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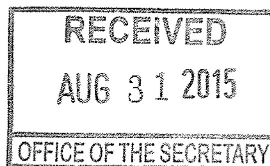

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-16293

In the Matter of

LAURIE BEBO, and
JOHN BUONO, CPA,

Respondents.

THE DIVISION OF ENFORCEMENT'S POST-HEARING REPLY BRIEF

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I. INTRODUCTION

Bebo's brief reads as if the hearing in this matter never occurred. Rather than accepting that her version of the events was uniformly refuted by every key witness, Bebo asks the Court to find she is telling the truth while everyone else – lawyers, accountants, and experienced executives – is lying. Bebo implores the Court to disregard the testimony of all the witnesses but her, to ignore the 35 instances where she was impeached, and to cast aside her best friend's testimony that she has credibility issues. In addition, Bebo wants the Court to believe a story that is internally inconsistent, facially nonsensical, and without support in the documentary record.

Given the overwhelming evidence against her, Bebo requires nearly 300 pages to attempt to legitimize her conduct. But the Court should reject Bebo's invitation to stretch the truth and ignore the extensive inculpatory record. Instead, the Court should accept the corroborating testimonial and documentary evidence showing Bebo orchestrated a multiyear scheme to cover-up ALC's covenant failures, falsely represented ALC's covenant compliance in its Commission filings, and repeatedly attempted to conceal her misconduct from Ventas, ALC's board, ALC's auditors, and ALC's shareholders. Applying these facts to established case law demonstrates that Bebo is liable for the charges alleged in the OIP, and that substantial sanctions are needed to punish Bebo, to protect investors from her, and to deter other executives from engaging in fraud.

II. BEBO'S VERSION OF THE FACTS DEMONSTRATES SHE IS NOT TELLING THE TRUTH

A. Bebo Accuses Nearly Every Percipient Witness Of Perjury.

Confronted by the testimony of every key witness who directly refuted Bebo's version of the events and the documentary record supporting those witnesses' testimony, Bebo asks the Court to believe her and to find everyone else is lying. However, unlike Bebo, these witnesses

had no motive to lie, let alone engage in a concerted effort to deceive.

Solari: Bebo first attacks the credibility of Solari, who testified that the covenants were not discussed on the January 20 call, that he never agreed to allow employees to be included in the covenant calculations, and that Bebo's version of the call was not true. (Tr. 416:8-15; 418:4-421:5, 423:13-426:6). While Bebo nonchalantly accuses Solari of perjury, she cannot answer the simple question: *Why would Solari lie?* Unlike Bebo, Solari had no motive to give false testimony. He faces no personal liability in this matter. He stopped working at Ventas in April 2009, during a mass layoff, and has no incentive to appease his former employer. (Tr. 399:23-400:12). And if Solari is somehow disgruntled from his layoff six years ago, there would be no reason for him, as Bebo claims, to lie by testifying, consistent with the other Ventas witnesses, that he was unaware of any proposal to include employees in the covenant calculations.

Buono: Bebo also claims Buono lied when he testified, consistent with Solari, that they did not discuss covenants on the January 20 call, and that Solari did not agree to anything. (Tr. 2344:18-2345:5). *But assuming Bebo's version of the January 20 call was accurate, why would Buono lie about it?* Indeed, if Solari truly agreed to everything Bebo claims he did, it would have been in Buono's self-interest to testify to that effect. Doing so would certainly have hindered the Division's case (against both Bebo and Buono). Buono's decision to settle to a securities fraud violation and substantial sanctions (Ex. 458) further demonstrates the lack of any agreement with Ventas or full disclosure to ALC's board.

To the extent Bebo claims Buono lied at the hearing but was truthful during the Division's investigation, the following statements made during Buono's pre-hearing proffer provide additional evidence of Bebo's fraudulent scheme:

- From "day one" Buono realized there was "not a good agreement" with Ventas.

- Regarding the quarterly certifications sent to Ventas, Buono "didn't think it was right from day one" and told Bebo he was worried Ventas could sue him for fraud.

- The statements in ALC's Forms 10-K and 10-Q that it complied with Ventas covenants were "not accurate"

- Buono "looked the other way" when he realized that people on Bebo's list of names weren't visiting the Ventas properties.

- Buono warned Bebo they could go to jail if ALC's SEC filings were incorrect.

- In response to Buono's concerns, Bebo responded: "I hear you, keep doing it."

(Ex. 482, pp. 12-13).

Further, Buono explained why inconsistencies may exist between his previous statements and his hearing testimony that the board was unaware of ALC's covenant practices: his earlier statements were based on false information given by Bebo – namely that she had told the board about ALC's covenant practices – and Buono did not realize Bebo lied to him until he reviewed the investigative testimony of the directors. (Tr. 2754:22-2755:4; 2784:14-2785:7).[1]

Bell, Buntain, and Rhinelander. Bebo claims that the three Canadian directors all lied when they testified they did not learn of ALC's use of employees in the covenant calculations before the March 6, 2012 CNG meeting. If Bebo is correct, *why would three prominent Canadian citizens, who were represented by sophisticated American attorneys, voluntarily travel to United States to commit perjury?* These directors have not been affiliated with ALC since it was purchased in 2013, and have no financial stake in this litigation. (Tr. 4514:20-4515:16). If Bebo is correct, and these directors knew the details of or were otherwise involved in Bebo's

[1] Bebo accuses the Division's attorneys of engaging in unprofessional conduct by purportedly allowing Buono to review all of the investigative transcripts except for Bebo's. (Resp. Br. at 6, n.4). This assertion is patently false. As the Division informed the Court, during the Wells process and again after this action was filed, Buono was afforded the same opportunity to review transcripts as was Bebo, which included the opportunity to review all of Bebo's investigative and arbitration testimony, as well all other transcripts in the Division's file. (Tr. 2502:2-25).

scheme, they could simply have stayed in Canada until the hearing in this matter had concluded.[2]

Roadman. Roadman, a retired three-star general and the former Surgeon General of the Air Force, testified consistently with the other directors that he was unaware of ALC's use of employees in the covenant calculations until March 2012. (Tr. 2558:2-22, 2592:16-2593:18). Again, assuming Bebo is correct and she fully apprised the board of her scheme, *why would Roadman risk his distinguished and unblemished reputation to give false testimony?*

Fonstad, Zak, and Davidson. Each of these experienced attorneys testified they never approved, or were made aware of prior to March 2012, ALC's inclusion of employees in the covenant calculations. (Tr. 1507:24-1512:17, 2292:4-2295:16, 4339:10-4340:16, 4344:6-4345:22). Fonstad and Zak, who attended board meetings, additionally corroborated the directors' testimony that the use of employees was not discussed at board meetings. (Tr. 1523:2-6, 4339:10-4340:16, 4344:6-4345:22). Bebo now claims each of these attorneys lied.[3] *But why would each attorney jeopardize their law license, let alone their liberty, to perjure themselves at the hearing?* Unlike Bebo and Buono, these attorneys did not sign or certify ALC's Commission's filings, or play any role in ALC's accounting function. Even accepting Bebo's allegations of perjury, it is hard to imagine what sort of liability these attorneys were trying to avoid through their allegedly false testimony.

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[2] The same could be said of Hennigar who, after the sale of ALC, voluntarily travelled to the United States to be deposed by Bebo's attorneys in her lawsuit against ALC, and testified consistently with the other directors that he was unaware of ALC's use of employees until March 2012. (Ex. 492A).

[3] Despite her current claims that she relied on Zak and Quarles, in her investigative testimony Bebo admitted she never discussed ALC's use of employees in the covenant calculations with Zak or any Quarles lawyer. (Tr. 2184:15-2185:17, 2187:16-2189:9, 2192:8-2193:1).

Herbner, Hokeness, and Ferreri. Bebo claims each of these CPAs provided false testimony at the hearing. Herbner expressly denied Bebo's claim that prior to the February 23, 2009 board meeting, Bebo discussed with Rhinelander (in Herbner's presence) the inclusion of employees in the covenant calculations. (Tr. 841:14-842:17). Bebo claims Hokeness lied when he corroborated the other witnesses that the use of employees in the covenant calculations was never discussed at board meetings. (Tr. 3134:21-3135:11). According to Bebo, Hokeness further lied by testifying he never distributed a draft memo about ALC's use of employees (Ex. 1129) to Buono and Fonstad. (Tr. 3052:5-11, 3122:22-3123:1).[4] Similarly, Ferreri rebutted Bebo's claims that he assured her he was comfortable with the employee-related journal entries and that she explained to him that the applicable criteria was whether employees had a "reason to go." (Tr. 1258:12-1259:3). *Again, why would each of these CPAs risk their licenses and careers to provide false testimony?* None of these ALC accountants were involved in the preparation of ALC's Commission filings; they had no incentive to perjure themselves.

Indeed, the only witnesses whose credibility Bebo does not challenge are her friends and family – her mother, Bucholtz, Zaffke, and Dengel – none of whom were present for Bebo's interactions with Ventas or ALC's attorneys, auditors, and board.[5] It is telling that Bebo cannot accept the testimony of a single percipient witness to the key events in this case.

B. Bebo's Story Is Inconsistent, Incredible, And Defies Common Sense.

Despite the consistent testimony of the percipient witnesses and the documentary record, Bebo asks the Court to ignore all that evidence and believe her instead. Even disregarding the

[4] Both Fonstad and Buono testified they never received Hokeness's memo, in draft form or otherwise. (Tr. 1512:8-11, 2358:4-9).

