satisfies the fair and reasonable standard, and the Court should approve it.

B. The Commission's Plan Is Fair And Reasonable Because It Is Based On The Amount We Could Recover Through The Disgorgement Remedy

As discussed in the Distribution Plan and in Section II above, the Commission's remedy to recover funds from the Defendants as a result of the fraud is disgorgement of their ill-gotten gains. *SEC v. Commonwealth Chemical Securities, Inc.*, 574 F.2d 90, 102 (2d Cir. 1978) ("the primary purpose of disgorgement is not to compensate investors. Unlike damages, it is a method of forcing a defendant to give up the amount by which he was unjustly enriched"); *SEC v. Tome*, 833 F.2d 1086, 1096 (2d Cir. 1987) (same); *SEC v. Huff*, 758 F. Supp. 2d 1288, 1358 (S.D. Fla. 2010) (emphasis added) ("Because disgorgement is remedial and not punitive, a court's power to order disgorgement *extends only to the amount with interest by which the defendant profited from his wrongdoing*"), quoting *SEC v. Blatt*, 583 F.2d 1325, 1335 (5th Cir. 1978). The Supreme Court recently reiterated this definition in *Liu v. SEC*, 140 S. Ct. 1936, 1947 (2020) ("Accordingly, Congress' use of the term 'disgorgement' in assorted statutes did not expand the contours of that term beyond a defendant's net profits—a limit established by longstanding principles of equity").

Under that controlling law, the Commission's disgorgement recovery is limited to the Defendants' actual profits. In the case of Stiefel Labs, that means the amount the Defendants underpaid shareholders in all three time periods for the shares they sold back to the company. As alleged in the Complaint, Stiefel Labs bought shares in specific transactions each year based on the three flawed as of March 31 valuations. Thus, to determine what Stiefel Labs' actual profits were, the Commission's task was to identify the share prices the company should have paid in those transactions if the as of March 31 valuations had been accurate, and then determine the difference between the accurate valuations and the flawed valuations the company used.

As described in Section II.C above, the Commission retained Mr. Brown to do this work. Mr. Brown determined the true value of the shares in each of the three valuations was $34,300 for March 31, 2006 (as opposed to the $13,012 price Stiefel Labs used), $56,800 for March 31, 2007 (as opposed to the $14,517 price Stiefel Labs used), and $40,600 for March 31, 2008 (as opposed to the $16,469 price Stiefel Labs used). The differences each year constituted Stiefel Labs' profits in transactions. The Commission used those calculations to develop the Distribution Plan. Thus, the Commission's Distribution Plan is based on objective evidence (Mr. Brown's valuations) and the controlling case law on disgorgement. Furthermore it treats all defrauded shareholders equally because the Commission determined each shareholder's Net Loss using an identical methodology. In addition, each shareholder gets the same *pro rata* share of their Net Loss.

Those factors alone lead to the conclusion that the Distribution Plan is fair and reasonable. *J.P. Morgan*, 266 F. Supp. 3d at 231 (denying objections because "[e]ven if the Objector's alternative makes some sense, the Amended Plan's proportional scheme is still a fair and reasonable one. Courts have favored *pro rata* distribution of assets where, as here . . . victims were similarly situated with respect to their relationship to the defrauders"); *Worldcom*, 467 F.3d at 84 ("It is clear that the SEC considered carefully how best to apportion investors"); *Intrinsic Investments*, 164 F. Supp. 3d at 435-36 (denying investors' objections and approving a Commission distribution plan "because the SEC provides a reasonable and detailed justification for doing so in the interest prioritizing equitable distribution to injured investors").

In contrast, the Objectors' request to use a much higher share price - $69,705 – for the 2008-2009 sales is neither fair nor reasonable. As set forth in Sections II.A and C and immediately above, that price is not a measure of the Defendants' ill-gotten gains, which is the remedy the

Commission is limited to. Rather it is the measure of a damages award a jury gave to one former shareholder in a private lawsuit against Stiefel Labs and Stiefel – based on the shareholder alleging the damages he suffered as a result of his decision to sell at Stiefel Labs' offered price of $16,469, rather than keeping his shares until GlaxsoSmithKline ("GSK") bought Stiefel Labs in July 2009. However, for purposes of disgorgement, the Commission cannot assume a hypothetical set of facts that the Objectors want the Court to accept – that the Objectors and other shareholders did not sell their shares in January and February of 2009 (when in fact they did) and therefore would have received the higher share price in a GSK sale. *Commonwealth Chemical*, 574 F.2d at 102 ("the primary purpose of disgorgement is not to compensate investors. Unlike damages, it is a method of forcing a defendant to give up the amount by which he was unjustly enriched").[7]

The Objectors claim the Commission's use of Mr. Brown's as of March 31, 2008 valuation "is not supported by anything the SEC has alleged in this case." Objections at 8. That statement is patently false. The allegations of the Complaint demonstrate that the Defendants used the March 31, 2008 valuation to repurchase shares from the Objectors and other similarly situated shareholders. Therefore the proper measure of Stiefel Labs' disgorgement and the harm to shareholders is Mr. Brown's calculation of the true share price in the as of March 31, 2008 valuation. *See* Section II.C above and the discussion of the law of disgorgement in this section.

It is the Objectors, not the Commission, who have picked an arbitrary date and price in an effort to boost their Distribution Payments. The Objectors attempt to justify their selection by

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[7] The 11th Circuit's affirmation of the jury's damages verdict, cited by the Objectors on Pages 3 and 6 of their objections, is of no precedential value. That opinion held that there was sufficient evidence to support the jury's damages award. *Finnerty v. Stiefel Laboratories*, 756 F.3d 1310, 1315 n.8 (11th Cir. 2014). The opinion did not address whether the share price at issue was the proper measure of either the Defendants' disgorgement or shareholder harm in developing a Commission distribution plan. As demonstrated in this Reply, the amount of damages a private plaintiff suffered is not a proper value on which to base the Distribution Plan payments.

cherry picking allegations from the Commission's Complaint that asserted the Defendants should have updated their as of March 31 valuations to account for the information they did not disclose to the Objectors and other shareholders. *See, e.g.*, Objections at Pages 8-9. However, the Defendants erroneously conflate the Commission's allegations constituting the fraud in the case – the Defendants should have disclosed the information and/or updated their valuations – with the *remedy* for the fraud, which is disgorgement. Stiefel Labs' disgorgement in this case is limited to the price the Defendants should have paid all groups of shareholders based on the true value of the shares in the as of March 31 valuations – the valuations the Defendants used to repurchase shares.

Even if the Court were to accept the premise that the Commission should have used February 13, 2009 to value the shares the Objectors and other later-selling shareholders sold back to Stiefel Labs, the Objectors have presented no evidence as to what the value of the shares actually was on that date. The *Finnerty* verdict is not evidence of what the share price was on February 13 for Plan shareholders. It demonstrated only what Finnerty's damages were as a result of GSK's purchase of Stiefel Labs that closed in July 2009.

To address this question, Mr. Brown prepared a declaration, attached as Exhibit 1, to supplement his report. That declaration shows that the $69,705 share price the Objectors use was based on what Stiefel Labs announced GSK was offering to pay in April 2009 to buy Stiefel Labs *in its entirety* – i.e., the purchase price contained a control premium. Brown Declaration at ¶4. Mr. Brown's declaration shows that any price the Objectors would have received in February 2009 would have been significantly discounted from $69,705 per share to account for the fact that the Objectors owned minority shares, not control of the entire company. *Id.* Mr. Brown's declaration goes on to show that the $69,705 price would have been further discounted by the fact that the Objectors' shares were not marketable. There was no free-trading market for Stiefel Labs shares;

in reality the company was the only buyer. *Id.* at ¶5. Finally, as Mr. Brown points out, any updated valuation in February 2009 would have to take into account the worsening economy between March 2008 and 2009, as well as Stiefel Labs' declining revenue and profits. *Id.* at ¶¶6-8.

Thus, Mr. Brown's declaration shows that any true valuation of the Objectors' minority, unmarketable shares in February 2009 may well have been *lower* than the $40,600 price the Commission used to determine the Objectors' Distribution Payments, not higher. *Id.* at ¶8. The Objectors' use of the $69,705 share price is therefore arbitrary and unsupported by any factual evidence or the law on disgorgement.

C. The 2008-2009 Fraud Was No Worse Than The Fraud In Any Other Time Period

The Objectors' use of a different share price than the as of March 31, 2008 valuation date also would have the effect of creating a two-tiered system of Distribution Payments – one for selling shareholders in the first two time periods based on Stiefel Labs' ill-gotten gains, and another for the Objectors based on a damages award in a private lawsuit. The only justification the Objectors offer for this arbitrary standard is that the fraud committed on them was somehow worse or "more sinister" than the fraud the Defendants committed on other shareholders. Objections at 12.