[5] Of these witnesses, only Bucholtz testified during the Division's investigation. At the hearing, Bucholtz was repeatedly impeached during her brief cross-examination. (*See, e.g.*, Tr. 2980:20-2982:2, 2986:11-2987:11, 3013:16-3014:15, 3020:9-3022:6, 3022:7-3023:7, 3023:8-3024:4).

fact Bebo was impeached 35 times, and the testimony of her best friend, Bucholtz, that Bebo has credibility issues (Tr. 3016:3-3017:23), Bebo's story makes no sense.

1. Why Would Ventas Agree To Effectively Waive The Covenants For Free?

A prime example of Bebo's story being nonsensical is her claim that Ventas, including the executives above Solari, effectively agreed to waive the covenants, *for no consideration*, by allowing ALC to include an unlimited number of non-residents with a "reason to go" in the covenant calculations. What's more, Bebo claims Ventas agreed ALC could include people who never stayed at the Ventas facilities, and that Ventas did not even want to know the numbers of non-residents ALC was including. (Tr. 1904:22-1907:13, 1912:7-1913:16, 1945:11-1946:4, 4005:2-5). But Bebo cannot explain why, for nothing in return, Ventas would agree to an arrangement that would preclude it from ascertaining true occupancy and revenue at its facilities.

The absurdity of Bebo's story of Ventas's "agreement" is demonstrated by what happened the following month, February 2009, when ALC attempted to obtain covenant relief by purchasing two New Mexico properties from Ventas. In response to ALC's New Mexico proposal, Ventas was willing to waive only a single covenant (for individual facility coverage ratio), yet demanded ALC pay an increased price for the New Mexico facilities, and also purchase the poorly performing Peachtree property. (Ex. 196). Ventas's demands for the *temporary suspension of only a single covenant* were so steep that Bebo would not accept Ventas's terms. (Exs. 195, 198). Given Bebo's knowledge that Ventas required substantial consideration to suspend only a single covenant, it defies reason that she believed Ventas, only one month earlier, agreed to effectively waive all covenants, for nothing in return.

2. Why Did Ventas Expend So Much Effort If It Didn't Care About The Covenants?

Another aspect of Bebo's story that defies belief is her claim that Ventas did not care

about ALC's compliance with the financial covenants. Bebo attempts to establish Ventas's ambivalence by claiming Ventas did nothing after ALC received a 2009 Alabama regulatory notice. (Ex. 2149). Yet Bebo concedes Ventas took action against ALC, by issuing a notice of default, and that Ventas and ALC resolved their dispute after ALC quickly cured the regulatory inquiries. (Resp. Br. at 63-64). On the other hand, Bebo admittedly never told Ventas that ALC would breach the covenants without using employees. (Tr. 1920:11-16).[6]

According to Bebo, the Ventas lease was ambiguous and not tailored for assisted living facilities. She claims Ventas thus gave ALC free reign to meet the covenants by manipulating its occupancy and revenue information, or to simply disregard the covenants altogether. But Bebo does not dispute that the lease required ALC to provide detailed financial and covenant data to Ventas each quarter, and that ALC routinely endeavored to meet these requirements through the preparation of the officer's certificate packages. (Exs. 32-45).[7] The attention Ventas paid to this information – and ALC's covenant compliance – is demonstrated by the detailed covenant analysis and signoff materials Ventas prepared following receipt of the officers certificates (Exs. 46-60), and the focused questions about occupancy Ventas asked during its quarterly discussions with Bebo and Buono. (Exs. 144, 147, 207, 208, 215, 217, 240, 241, 279, 300, 301).

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[6] Bebo disingenuously cites to ambiguous portions of Doman's testimony, in order to support the proposition that Ventas allowed ALC to breach the financial covenants early in the ALC-Ventas relationship. (Resp. Br. at 65). To be clear, Doman testified that he learned ALC breached the covenants sometime between 2008 and 2012, and that he learned of this only after Bebo asked for a release in the course of Ventas's 2012 lawsuit. (Tr. 281:12-282:1). Moreover, there is zero evidence in ALC or Ventas's covenant compliance materials, or elsewhere, documenting that ALC ever disclosed to Ventas that it breached any of the financial covenants.

[7] Bebo attempts to justify her repeated attempts to hide true occupancy from Ventas as a means to prevent Ventas from learning competitive information. If Ventas was truly a competitor of ALC, or if Bebo really believed that its occupancy and revenue information was proprietary, *why would she sign a lease requiring ALC to provide this information to Ventas on a quarterly basis?*

Moreover, Ventas was prepared to evict ALC in the event of noncompliance with the covenants and replace ALC with another operating company. (Tr. 185:18-187:6). Solari recognized this and, in 2010, emailed his former colleagues at Ventas, and offered to have his current employer replace ALC should Ventas need a new operator for the facilities. (Tr. 438:25-440:3; Ex. 258, p. 2).

3. Why Didn't ALC Utilize The Alternative Covenant Methodologies Bebo Claims Were Available?

Bebo's claims that she believed ALC could comply with the covenants by using alternative methodologies cannot be squared with reality. As discussed in the Division's opening brief, besides Bebo's self-serving testimony, there is no evidence that anyone contemplated using an alternative methodology to avoid covenant defaults, and using alternative methodologies would still result in significant covenant violations. (Div. Br. at 18-19).

Moreover, if Bebo truly believed ALC could meet the covenants using alternative methodologies:

- Why didn't ALC change methodologies when it first experienced covenant problems?
- Why would Bebo even need to ask Solari for an agreement to include employees?
- Why would, as Bebo testified, Fonstad be so excited by Solari's agreement that he reached over Bebo's desk to give her a high-five? (Tr. 4011:1-4)
- Why would ALC attempt to seek covenant relief in February 2009 by purchasing buildings in New Mexico or making other concessions to Ventas?
- Why would ALC devote significant accounting staff resources to the preparation of the Occupancy Recons, especially when all of ALC's accounting personnel were uncomfortable with the process?
- Why, as Bebo concedes, didn't ALC propose alternative methodologies to the board, including in the October 27, 2008 memo to the board outlining ALC's strategies to address declining occupancy at the Ventas facilities? (Tr. 1872:7-21; Ex. 150).
- Why, according to Bebo, did she tell Rhinelander in February 2009 that ALC had two

options for addressing covenant issues (using employees or negotiating with Ventas), if the easiest option would be to just change methodologies? (Tr. 1961:16-1962:12).

The simple answer to these questions is, as various witnesses testified, ALC never contemplated using an alternative methodology to meet the covenants. (Tr. 1304:24-1305:20, 1521:18-1522:3, 2314:14-2315:8, 2813:4-20).

Further, changing the methodologies as Bebo suggested would not have avoided covenant defaults, for either occupancy or coverage ratio. (*See* Div. Br. at 18-19). In her brief, Bebo claims CaraVita used a different methodology – occupied beds over units – to calculate occupancy, and that doing so allowed CaraVita to achieve occupancy between 6% and 12% higher than would have resulted from ALC's "units over units" methodology. (Resp. Br. at 51-52). However, even these gains would not have avoided covenant defaults, as ALC's occupancy shortfalls were so severe that even a 10% increase in occupancy would have resulted in over 40 covenant failures during the relevant time period. (Tr. 4567:24-4569:8; Ex. 583A).

Similarly, any change in the occupancy methodology, or in coverage ratio methodology permitted under the lease, would not have allowed ALC to avoid *coverage ratio* defaults. (Tr. 1870:16-1871:1, 1873:20-1874:4, 2315:9-2317:3). Buono acknowledged, *in an email to Ventas*, that altering ALC's allocation of expenses would not affect the coverage ratio, writing: "How we do things internally *is irrelevant to the equation*…If we were doing anything inconsistent…you would have seen a dramatic improvement in the ratios (which you don't)." (Ex. 1994 (emphasis added)).[8]

4. Why Didn't Bebo Document Her Purported Agreement With Ventas?

Another nonsensical aspect of Bebo's story is her claim that various Ventas executives

[8] It is telling Bebo claims to be ignorant of GAAP and other financial matters, yet argues that Buono is incorrect in testifying that manipulating the coverage ratio would have violated GAAP.

learned of Solari's purported covenant agreement simply by reviewing Bebo's February 4, 2009 email. But that email says nothing about the covenants, and merely references, buried in a paragraph near the end, the "rental of rooms to employees." (Ex. 184). While Bebo tries to emphasize Buono's testimony that *Buono* thought the only reason for employees to rent rooms was to meet the covenants, there is no evidence Ventas shared this understanding. Rather, as Bebo admits, she told Solari that ALC was sending employees to the Ventas properties to assist with the operations of the properties, but she never told Solari that ALC would fail the covenants without the use of employees. (Tr. 1920:14-17, 4003:6-15).

Bebo also admits that, at the time of her January 2009 call with Solari, ALC was sending a "taskforce" of employees to the Ventas facilities in a real effort to address poor occupancy. (Ex. 97, p. 4; Ex. 150, p. 4; Ex. 567). Various witnesses testified that in discussions about the taskforce, Bebo did not say that the taskforce's purpose was to treat its members as "occupants" for covenant compliance. (Tr. 560:3-9, 2645:3-25, 2813:21-25).[9] Thus, there is no reason to believe Ventas would have divined from Bebo's February 4, 2009 email that ALC intended to use the employees it was sending to the Ventas facilities to meet the covenants.