The Objectors are wrong about this assertion for two reasons. First, they again conflate the allegations of the Complaint demonstrating the fraud that occurred with the allegations of the Complaint setting forth the Commission's remedy. There is no doubt the fraud the Defendants committed in late 2008 and early 2009 in failing to disclose to selling shareholders that they were attempting to sell Stiefel Labs was egregious, and the multiple paragraphs of the Complaint setting forth the details of that fraud make that clear. But alleging the fraud in detail does not determine what the remedy is for that fraud, and as discussed in the preceding section, the remedy is limited to disgorgement of the Defendants' ill-gotten gains.

Second, the detailed allegations of Complaint set forth in Section II.A belie the Objectors' claim that the fraud against them was worse. In fact, the fraud committed against all three groups of selling shareholders was egregious and followed an identical pattern – the Defendants undervalued Stiefel Labs shares and failed to update their valuations with significant later information showing the company's shares were undervalued. The Objectors do not articulate why that pattern was worse when it came to them.

In fact, as demonstrated by the Complaint's allegations and a letter the Commission received from William Carr, a shareholder who sold based on the as of March 31, 2007 valuation, the information the Defendants kept from those shareholders was also significant. *See* Letter of William Carr at 1-2 (the Commission, at Mr. Carr's request, is filing the letter simultaneously with this reply). In contrast to the Objectors' claims that the earlier-selling shareholders "were not enticed" to sell their shares to Stiefel Labs, the Complaint's allegations and Mr. Carr's letter demonstrate that is exactly what happened. Accordingly, the claim that the fraud in the later time period was worse is wrong, and does not justify departing from the Commission's equitable and evidence-based Distribution Plan.

Finally, the Objectors claim selling shareholders in the earlier time periods are somehow getting a windfall under the Commission's Distribution Plan. Objections at 13. This is untrue because all shareholders are receiving a *pro rata* distribution based on the same valuation methodology. Furthermore, one of the objectors, Wayne Hazelton, sold 19 shares in February 2009 and as a result is due a Distribution Payment of [redacted] under the Distribution Plan. But unlike many other shareholders who sold all their shares back to Stiefel Labs before the GSK acquisition, Mr. Hazelton only sold about one-quarter of his shares in

February 2009. He kept the remainder – [redacted] – and as a result received the higher share price GSK paid in July 2009. He received at least [redacted] for those shares. Although Mr. Hazelton is certainly entitled to the merger payment, it is illogical to describe other shareholders as receiving a windfall at Mr. Hazelton's expense under those circumstances.[8]

Another result of the objections would be to benefit the Objectors and other similarly-situated shareholders at the expense of the earlier-selling shareholders. The $37 million Fair Fund is a finite amount. Any order upholding the objections would result in a drastic reconfiguration of the amounts the different groups of selling shareholders would get from that $37 million. Rather than getting approximately 40 percent of the $37 million distribution, the as of March 31, 2008 selling Plan shareholders would get more than half of the total. Other groups would get significantly less. Rewriting the Distribution Payments in this fashion would turn a fair and reasonable Distribution Plan into an arbitrary and capricious one. In accordance with the law, the Court should deny the objections and approve the Commission's equitable and *pro rata* Distribution Plan. *J.P. Morgan*, 266 F. Supp. 3d at 231: "Courts have favored *pro rata* distribution of assets where, as here . . . victims were similarly situated with respect to their relationship with the defrauders."

D. The Commission Properly Excluded Attorneys' Fees And Costs From Distribution Payments

Objectors James Bacon and Denise Hulbert claim the Commission improperly classified them as Excluded Shareholders because the Distribution Plan failed to subtract attorneys' fees and

[8] Two other objectors settled private lawsuits against the Defendants several years ago and received significant payments as a result. We discuss their circumstances in the next section. In addition, the attorney for the four Objectors could receive several hundred thousand dollars in contingency fee payments from the Objectors if they succeed on both prongs of the objections. The Commission estimated this amount by determining the additional amounts the Objectors would get if they succeed on both their objections, and taking one-third of those amounts as the contingency fees the Objectors would pay the attorney – the same contingency fee the objections state he collected in the private lawsuits against Stiefel Labs.

costs from recoveries they obtained in private lawsuits more than five years ago. Both the factual and legal basis for this claim are wrong.

Inexplicably, the Objectors assert that "there does not appear to be any case law exactly on the point" when they know otherwise. As the Commission informed their lawyer in pre-filing conferrals, there is a federal statute *exactly* on point barring use of disgorgement funds to pay attorneys' fees that is dispositive of their claim. The language of the statute is set forth in Section 21(d)(4) of the Exchange Act, which provides:

> PROHIBITION OF ATTORNEYS' FEES PAID FROM COMMISSION DISGORGEMENT FUNDS.
>
> Except as otherwise ordered by the court upon motion by the Commission. . . funds disgorged as the result of an action brought by the Commission in Federal court … shall not be distributed as payment for attorneys' fees or expenses incurred by private parties seeking distribution of the disgorged funds.

This statute codified the federal policy "against using funds collected by SEC enforcement efforts to pay attorneys' fees . . ." *SEC v. Sterling & Foster Co.*, Case No. 97 Civ 1077, 2000 WL 697469 at *2 (S.D.N.Y. May 26, 2000) (denying request by attorneys to intervene in Commission enforcement action to have disgorged funds used to pay their fees for representing the defendants). *See also In re Ivan Boesky Sec. Litig.*, 888 F. Supp. 551, 558 (S.D.N.Y. 1995) (attorneys granted fees from funds collected through class litigation but denied fees from funds collected in Commission enforcement action).

The Exchange Act statute is dispositive because if the Court were to grant Bacon and Hulbert's objections, it could result in them receiving Distribution Payments that they would not otherwise receive. If this occurred, other shareholders' Distribution Payments would be reduced. In effect, other shareholders would be subsidizing the two Objectors' payment of attorneys' fees – which would violate the statute. Accordingly, the Court should deny this objection.

Furthermore, there is an additional reason to deny this objection. Even if the Court were to agree with the Objectors and subtract attorneys' fees and costs from their settlement payments in 2015, they still wound up receiving more than they would receive in Distribution Payments under the current Distribution Plan. The following table shows the result:

[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]

The table clearly shows the subtraction of attorneys' fees and costs from the two Objectors' recovery still results in them receiving more in their private lawsuit settlements than they would under the Distribution Plan – approximately [redacted] for Mr. Bacon and about [redacted].[9] The only way Mr. Bacon and Ms. Hulbert would receive more under the Distribution Plan is if the Court sustains the first objection, which it should not. The Court should therefore also deny this objection.[10]

IV. Conclusion

For all of the reasons set forth in this Reply, the Court should deny both objections and approve the Commission's Distribution Plan as is set forth in DE 240-1. As we indicated in the motion to approve the Distribution Plan, once the Court has ruled on the objections, the Commission will submit a proposed order approving the Distribution Plan.

[9] The Objectors' calculations of what they would receive under the Distribution Plan without including attorneys' fees and costs are wrong. Objections at 15-16. Furthermore, the Objectors fail to account for the fact that they received money more than five years ago, while other harmed shareholders received nothing and had no guarantee of receiving a Fair Fund distribution. The funds the Objectors received in 2015 are worth more today – another benefit of the settlements that other shareholders in the Distribution Plan did not get.

[10] The Objectors' claim that Mr. Bacon should receive funds because his private lawsuit was the basis for the Commission's claim is both irrelevant and wrong. The basis of the Commission's Complaint was the facts the Commission uncovered in its own investigation.

December 8, 2020

Respectfully submitted,

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on December 8, 2020, I electronically filed the foregoing document with the Clerk of the Court using CM/ECF.

s/Robert K. Levenson
Robert K. Levenson, Esq.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

EXHIBIT
A

SECURITIES AND EXCHANGE COMMISSION,	)
	)
Plaintiff,	)
v.	)
	)
STIEFEL LABORATORIES INC. and	)
CHARLES W. STIEFEL,	)
	)
Defendants.	)

Declaration of Marc J. Brown, CFA
November 30, 2020

1. I am a Managing Director with AlixPartners, a financial and operational consulting firm with more than 2,000 employees located in 23 offices worldwide, where I focus on providing valuation and other financial advisory services. I am AlixPartners' Valuation Services Practice Coordinator. I have more than 20 years of professional experience in financial analysis, with a primary focus on valuing private and public companies and related securities in a variety of contexts, including in connection with employee stock ownership plans. I have extensive experience in analyzing and valuing entities operating in the healthcare industry, including the pharmaceutical and life sciences sector.