Moreover, if Ventas actually agreed to include employees in the covenant calculations, then Bebo should have been comfortable expressly documenting that agreement. Indeed, if an agreement truly existed:

- Why didn't Bebo send Solari the template letter recommended by Fonstad, or follow Fonstad's advice to obtain a signed confirmation from Ventas? (Ex. 1152, p. 2).

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[9] Throughout her brief, just as she did at the hearing, Bebo continues to conflate (a) ALC's practice of sending the taskforce employees to stay at the Ventas facilities with (b) ALC's inclusion of such employees in the covenant calculations. Despite the critical distinction between the two practices, Bebo insists on referring to both practices as "employee leasing." When Bebo used the vague and misleading term "employee leasing" during the relevant time period, it appears she did so in an effort to conceal ALC's true covenant practices.

- Why didn't Bebo's February 4, 2009 email to Solari mention the covenants or the purported agreement to use the "reason to go" standard? (Ex. 184).

- Why, as Bebo admits, did she never disclose the use of employees to Ventas following the January 20, 2009 call with Solari? (Tr. 4074:6-9).

- Why did Bebo fail to reference the agreement, or ALC's use of employees, in any document (such as board books, minutes, or emails) shared with ALC's directors?

- In the board book and PowerPoint pages documenting ALC's compliance with the covenants, why didn't Bebo simply disclose the number of actual occupants and the added number of employees needed to ensure compliance?[10]

- Why did Bebo admittedly never tell the board that: (a) ALC would fail the covenants without including employees, (b) ALC was including her family and friends, or (c) ALC was including large numbers of employees who did not visit the Ventas facilities? (Tr. 2035:11-25).

C. Bebo's Actions And Admissions Prove She Knew No Agreement Existed.

The reason Bebo never documented any agreement to include employees in the covenant calculation is – as Solari and Buono testified – no agreement ever existed. The following documentary evidence and admissions by Bebo demonstrate that she knew Ventas was unaware of ALC's use of employees in the covenant calculations:

- Bebo admittedly instructed Herbner not to disclose to Ventas ALC's use of employees in the covenant calculations. (Tr. 2088:11-2089:25).

- In response to an inquiry from Ventas to explain occupancy changes, Bebo admittedly provided answers that did not reference the true reason for the changes: ALC's use of employees. (Tr. 2090:22-2092:12; Ex. 212).

- Bebo's admitted attempts to prevent Ventas and Grant Thornton from visiting the Ventas facilities. (Exs. 220, 223, 262)

[10] Bebo reiterates that in certain quarters, the board received presentations which, if scrutinized carefully in their entirety, could show a discrepancy between actual occupancy and the occupancy reported to Ventas. (Resp. Br. at 129-132). For these quarters, the presentations make no reference to a discrepancy existing or that the reason for the discrepancy was the inclusion of employees. (*See, e.g.,* Exs. 81, 82). The directors testified that no one brought to their attention any inconsistencies in board materials, and if any discrepancy existed, it was management's responsibility to alert the board. (Tr. 742:9-19, 1370:12-1371:3, 2642:8-2643:8).

- Bebo's admitted concern that, in the course of ALC's sale process, Ventas would discover that actual occupancy was lower than what ALC reported in the quarterly financial materials. (Tr. 2120:9-2123:8, 2126:9-22; Ex. 292).

- Bebo's instructions to ALC's investment bank not to disclose to Ventas actual occupancy data at the Ventas facilities. (Exs. 287, 292).

- Bebo's admitted belief in 2012 that neither ALC's buyer nor Ventas would credit her purported agreement with Solari. (Tr. 2128:13-2131:10, 2132:13-2134:8).

- Bebo's efforts to reject Bell's March 2012 advice to disclose the 997 account to ALC's potential buyers. (Tr. 595:6-597:21, 2207:12-25, 2209:4-22; Exs. 325, 326).

- Bebo's attempts in April 2012 to edit a letter to Ventas to remove references to ALC's use of employees in the covenant calculations, and her email recognizing that keeping the references in the letter would "create other disagreements" with Ventas. (Tr. 4721:6-4723:10, Ex. 568, p. 4; Ex. 570).

- Bebo's attempts, after Ventas sued ALC, to withhold from any settlement documents the reference to employees being included in the covenant calculations. (Tr. 611:15-613:22, 2846:3-2848:4; Ex. 351).

Bebo's words and actions simply cannot be reconciled with the notion that she believed Ventas was aware of ALC's use of employees in the covenant calculations.

D. Bebo's Account Of Key Events Is Refuted By Multiple Witnesses.

Further demonstrating that Bebo's story should not be believed is the fact that for each of the key events in her narrative, she is disputed by the other witnesses.

1. The January 20, 2009 Solari Call And Its Aftermath

Each witness Bebo claims participated in her January 20, 2009 call with Solari denies Bebo's version of the events. Both Solari and Buono testified there was no discussion of the covenants and Ventas didn't agree to anything. (*See* Div. Br. at 12-13). Similarly, Fonstad disputed Bebo's claim that he was on the call, and Fonstad's notes do not show him

participating. (Tr. 1504:25-1505:15, 1516:12-19).[11]

Buono and Fonstad likewise deny Bebo's account of what transpired immediately after the call. Bebo testified that, after hanging up with Solari, Buono and Fonstad confirmed Solari had agreed ALC could meet the covenants using an unlimited number of rooms that ALC would lease for its employees who had a "reason to go" to the Ventas facilities, even if the employees never visited the properties. (Tr. 1924:14-1925:16, 1926:16-1927:11, 1928:22-1929:17). Bebo contends Fonstad was so excited he reached across her desk and gave her a "high-five." (Tr. 4010:3-4011:4). Bebo also testified Fonstad retracted his advice from the day before that Ventas's written confirmation was required, yet cannot explain what caused Fonstad's supposed change of heart. (Tr. 1929:18-22).[12]

Refuting Bebo, Fonstad and Buono both deny Bebo discussed Solari's purported agreement with Fonstad, or that Fonstad otherwise approved any practice following the January 20, 2009 call.[13] (Tr. 1507:24-1511:16, 1518:10-1519:1, 2318:16-19, 2321:21-2352:4).

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[11] Even if Fonstad was on the call, that would not absolve Bebo of liability. There was no discussion of the covenants on the call, nor were the covenants mentioned in the emails Fonstad received which purported to summarize the call. (Ex. 1171). As discussed below, Fonstad's alleged attendance on the Solari call and receipt of Bebo's email is far short of the required full disclosure necessary to invoke a reliance on counsel defense.

[12] Incredibly, Bebo also claims Fonstad later approved listing employees and family members at multiple properties at the same time, and also advised that ALC's statements in its Commission filings that it complied with the covenants were appropriate in light of the inclusion of employees. (Tr. 1928:1-21, 1929:23-1930:19). Bebo even testified Fonstad approved Bucholtz's seven-year old nephew for the covenant calculations, which Fonstad denied and was inconsistent with Bebo's investigative testimony. (Tr. 1318:17-20, 2050:8-12; 2194:3-24).

[13] Bebo repeatedly claims Buono said that Fonstad advised that the use of employees in the covenant calculations was "Kosher." Yet Buono did not testify to that effect at the hearing, and Bebo misinterprets Buono's investigative testimony on the subject, which took place prior to ALC's privilege waiver and the Division's ability to question Buono on his communications with Fonstad. (Tr. 4651:22-4653:1).

2. The February 23, 2009 Board Meeting

Herbner, Rhinelander, and Hennigar dispute Bebo's account of what occurred prior to the February 23, 2009 board meeting. Bebo testified that before the meeting started, in the presence of Herbner and Buono, she proposed to Rhinelander using employees in the covenant calculations. (Tr. 1958:16-1966:20). Bebo testified she told Rhinelander ALC would be challenged meeting the covenants, and that ALC had two options: (1) negotiate covenant relief with Ventas; or (2) *per Ventas's agreement*, include employees in the covenant calculations.[14] (Tr. 1959:1-1965:5). According to Bebo, Rhinelander then spoke with Hennigar, returned to Bebo's office and told Bebo, Buono, and Herbner that Hennigar preferred the option of including employees. (Tr. 1965:6-1966:20).

Herbner, Rhinelander, and Hennigar refute Bebo's story. (Tr. 841:14-842:17, 2823:14-2824:12; Ex. 492A). Herbner testified she was never in a meeting with Rhinelander where the covenants were discussed. (Tr. 841:14-842:17). Rhinelander denied Bebo's story and testified he had never even met Herbner. (Tr. 2822:14-2824:12). Hennigar testified that prior to the March 2012 CNG meeting, he never discussed with anyone, including Rhinelander, ALC's use of employees to meet the covenants. (Ex. 492A, at 55:21-56:19).

Buono testified about a meeting in December 2008 involving the same participants. According to Buono, Rhinelander said something to the effect of "if the lease doesn't say you can't include employees, let's include employees" and told Bebo proceed with the "employee leasing program." (Tr. 2393:20-2396:6).[15] Buono testified the meeting took place while ALC

[14] Bebo admits, at this meeting, she did not raise the option of meeting the covenants by changing ALC's occupancy or coverage ratio methodologies. (Tr. 4550:3-4551:14, 4580:13-4582:15).

[15] Bebo admits that employees staying at the Ventas facilities implicated the "affiliate transaction" section of the lease (Section 8.1.3), and that she consulted Fonstad on whether the

was contemplating sending the employee taskforce to the Ventas facilities to improve occupancy. (Tr. 2759:21-2760:10). Buono further testified, and Bebo admits, in February 2009 Bebo had not yet determined to include large numbers of employees, or employees who did not stay at the properties, in the covenant calculations. (Tr. 1989:2-1990:7, 2760:11-2761:7). Accordingly, even accepting Bebo's testimony regarding the morning of February 23, 2009, Rhinelander and Hennigar did not approve Bebo's scheme to meet the covenants using large numbers of non-residents who did not stay at the Ventas facilities. Moreover, crediting Bebo's claims that she told Rhinelander and Hennigar that Ventas agreed to the use of employees merely proves she lied to them, since there never was an agreement.

As for the actual February 23, 2009 board meeting, eight witnesses – Bell, Buono, Buntain, Fonstad, Hennigar, Hokeness, Rhinelander, and Roadman – refute Bebo's testimony that the board approved the practice of including employees in the covenant calculations. (Tr. 563:24-564:6, 567:4-23, 1521:22-1524:2, 1363:10-25, 2646:15-2648:8, 2761:19-23, 2816:3-14, 2824:13-22, 3134:21-3135:11; Ex. 492A). The minutes of that board meeting likewise make no mention of the board approving any such practice. (Exs. 99, 100).

3. The Third Quarter 2009 Board Meeting

Bebo testified that at the third quarter 2009 meeting, she fully disclosed the details of her scheme to ALC's board. According to Bebo, at that meeting she disclosed ALC's use of: (a) large numbers of employees to meet the covenants; (b) employees who did not visit the Ventas properties; (c) non-employees; (d) the same employee at multiple properties; and (e) the 997 account to cancel the employee revenue reported to Ventas. (Tr. 2023:18-2024:25, 2025:11-

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lease allowed ALC employees to stay at the facilities, regardless of whether they were included in the covenant calculations. (Resp. Br. at 83; Ex., 1152).

2026:15, 2027:11-2028:10, 2030:7-23, 2031:1-14).

Five directors, plus Buono, Fonstad, and Hokeness, deny Bebo made these disclosures at the Q3 2009 board meeting. (Tr. 563:24-564:6, 567:4-23, 1521:22-1524:2, 1363:10-25, 2646:15-2648:8, 2761:19-23, 2816:3-14, 2824:13-22, 3134:21-3135:11; Ex. 492A). Similarly, the minutes and board materials for that meeting – which Bebo reviewed and approved – make no reference to ALC's use of employees, let alone the detailed disclosures Bebo claims she provided. (Exs. 81, 105, 106).

Bebo claims that at this board meeting, Buntain directed management to include more employees to avoid the appearance that ALC was barely meeting certain covenants. (Tr. 2037:13-2038:17). Buntain, however, explained that in 2009 he did not know ALC was including employees in the covenant calculations, and was suggesting that ALC attempt to get more residents into the properties to raise the occupancy rates. (Tr. 1372:13-1373:10, 1416:3-1417:19).[16] Bell, Buono, Fonstad and Rhinelander each denied that Buntain ever gave a directive that ALC should increase the number of employees included in the covenant calculations. (Tr. 571:10-15, 1521:6-12, 2765:24-2767:1, 2816:15-2817:17).[17]

Given the uniform testimony of the directors and other witnesses that the board was unaware of the use of employees in the covenant calculations, the most likely explanation of Buntain's comment at the Q3 2009 meeting was that he was suggesting that ALC redouble its

[16] Buntain further testified that in March 2012, after Buono disclosed the use of employees in the covenant calculations, Buntain made a "tongue in cheek" comment about adding employees that was meant to convey Buntain's frustration and anger over the issue. (Tr. 1377:11-1379:1).

[17] Rhinelander testified that Buntain made a sarcastic comment about employees at the Ventas facilities in the fall of 2011. (Tr. 2818:1-19, 2871:1-5). Buono likewise testified that at some point Buntain made a similar sarcastic comment. (Tr. 2392:13-2393:19). Both witnesses testified that they did not believe Buntain was making an actual recommendation to use employees for covenant compliance. (Tr. 2765:24-2767:1, 2816:15-2817:17).

efforts to address declining occupancy at the Ventas facilities. This is consistent with Bebo's statements to the board that ALC was sending a taskforce of employees to the Ventas facilities in order to improve occupancy. In fact, Q3 2009 was the height of the taskforce's utilization, as ALC sent the most employees, approximately 28, to the Ventas facilities during that quarter. (Resp. Br. at 107-108; Ex. 3507).

4. The Second Quarter 2011 Board Meeting

Bebo testified that at the Q2 2011 board meeting, she told the directors and Grant Thornton the same extensive details about the use of employees in the covenant calculations that she claims to have disclosed in Q3 2009. (Tr. 2167:13-2170:12, 4702:19-4703:12). This directly conflicts with Bebo's investigative testimony, in which she testified that she did not discuss ALC's use of employees with the board between the Q3 2009 board meeting and the March 2012 CNG meeting. (Tr. 2040:20-2042:14).

Again, five directors, as well as Buono, Zak, and Hokeness, denied Bebo discussed ALC's use of employees during the Q2 2011 board meeting. (Tr. 567:4-571:15, 1363:10-1366:16, 2382:12-2383:19, 2384:25-2388:3, 2645:11-2646:11, 2648:22-2651:7, 2825:2-2827:17, 3134:21-3135:11, 4339:10-4340:16, 4344:6-4345:22; Ex. 492A). The testimony of these witnesses is consistent with minutes and board books for the Q2 2011 board meeting, as well as Zak's handwritten notes of that meeting, none of which reference ALC's use of employees in the covenant calculations. (Exs. 86, 115, 116, 118).

Bebo's claim that she disclosed the specifics of her scheme in the context of the board's discussion of the SEC comment letter (Resp. Br. at 126-127), is further refuted by Bebo's own

notes from that meeting. (Ex. 571).[18] Despite Bebo's claim that she took copious notes in her board books, the draft response to the SEC's comment letter included in Bebo's board book makes no reference to ALC's use of employees. (Tr. 4706:12-4711:24; Ex. 571, pp. 31-32).

While Buono testified that at the Q2 2011 board meeting he (not Bebo) made a single reference to employees and the covenant calculations, he was explicit that no specifics were given regarding the practice. (Tr. 2382:12-2383:19, 2384:25-2388:3, 4631:7-4632:20). Buono further testified this was the first such reference made at any board meeting. (Tr. 2382:12-16). At minimum, if the Court credits this testimony, it shows the board was entirely unaware of any aspect of Bebo's scheme for the first two and a half years of its existence.

Bebo disingenuously asserts that Buntain testified that in the context of the board's review of the response to the SEC comment letter, there was a discussion of ALC's use of employees. (Resp. Br. at 127-128 (citing Tr. 1452-54)). Indeed, on the very next transcript page following Bebo's citation to Buntain's testimony, Buntain makes clear there was no discussion of employees being used in the covenant calculations during the board's review of the SEC comment letter, or at any other time prior to March 2012. (Tr. 1454:7-1455:9).

E. Grant Thornton Did Not Disclose ALC's Covenant Practices To The Board.

Koeppel's and Robinson's testimony that they discussed ALC's use of employees at audit committee meetings is refuted by the minutes of those meetings, Grant Thornton's agendas and reports contained in the board materials, and the testimony of every other witness, save Bebo, who attended those meetings. (Exs. 74-90, 92-120).

Grant Thornton's unsuccessful attempts to find evidence of disclosure to the board prove

[18] Exhibit 571 is a copy of the board materials for the Q2 2011 meetings. Bebo's name is written on the first page of the exhibit, and Bebo concedes that these board materials contain her handwriting. (Tr. 4706:12-4711:24; Ex. 571, pp. 31-32).

that Koeppel and Robinson are wrong. Specifically, in April 2012, after ALC's board learned about the inclusion of employees and confronted Grant Thornton, Robinson emailed his subordinate, Henselin, and asked if she was "able to find any documentation that we discussed the issue of employee occupancy with the board." (Ex. 1744). In response, Henselin wrote that she could only find evidence of a *single occasion* where Grant Thornton discussed the issue with the board: Grant Thornton's presentation for the Q3 2010 audit committee meeting, which preceded Robinson joining the ALC engagement.[19] (*Id.;* Ex. 1744A, p. 4). However, the presentation that Henselin attached to her email as "documentation" referenced the "Caravita covenants" and "Minimum average occupancy," but made no mention of ALC's use of employees. (Ex. 1744A, p. 4). Grant Thornton's inability to document that it discussed the use of employees with ALC's board prior to April 2012 supports the testimony of the ALC board meeting attendees who agreed that no such discussion occurred.

In addition to Grant Thornton's inability to evidence the disclosure of ALC's use of employees to the board, Koeppel and Robinson concede they never told the directors the number of employees being included in the covenant calculations or that ALC would fail the calculations without the use of employees. (Tr. 3368:18-24, 3514:9-17, 3519:6-22). Further, Bebo testified that she never told Koeppel, *who could not have informed the board during 2009 or 2010*, that ALC was including in the covenant calculations: (a) employees who did not actually visit the Ventas properties; (b) non-employees; or (c) Bebo's friends and family. (Tr. 2150:4-18, 2150:25-2151:15, 2151:22-2154:16).