2. I have been disclosed as the testifying valuation expert in this case and issued three expert reports.[1] I have reviewed the SEC's proposed Distribution Plan [DE240-1] and the Objections to the Distribution Plan filed by Normal Segall of Lubell & Rosen, LLC [DE 250] (the "Objections"). I was asked by the SEC to evaluate the Objections and determine whether the $69,705 value per share was the appropriate fair market value assuming that the objecting

[1] Defined terms not defined herein have been defined in the previously issued expert reports.

shareholders sold their individual shares on the date the shares were actually sold, which the objecting shareholders indicate was February 13, 2009 for the majority of the shares.[2]

3. As explained further below, the value per share of Stiefel Labs Plan shares as of February 13, 2009 was worth considerably less than $69,705 a share.

4. I understand that the $69,705 share price was derived based on the value of the transaction that ultimately occurred between Stiefel and GSK in April 2009. This transaction was a controlling transaction for the entire firm, meaning that a controlling stake was acquired. As discussed in my Affirmative Report dated April 11, 2019, which is attached hereto as Ex. A,[3] valuations stemming from transactions where control is conveyed need to be adjusted to arrive at the value that Plan participants would receive, given that the Plan participant's value would be on a minority basis.[4] As further discussed in my Affirmative Report, this is a standard adjustment to recognize that minority shares are generally worth less than controlling positions.[5] In my Affirmative Report, I adjusted the controlling equity value from the guideline transaction approach down by a 28.6% minority discount to adjust for the Plan participants' minority holding, in order to first arrive at the value per share on a marketable, minority basis as of March 31, 2006, 2007, and 2008.[6]

5. In addition to the need to adjust the Plan shares for lack of control, the Plan shares were also not actively traded. As such, these shares need to be further discounted for their lack of marketability. While the Defendants' valuation expert, Mr. Gougis, and I differed on the exact discount, the experts in this matter all agreed that a discount for lack of marketability was warranted. This lack of marketability that existed in February 2009, before a transaction was consummated, would further reduce the $69,705 value per share.

6. In addition, I understand that the objecting shareholders are specifically objecting to the Commission using the share price from the March 31, 2008 plan valuation date that I calculated as $40,600. This is the last annual plan valuation prior to the objectors' proposed February 13,

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[2] The Objections, page 7.
[3] My report adopted the previous report of Bruce Den Uyl of my firm, whom the Commission had retained but passed away during the litigation. The Objectors refer to Mr. Den Uyl's report in their Objections, which can be found at DE 145-15. The Objections, page 5 footnote 2. For purposes of this declaration, they are identical.
[4] Affirmative Report page 27.
[5] Affirmative Report page 27.
[6] Affirmative Report page 27.

2009 minority share sale date. In order for me to perform a valuation of the stock price as of February 13, 2009, I would need to consider the same valuation techniques that I used to value the stock as of March 31, 2008. It is my understanding that several of these financial and valuation metrics had decreased from March 31, 2008 through February 13, 2009. For example, during Stiefel's 2009 fiscal year, Stiefel's revenues and profits declined from the fiscal year 2008 that were reflected in the March 31, 2008 valuation. From fiscal year 2008 to fiscal year 2009, revenue declined from $912 million to $888 million and EBITDA declined from $161 million to $98 million, a decline of 2.7% and 41%, respectively.[7] All else equal, these declines in Stiefel's financial performance would lead to a lower valuation.

7. In addition, during this timeframe there were general declines in equity markets, including the public companies that I utilized in my March 31, 2008 valuation in my Affirmative Report. The enterprise value of the guideline public companies utilized in my Affirmative Report fell by an average of 28% from March 31, 2008 to February 13, 2009.[8]

8. The U.S. economy had also performed poorly between March 2008 and February 2009. According to the NBER, the economic recession known as the Great Recession was ongoing through all of fiscal year 2009.[9] Hence, the decrease in all these financial metrics indicate that, barring a synergistic, controlling transaction such as the GSK deal, the valuation of the objecting shareholders minority shares was worth considerably less than $69,705 a share and would have likely been worth less than the March 31, 2008 valuation of $40,600 per share.

9. In conclusion, the $40,600 share price the Commission used in its proposed Distribution Plan is much closer to the value of the Plan shares at issue when they were sold in February 2009 than the objectors' $69,705 share value.

[7] Affirmative Report, page 5.
[8] Source: CapitalIQ. Note: Average excludes Barrier Therapeutics which was acquired before February 2009 and was no longer publicly traded.
[9] https://www.nber.org/research/data/us-business-cycle-expansions-and-contractions

10. I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct.

Marc J Brown

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Marc J. Brown, CFA

Dated: November 30, 2020