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[19] Henselin's email also referenced a discussion with Ng, outside the presence of the other directors, in advance of the Q1 2011 meeting. (Tr. 3514:24-3516:10; Ex. 1744B). But the agenda for that meeting with Ng merely references the "Caravita covenants," and makes no reference to employees. (Ex. 1744B). Robinson conceded that the minutes of the Q1 2011 board meetings make no reference to ALC's use of employees, and that Henselin could not provide Robinson with documentation that the practice was discussed. (Tr. 3520:5-3521:1).

F. Milbank's Investigation Was Limited In Scope And Did Not Exonerate Bebo.

Bebo continues her refrain that Milbank's investigation vindicated her conduct. However, as demonstrated by Milbank's report to the board, Bebo was in no way exonerated. Moreover, because Milbank did not interview important witnesses – particularly Solari, anyone from Grant Thornton, and certain directors – Milbank could not obtain key evidence to refute Bebo's story. (Tr. 626:24-627:18, 2654:10-12; Ex. 558, pp. 1, 6; Ex. 1873, p. 4). Nevertheless, even with its inquiry limited to ALC personnel, Milbank made the following findings and conclusions discrediting Bebo's version of the events:

- No documents had been lost or erased. (Tr. 627:19-628:7; Ex. 558, p. 1).
- Grant Thornton "never confirmed that the employees on the list actually worked at the facilities or even attended the facilities at the relevant time." (Ex. 558, p. 2).
- Bebo told Milbank that the board had approved the use of an "internal allocation" to meet the covenants, yet no board member had any recollection of Bebo using that terminology. (Ex. 558, p. 3).
- Fonstad advised Bebo that ALC could not enter into the "employee arrangement" unless Ventas sent a "written confirmation agreement." (*Id.*, p. 4; Tr. 633:14-634:1).
- Bebo's February 4, 2009 email to Ventas did not incorporate Fonstad's advice or disclose the use of employees to meet the covenants. (Ex. 558, p. 5).
- "Bebo said she got to a bottom line income number and then established the employee list." (*Id.*).
- "Bebo did not tell Solari that the employee leasing arrangement would be used for purposes of covenant compliance or that ALC was close to violating the covenant." (Tr. 636:12-17; Ex. 558, p. 6).
- "Bebo decided herself all the names of the employees and their relatives who would go on the list of persons. She said that they were people who 'could of, would have, should have' [been] in the position to go to the facilities." (Tr. 637:2-7; Ex. 558, p. 6).
- "A list of all employees went to Grant Thornton but never went to Ventas and never went to the board." (Ex. 558, p. 6).

- "The materials provided to the board on a quarterly basis discussed the compliance with the CaraVita covenants and always showed compliance." (*Id.*, p. 8).

- "The board never knew the employees were needed for purposes of compliance with the Ventas lease covenants…The board believed the number of employees were small." (*Id.*, p. 8).

- "GT wanted to talk to Ventas. Bebo said, no, GT can't talk to Ventas." (*Id.*, p. 9).

- "Ventas…only came to realize the issue of the employee leasing arrangements when it saw in an ALC draft purchase agreement a release in respect of the leasing matters." (*Id.*, p. 10).

- "The corporate employees in 2009 were a very small number; however, the employees grew to over 100, and the employees at the end of the arrangement were not going to the properties. They were a paper entry." (*Id.*, p. 11).

- While Milbank "can't disprove" Bebo's claim that Ventas approved the use of employees, Milbank recognized that the problem with its analysis is that Bebo's February 4, 2009 email did not disclose that employees would be used for covenant compliance or that ALC would be in "default" under the lease without the use of employees. (Tr. 643:21-645:3; Ex. 558, p. 10).

While Bebo stresses that Milbank did not recommend any corrective action, given that she had already been terminated by the company, the most logical corrective action for ALC to take was no longer necessary. (Tr. 745:19-746:2, 2655:4-10).

G. Only A Limited Number of Employees Stayed At The Ventas Facilities.

Bebo's fraud is also demonstrated by the fact that most "employees" she included in the covenant calculations never stayed at the Ventas facilities. Based on Bebo's analysis of the travel records, the number of "visits" to the Ventas facilities peaked at 78 to 88 in Q3 and Q4 2009, and thereafter fluctuated between 18 and 57 "visits." (Resp. Br. at 108 (citing Ex. 3507). These are very modest numbers, given that from Q3 2009 onwards, ALC listed between 61 and 103 rooms as occupied by employees for every day of each quarter.[20] (Ex. 377, ¶ 80).

[20] Presumably, when an employee did stay overnight at a Ventas facility, the employee typically stayed for far less than the 91 days in that particular quarter.

Moreover, the following analysis of Exhibit 3507 shows that the actual numbers of *employees* travelling to the Ventas facilities in any given quarter was much smaller than the cumulative number of "visits" purportedly documented in the exhibit. Thus, ALC still failed the covenants by wide margins, even assuming (a) the employees listed on Exhibit 3507 actually stayed at the Ventas facilities for *every day of each quarter*, and (b) that ALC was allowed to include these employees in the calculations. (Ex. 377, ¶ 83). Further, of the limited number of employees listed in Exhibit 3507, seven (Abel, Bell, Brake, Hamm/Vadakin, Houck, Parker, and Schug) testified they never spent the night at any of the Ventas facilities, and instead stayed at hotels. (Tr. 1468:18-1469:1; Exs. 451, 452, 454, 462, 470, 473).[21]

	Number of "Visits" to the Ventas Facilities per Bebo's Brief (p. 108)	**Number of Employees Listed on Exhibit 3507**	**Number of Employees Listed on Exhibit 3507 Who Stayed at the Facilities and Not at Hotels**
Q1 2009	53	21	17
Q2 2009	59	20	16
Q3 2009	88	27	21
Q4 2009	78	28	24
Q1 2010	41	22	20
Q2 2010	57	19	16
Q3 2010	18	14	11
Q4 2010	18	11	10
Q1 2011	27	12	10
Q2 2011	34	17	13
Q3 2011	25	13	10
Q4 2011	45	14	10

In the course of its investigation, Milbank reviewed the same records supporting Exhibit 3507 and reached a similar conclusion: "there were rarely more than three ALC employees who actually travelled to the Ventas-leased facilities in any month, and those employees remained only for a few days." (Ex. 365, p. 25).

[21] Bucholtz, who is listed on Exhibit 3507 as visiting the Ventas facilities throughout Bebo's scheme, testified she did not stay at the Ventas facilities after March 2009, and instead stayed at hotels when she traveled to visit those facilities. (Tr. 2998:1-7).

III. BEBO'S LEGAL ARGUMENTS FAIL

A. Even If The Board Was Aware Of ALC's Use of Employees, Bebo Is Still Liable.

Even accepting Bebo's story that she, or someone else, informed the board or certain of its members that ALC was using employees in the covenant calculations, Bebo is still liable. While certain witnesses other than Bebo, namely Buono and Grant Thornton, testified that the use of some employees was brought to the board's attention, these witnesses are in agreement that key details of the scheme were not disclosed. Indeed, no witness other than Bebo testified the board was aware that ALC included in the calculations: (a) large number of employees, (b) Bebo's friends and relatives, and (c) employees who did not stay at the Ventas facilities. For this reason, telling the board that ALC was including a limited number of employees, in the context of Bebo's assurances that she was sending employees to the Ventas facilities to improve operations and occupancy, at best, is a misleading "half-truth" that still evidences an intent to deceive. *See, e.g. Schlifke v. Seafirst Corp.*, 866 F.2d 935, 944 (7th Cir. 1989) ("incomplete disclosures, or 'half-truths,' implicate a duty to disclose whatever additional information is necessary to rectify the misleading statements").

Moreover, even ignoring every percipient witness and accepting Bebo's testimony that she disclosed the details of her scheme to the board, this merely proves she lied to ALC's board, given Bebo's testimony that she told the board Ventas *agreed* to all of ALC's practices.[22]

Additionally, crediting Bebo's claims that she merely followed the orders of Rhinelander,

[22] Bebo also claims that Ng's limited knowledge of ALC's use of employees also absolves Bebo of liability. Since Bebo concedes she never discussed ALC covenant practices with Ng, Bebo could not have known, or relied on, any information Ng was given about ALC's covenant practices. (Ex. 497, at 328:12-20)

Hennigar, or the board, is not a sufficient defense.[23] Indeed, the Commission and federal courts have "repeatedly affirmed that someone who participates in a fraudulent scheme by following his superior's instructions to carry out fraudulent acts can be liable as a primary violator under Section 10(b) and Rule 10b-5." *Robert W. Armstrong, III*, AP File No. 3-9793, 58 S.E.C. 542, 563 (June 24, 2005); *U.S. v. Hill*, 643 F.3d 807, 864-865 (11th Cir. 2011) (wire fraud defendant's "contention that he was simply following [superior's] orders ... is no defense"); *SEC v. Antar*, 15 F. Supp. 2d 477, 523-24 (D.N.J. 1998) (rejecting "good soldier defense" that defendant "was just following orders and he never asked about nor was he ever interested in the significance of the activities which he was ordered to carry out"), *aff'd*, 44 Fed. Appx. 548 (3d Cir. 2002).

B. Bebo's Reliance Defenses Fail.

Bebo contends she did not act with scienter because she relied in good faith on a variety of constituencies, including ALC's attorneys, auditors, and disclosure committee. But Bebo cannot meet the elements for any such defense, and her claims of good faith reliance fail accordingly. For instance, a reliance on counsel defense "[1] requires that a respondent 'made complete disclosure to counsel, [2] sought advice as to the legality of his conduct, [3] received advice that his conduct was legal, and [4] relied on that advice in good faith.'" *John A. Carley*, AP File No. 3-11626, 2008 SEC LEXIS 222, *46-47 (Jan. 31, 2008) (quoting *Markowski v. SEC*, 34 F.3d 99, 104-105 (2d Cir. 1994)); *see also U.S. v. Van Allen*, 524 F.3d 814, 823 (7th Cir.

[23] Bebo's claims that she acted as a mere instrumentality of Rhinelander or Hennigar is belied by her own testimony that she was a micromanager and deeply involved in the execution and oversight of ALC's operations. (Tr. 3849:5-22). Bebo previously testified that she performed "the customary responsibilities" of president and CEO. (Ex. 488, 47:22-49:15). To that end, unlike Rhinelander or Hennigar, neither of whom had management responsibilities, Bebo was ultimately responsible for ALC's management, with approximately 20 ALC executives reporting directly to her. (Tr. 3847:14-18). Further, ALC's Commission filings never disclosed, as Bebo now claims, that Bebo had a diminished managerial role or that Rhinelander acted as a *de facto* CEO. (Exs. 2-13).

2008); *Zacharias v. SEC*, 569 F.3d 458, 467 (D.C. Cir. 2009).[24]

Bebo's reliance on counsel defense fails because she did not fully disclose her conduct to, or follow the advice of, any attorney. In her brief, Bebo claims the only attorney she relied on was Fonstad. But beyond Bebo's self-serving testimony, the only evidence of Bebo seeking Fonstad's advice was her general inquiry into whether the limited number of employees who stayed at the Ventas facilities could be included in the covenant calculations. (Ex. 1152). Bebo never disclosed to Fonstad, or received advice regarding the legality of, key details of her scheme, such as the use of (a) large number of employees, (b) employees who did not stay at the Ventas facilities, and (c) the use of employees at multiple properties. Indeed, when Bebo sought Fonstad's advice in January 2009, ALC was only slightly missing the covenants, and there was not yet any need to employ these additional measures.

Moreover, Bebo did not rely on Fonstad because she failed to follow his express advice. Fonstad advised Bebo to send a letter to Ventas that (a) disclosed ALC wanted to include employees in the covenant calculations, (b) set a limit on the number that could be included, and (c) requested Ventas's signature to document any agreement. (Ex. 1152). Yet Bebo chose to disregard this advice by never informing Ventas that ALC used employees in the covenant calculations, let alone the details of her scheme, and never obtaining Ventas's written approval.

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[24] Bebo's "reliance on auditors" defense contains identical requirements of full disclosure and confirmation from the auditor that the contemplated conduct is appropriate. *See, e.g., SEC v. Yuen*, 2006 U.S. Dist. LEXIS 33938, *110-113 (C.D. Cal. Mar. 16, 2006) (discussing elements that must be established to assert "reliance on auditors"), *aff'd*, 2008 U.S. App. LEXIS 7606 (9th Cir. Apr. 1, 2008); *SEC v. Johnson* 174 Fed. Appx. 111, 114-15 (3d Cir. 2006) (reliance on auditor defense "is available, however, only when all pertinent facts are disclosed to the professional"); *Provenz v. Miller*, 102 F.3d 1478, 1491 (9th Cir. 1996) ("If it is true that defendants withheld material information from their accountants, defendants will not be able to rely on their accountant's advice as proof of good faith."); *The Rockies Fund, Inc.*, AP File No. 3-9615, 2007 SEC LEXIS 1954, *10-11, n.14 (Aug. 31, 2007) (reliance on auditor defense failed when "Respondents adduced no evidence showing full disclosure of relevant facts to the auditor and communication of the auditor's opinion to those asserting reliance on it").

Bebo also cannot meet the elements of any reliance on auditor defense because she failed to disclose key material facts to Grant Thornton – namely that ALC was including employees who did not stay at the Ventas facilities – and affirmatively lied to Koeppel and Robinson when she told them Ventas had agreed to include employees in the covenant calculations.[25] Bebo concedes that she "rarely, if ever, spoke directly with Grant Thornton about employee leasing after her initial conversation with Melissa Koeppel in April or May of 2009." (Resp. Br. at 203). Thus, by her own admission, Bebo did not provide Grant Thornton with full disclosure about ALC's use of employees and relatives who did not stay at the Ventas properties, which did not begin until later in 2009.

Bebo also deceived Grant Thornton by selecting the names of large numbers of persons who did not stay at the Ventas facilities, knowing Grant Thornton was looking for supporting documentation for the employees who were "leasing rooms" at the Ventas facilities. And she failed to disclose to Grant Thornton that the list of names included her parents, husband, friend, and Bucholtz's family members. While Bebo claims these names would "stick out like a sore thumb to any third party reviewing the lists," (Resp. Br. at 109), she cannot explain how Grant Thornton would be able to divine how people with the last name Welter, Paremsky, Schweer, Rodwick, or Salvani were related to Bebo or Bucholtz.

Nor can Bebo claim she relied on ALC's disclosure committee. No evidence exists that the committee ever advised Bebo that ALC's use of employees was appropriate. Bebo never attended disclosure committee meetings, and admits she has no idea whether the committee even discussed the topic. (Ex. 502, at 1139:20-21 ("I was not at the disclosure committee meeting, so

[25] For the same reason, Bebo cannot assert reliance on ALC's accounting staff, all of whom were told the inclusion of employees was premised on an agreement with Ventas. Moreover, ALC's highest ranking accountant, Buono, repeatedly warned Bebo about ALC's covenant practices, and Grochowski later confronted Bebo with his own concerns.

I don't know what was shown at the meeting.")). Moreover, four of the five witnesses who attended disclosure committee meetings – Buono, Fonstad, Lucey, and Zak – had no recollection of ALC's inclusion of employees ever being discussed. (Tr. 1619:5-20, 2389:14-22, 3740:13-25, 4380:14-4381:3). The fifth disclosure committee witness, Hokeness, testified that the committee was never given any specifics regarding the use of employees in the covenant calculations, such as the number of employees included or the fact that employees who did not stay at the facilities were being used to meet the covenants.[26] (Tr. 3133:19-3134:15). Consistent with these witnesses' testimony, the disclosure committee meeting minutes do not mention the inclusion of employees in the covenant calculations and, in the case of the 2009 minutes, instead refer generally to "adjustments" and "clarifications as to census."[27] (Exs. 124-127).

Regardless of whom Bebo claims she relied on, any reliance defense is limited to the charges containing a scienter element. This is because a defendant's claim of reliance "is simply a means of demonstrating good faith and represents possible evidence of an absence of any intent to defraud." *U.S. v. Peterson,* 101 F.3d 375, 381 (5th Cir. 1996); *see also SEC v. McNamee,* 481 F.3d 451, 455-56 (7th Cir. 2007). Put another way, a reliance defense merely "addresses scienter." *SEC v. Huff,* 758 F. Supp. 2d 1288, 1348 (S.D. Fla. 2010). For this reason, courts routinely refuse to allow a reliance defense to negate claims that do not have a scienter element. *Erenstein v. SEC,* 316 Fed. Appx. 865, 869-70 (11th Cir. 2008); *SEC v. Verdiramo,* 2011 U.S. Dist. LEXIS 101856, *31 (S.D.N.Y. Sept. 9, 2011); *SEC v. Mut. Benefits Corp.,* 2004 U.S. Dist. LEXIS 23008, *55 (S.D. Fla. Nov. 10, 2004). As in these decisions, Bebo's purported reliance

[26] Hokeness additionally testified that he had been told Ventas agreed to ALC's use of employees in the covenant calculations. (Tr. 3081:12-19, 3100:14-19)

[27] Beginning with the February 2010 meeting minutes, the minutes merely state: "Per J. Buono – lease covenants have all been achieved." (Exs. 128-136).

does not serve as a defense to the charges in the OIP lacking a scienter element.

C. The False And Misleading Statements In ALC's Commission Filings Are Actionable.

Bebo argues that the statements in ALC's Commission filings that it was "in compliance" with the Ventas covenants are mere "opinions" that cannot sustain a securities fraud charge. But she ignores that a federal court, in a securities fraud case against her, found those very statements to be actionable while rejecting the same arguments Bebo again raises here. *Pension Trust Fund for Operating Eng'rs v. Assisted Living Concepts, Inc.* 2013 U.S. Dist. LEXIS 87568, at *24-27, *45-46 (E.D. Wis. June 21, 2013) ("[I]t is clear that [the plaintiff] has pled facts sufficient to establish that ALC and Bebo provided false statements when they stated that ALC was in compliance with its Lease with Ventas.").[28] Given the statements are identical, there is no need to revisit the district court's ruling that ALC's false and misleading statements of compliance with the Ventas covenants are actionable under Section 10(b) and Rule 10b-5.

Moreover, as the Supreme Court recently confirmed, ALC's statements that it was "in compliance" with the Ventas covenants – as opposed to statements that ALC "believed" or "thought" it was in compliance – were statements of fact as opposed to statements of opinion. *Omnicare, Inc. v. Laborers' Dist. Council Constr. Indus. Pension Fund*, 135 S. Ct. 1318, 1325-26 (2015). This distinction is best shown by ALC's own representations regarding the Ventas covenants, one of which is a statement of fact while the other is an opinion:

Statement of Fact	Statement of Opinion
"…the failure to meet certain operating and occupancy covenants in the CaraVita operating lease could give the lessor the right to accelerate the lease obligations and terminate	"The acceleration of the remaining obligation and loss of future cash flows from operating those properties could have a material adverse impact on our operations. Based upon current

[28] As noted in the Division's brief, the *Pension Trust* decision is simply the latest in a long line of authority holding that a statement of compliance with contractual covenants, if false or misleading, satisfies the standards of Section 10(b) and Rule 10b-5. (Div. Br. at 48).

our right to operate all or some of those properties. *We were in compliance* with all such covenants as of December 31, 2011…"	and reasonably foreseeable events and conditions, *ALC does not believe* that there is a reasonably likely degree of risk of breach of the CaraVita covenants."

(Ex. 13, p. 43 (emphasis added)).[29]

Even if the Court were to consider both statements above to be expressions of opinion, they both are actionable under *Omnicare* because Bebo did not believe them to be true. 135 S. Ct. at 1326-27. They would also be actionable because they contain material omissions. *Id.* at 1329 ("[I]f a registration statement omits material facts about the issuer's inquiry into or knowledge concerning a statement of opinion, and if those facts conflict with what a reasonable investor would take from the statement itself, then [the antifraud provisions] create[] liability."). Absent any disclosure that ALC's compliance with the Ventas covenants was contingent on the use of large numbers of "employees," investors were left with the false impression that actual occupancy and coverage ratio at the Ventas facilities met the covenants. This critical omission renders the above statements actionable, either as statements of fact or opinion.

Bebo places the most emphasis on the pre-*Omnicare* decision in *Zaluski v. United Am. Healthcare Corp.*, 527 F.3d 564 (6th Cir. 2008). Despite Bebo's claim that *Zaluski* is even more "on point" than the *Pension Trust Fund* case involving the exact same statements at issue in these proceedings, *Zaluski* did not involve a company's statement that it was in compliance with any covenant or contract. Rather, as opposed to ALC's filings which expressly stated ALC's compliance with the financial covenants, the *Zaluski* "financial statements contained no reference to the impairment or likelihood of impairment to [a] contract" and the plaintiffs' claims were based "entirely on Defendants' failure to disclose" the breach of a contract. *Id.* at 571, 577. Thus, unlike in Bebo's case, the analysis was not whether there had been a false or misleading

[29] Bebo admits she was aware of these statements at the time she certified ALC's Commission filings. (Ex. 502, pp. 1145:3-1150:17).

statement, but whether the company had a duty to disclose certain information. *Id.* at 572.[30]

Bebo also fails to cite *Zaluski*'s holding that "once a company chooses to speak," as ALC did when it represented it was in compliance with the financial covenants, "it must provide complete and non-misleading information with respect to subjects on which [it] undertakes to speak." 527 F.3d at 572 (citations omitted). To that end, *Zaluski* cited to a prior Sixth Circuit holding, consistent with *Omnicare*, that "once [the issuer] elected to make statements such as the statement regarding...objective data, it was required to qualify that representation with known information undermining (or seemingly undermining) the claim." *Id.* at 573 (quoting *City of Monroe Emps. Ret. Sys. v. Bridgestone Corp.*, 399 F.3d 651, 673 (6th Cir. 2005)).

Thus, rather than helping Bebo, *Zaluski*, like *Omnicare*, supports a fraud charge by standing for the proposition that once ALC chose to disclose that it was in compliance with the financial covenants, ALC could not hide from investors that it was only meeting the covenants by including large numbers of employees and others who never stayed at the Ventas facilities.

D. ALC's False Statements Were Material.

Bebo premises her materiality argument on the event study performed by Smith. But as Bebo conceded in her Wells submission, stock price movement is only "one indicator" among a variety of measures that can demonstrate materiality. (Ex. 373, p. 30); *see also, Basic Inc. v. Levinson*, 485 U.S. 224, 236 (1988) (rejecting "approach that designates a single fact or occurrence as always determinative of an inherently fact-specific finding such as materiality"); *No. 84 Empl'r-Teamster Joint Council Pension Trust Fund v. Am. W. Holding Corp.*, 320 F.3d 920, 934 (9th Cir. 2003) (rejecting assertion that stock drop is required to establish materiality);

[30] *Zaluski* also analyzed the company's duty to disclose in the context of the PSLRA's "safe-harbor" provisions for forward-looking statements. 527 F.3d at 572. That safe-harbor provision does not apply in SEC enforcement actions. *See, e.g., SEC v. E-Smart Techs.*, 31 F. Supp. 3d 69, 84 (D.D.C. 2014) (citations omitted); 15 U.S.C. § 78u-5(c)(1).

U.S. v. Bilzerian, 926 F.2d 1285, 1298 (2d Cir. 1991) (stock price movement "does not establish the materiality of the statements made, though stock movement is a factor the jury may consider relevant"); *Geiger v. Solomon-Page Grp.*, 933 F. Supp. 1180, 1188 (S.D.N.Y. 1996) ("Evidence of stock price movement may be relevant to the issue of materiality but it is not determinative.").

Staff Accounting Bulletin ("SAB") 99 recognizes that materiality may be determined using both quantitative – in terms of impact to the financial statements – and qualitative measures, and courts routinely employee SAB 99's guidance when assessing materiality. *See, e.g., Ganino v. Citizens Utils. Co.*, 228 F.3d 154, 163 (2d Cir. 2000) ("SAB No. 99 is thoroughly reasoned and consistent with existing law – its non-exhaustive list of factors is simply an application of the well-established *Basic* analysis to misrepresentations of financial results – we find it persuasive guidance for evaluating the materiality of an alleged misrepresentation."); *Higginbotham v. Baxter Int'l, Inc.*, 495 F.3d 753, 759 (7th Cir. 2007) ("securities lawyers often use a 5% [impact to financial statements] as a rule-of-thumb approach to what is 'material'") (citing SAB 99)).

The Division's expert, Barron, applied SAB 99 and offered unrebutted testimony that a default would have been material to ALC's financial statements, even if ALC could not, *ex ante*, quantify a default's potential effect. (Ex. 377, ¶¶ 60-77). Indeed, each of ALC's Forms 10-K and 10-Q represented that a covenant default "could have a material adverse impact on our operations." (Exs. 2-13). These filings also disclosed the amount of unpaid rent that ALC could owe resulting from a default, between $16.7 and $26.8 million. (*See, e.g.*, Ex. 2, p. 30, Ex. 13, p. 43). Moreover, when ALC bought the eight properties to settle its litigation with Ventas, ALC wrote off the $8.9 million intangible asset associated with the Ventas lease, which ALC was required to write off once the lease was terminated. (Ex. 16, p. 6). These amounts greatly

exceeded the 5% of net income threshold provided for by SAB 99, which merely ranged from $1.15 to $1.73 million during the relevant period, and demonstrate the materiality of the Ventas covenants to ALC. (Ex. 377, ¶¶ 64-65).

The Court also heard unrebutted lay testimony that actual investors considered ALC's compliance with the Ventas covenants to be important. Specifically, ALC's directors, all of whom were ALC shareholders, repeatedly inquired at board meetings about ALC's compliance with the financial covenants.[31] (*See, e.g.*, Ex. 95, pp. 4-5; Ex. 100, p. 2; Ex. 104, pp. 2-3). Buntain testified ALC's compliance was important to him as an investor, and that he had discussions with Hennigar about the impact of non-compliance on ALC's stock price. (Tr. 1357:22-1358:17, 1359:6-15). Bebo herself admitted a potential investor in ALC would want to know whether a valid agreement existed to include employees in the covenant calculations. (Tr. 2134:17-2136:23). She also conceded in her May 3, 2012 handwritten letter: "we are off-side on the covenants and we are facing a material financial impact." (Tr. 2229:3-12; Ex. 354, p. 2).

Finally, Bebo's expert, Smith, acknowledged that the $2.37 drop in stock price following ALC's May 4, 2012 disclosure of the investigation into "irregularities" in the lease was a "significant abnormal decline." (Tr. 3637:5-3638:4; Ex. 14). While Bebo claims the stock drop resulted from the disclosure of the Ventas lawsuit, that lawsuit was publicly filed on April 26, 2012, and the market had more than a week to factor the lawsuit's impact into ALC's stock price. (Tr. 3650:2-3651:15; Ex. 14). Thus, the only "new" information contained in the 8-K which resulted in the significant drop in ALC's stock price was the disclosure that ALC had

[31] Bebo claims she lacked motive to engage in fraud. However, her assurances to the board prior to ALC entering the lease about her ability to meet the covenants, and her continuing representations that ALC was in compliance, provide a natural motive for her conduct. Also, as a young and inexperienced CEO, Bebo could have faced reputational damage or discipline had ALC breached the covenants, especially if ALC was required to make concessions to Ventas.

retained counsel to investigate "irregularities" in the Ventas lease, a reference to Milbank's internal investigation. (Tr. 386:3-6; Ex. 14).[32]

E. Bebo's Other Legal Arguments Fail.

Bebo's arguments challenging the Division's books and records claims are unavailing. At the hearing, the Division demonstrated that as a result of ALC's use of employees in the covenant calculations, various ALC books and records were inaccurate and falsified. These included the journal entries Bebo signed and the facilities' financial statements ALC sent to Ventas, all of which improperly recorded revenue associated with the fake occupants. Moreover, the officer's certificates provided to Ventas, which certified ALC's compliance with the covenants and calculated compliance using the fake occupants, were patently false and misleading. Bebo ordered ALC's use of employees and the attendant revenue, selected the employees' identities, and signed the improper journal entries. Thus, she was a direct cause of ALC's falsified and inaccurate books and records, and is liable for the charges in the OIP. While Bebo now claims her conduct involved "inadvertent mistakes," that is no defense to the books and records charges (Sections 13(b)(2)(A) and 13(b)(2)(B) and Rule 13b2-1), which lack an intent element.

Bebo has the audacity to argue that the very instrumentality of her fraud – the 997 account – operated as ALC's "key internal control" relating to its use of employees in the covenant calculations. Bebo rests this argument on the incorrect claim that her fraud had no

[32] Bebo also claims ALC's decision to settle the Ventas lawsuit had nothing to do with the occupancy covenants. However, shortly after ALC's May 4, 2012 8-K, which Ventas *understood to reference ALC's occupancy calculations*, Ventas sent ALC a letter alleging fraud related to the occupancy covenants and filed a motion for expedited discovery on the issue of the lease "irregularities" disclosed in the 8-K. (Tr. 386:3-6; Exs. 356, 357). ALC and Ventas settled the lawsuit shortly thereafter, on terms undisputedly material to ALC, before Ventas had the opportunity to take discovery and assert claims relating to the occupancy covenants. (Ex. 16).

impact on ALC's financial statements. To the contrary, the notes to the financial statements in ALC's Forms 10-K expressly state that, for the year at issue, ALC "was in compliance" with the Ventas covenants.[33] (Ex. 5, p. F-25; Ex. 9, p. F-26; Ex. 13, p. F-24). As Barron explained, no control existed to ensure that (a) this statement was accurate in light of ALC's inclusion of employees; (b) Ventas had agreed to allow the use of employees that ALC needed to comply with the covenants; or (c) that the employees were appropriately included based on some applicable criteria. (Ex. 377, ¶¶ 98-99). Further, Bebo concedes that ALC's controls relating to its covenant practices "were not as robust as they should have been." (Resp. Br. at 106). For these reasons and the reasons stated in the Division's opening brief, Bebo violated and caused violations of the Exchange Act's internal controls provisions.

In arguing against the OIP's reporting and certification charges, Bebo acknowledges that those provisions are violated if an issuer's Commission filings contain material misstatements or omissions. (Resp. Br. at 214). As discussed above, from 2009 through 2011, ALC's filings contained the false and misleading representation that ALC was in compliance with the Ventas covenants. Each of these filings similarly omitted the key disclosure that the only reason ALC was "in compliance" was by virtue of its inclusion of large numbers of employees and other non-residents who did not stay at the Ventas properties. While Bebo does cite a single decision, *SEC v. Black*, precluding claims under Rule 13a-14, she acknowledges that other courts allow the Commission to bring such claims. (Resp. Br. 215). Indeed, this Court has held that Rule 13a-14 claims are actionable. *China Ruitai Int'l Holdings Co., Ltd.*, AP File No. 3-15544, 2015 SEC LEXIS 424, *47-48 (Feb. 5, 2015).

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[33] ALC's Forms 10-K represented that: "The accompanying notes are an integral part of these consolidated financial statements." (Ex. 5, p. F-6; Ex. 9, p. F-6; Ex. 13, p. F-6).

IV. BEBO WAS NOT DENIED PROCEDURAL DUE PROCESS.

Bebo alleges various due process violations stemming from the Commission's administrative process, generally, as well as from the Court's evidentiary rulings and the Division's conduct in this case. None of those claims has merit.

A. Bebo's Challenges To The Structure And Rules Of The Commission's Administrative Proceedings Are Meritless.

Bebo argues that the "nature of" these proceedings itself violates due process and, as a result, the decision to initiate this action (instead of suing in district court) impaired her ability to mount an effective defense. It is well settled, however, the Federal Rules of Evidence and Civil Procedure do not apply in administrative proceedings, including those brought by the Commission. *Ralph Calabro, et al.*, AP File No. 3-15015, 2015 SEC LEXIS 2175, *46 & n.66 (May 29, 2015); *Niam v. Ashcroft*, 354 F.3d 652, 659-660 (7th Cir. 2004); *Richardson v. Perales*, 402 U.S. 389, 400-410 (1971). Thus, to the extent Bebo claims the Court erroneously failed to apply any federal rules, such a claim necessarily fails. To the extent she argues any evidence was inadmissible under the Commission's rules of practice, those claims likewise fail given the breadth of Rule 320 and the Commission's guidance to "favor liberality in the admission of evidence." *Del Mar Fin. Servs., Inc.*, AP File No. 3-9959, 56 S.E.C. 1332, 1350 (Oct. 24, 2003).

Nor is it the case, as Bebo argues, that these proceedings are unconstitutional because they follow a different set of discovery and evidentiary rules than do federal courts. The Commission has repeatedly rejected such challenges. *See, e.g.*, *Mitchell M. Maynard*, AP File No. 3-13008, 2009 SEC LEXIS 1621, *24 & n.21 (May 15, 2009); *Gregory M. Dearlove, CPA*, AP File No. 3-12064, 2008 SEC LEXIS 223, at *123-142 (Jan. 31, 2008) (rejecting argument that Commission rule governing hearing schedule violated due process), *pet. denied*, 573 F.3d

801 (D.C. Cir. 2009). Administrative proceedings satisfy the "the fundamental requirement of due process" because they afford respondents, like Bebo, an adequate "opportunity to be heard at a meaningful time and in a meaningful manner." *Mathews v. Eldridge*, 424 U.S. 319, 333 (1976) (citations omitted); *see also, e.g., Kornman v. SEC*, 592 F.3d 173, 182-83 (D.C. Cir. 2010) (Commission's summary disposition standards afford due process, as respondents are afforded "an opportunity to set forth [their] evidence, challenges, and defenses").

More specifically, Bebo's complaints about lack of access to evidence and particular witnesses ring hollow. Bebo's access to Hennigar and Ng – Canadian nationals residing in Canada – would not have been assured if this case was filed in district court. Federal Rule of Civil Procedure 45(b) does not provide for issuance or service of a subpoena to a foreign national in a foreign country. *See also* 28 U.S.C. § 1783 (providing for subpoena service in a foreign country only upon a national or resident of the United States).

As Bebo concedes, the only method of obtaining those witnesses' testimony would be via letters rogatory. However, Canada's letters rogatory process is time-consuming, burdensome, and litigants often encounter difficulties in obtaining discovery through this process. *See In re Ethicon, Inc.*, 2014 U.S. Dist. LEXIS 15292, *2566-67 (S.D.W.Va. Jan. 30, 2014) (citing other resources and cases). Further, "Congress gave the federal district courts broad discretion to determine whether, and to what extent, to honor a request for [letters rogatory] under 28 U.S.C. § 1782," (*In re Premises Located at 840 140th Ave. NE, Bellevue, Wash.*, 634 F.3d 557, 563 (9th Cir. 2011)), and "a district court is not required to grant a § 1782(a) discovery application simply because it has the authority to do so." *Intel Corp. v. Advanced Micro Devices, Inc.*, 542 U.S.

241, 264 (2004). Therefore, even if this case were brought in district court, there is no guarantee Bebo could have compelled discovery or testimony from Hennigar or Ng.[34]

Bebo also complains she was deprived of the opportunity to depose and cross-examine the ALC employees whose prior sworn declarations were admitted in lieu of live testimony. As a preliminary matter, Bebo's claimed inability to obtain information from these witnesses – because they purportedly were unwilling to meet with her counsel – was not caused by the Division. In fact, Bebo was able to meet with several of these witnesses and even obtained her own supplemental declarations, which were then introduced into evidence. (*See* Exs. 2142 and 2143). Even if other witnesses were unwilling to meet with Bebo, nothing precluded her from requesting the issuance of subpoenas to obtain relevant documents and/or trial testimony. Bebo also fails to cite to any additional admissible or exculpatory evidence that these witnesses would have provided. Indeed, *she does not dispute any fact contained in the admitted declarations*, which are limited to the witnesses' dates of attendance at the Ventas facilities and are uniquely within the knowledge of the declarants. Accordingly, Bebo was in no way prejudiced by the admission of the declarations.

Bebo's argument that this forum prejudiced her ability to properly investigate the disposition of her notes and board books is equally speculative and without merit. In the first instance, because Bebo concedes the Division is not responsible for the spoliation of any evidence, she cannot assert a spoliation defense or seek spoliation sanctions against the Division. *See, e.g., U.S. v. Esposito*, 771 F.2d 283, 286 (7th Cir. 1985) (spoliation doctrine does not apply

[34] In claiming she lacked access to Hennigar, Bebo ignores that her present attorneys deposed Hennigar in the course of her litigation with ALC and asked him detailed questions related to the allegations in these proceedings. (Ex. 492A). Moreover, Bebo could have sought to admit favorable portions of Hennigar's and Ng's investigative testimony in these proceedings, pursuant to Rule 235(a)(2), but chose not to do so.

unless *a party* engages in bad faith destruction of documents); *SEC v. Goble*, 682 F.3d 934, 947-48 (11th Cir. 2012) (same). Further, Bebo cannot articulate how she would have been able to investigate more fully her spoliation claims had this action been brought in district court. Bebo was permitted in these proceedings to seek subpoenas for documents and testimony from whomever she believes destroyed evidence. Indeed, Bebo had the opportunity to cross-examine the very ALC personnel whom she apparently accuses, without any proof, of disposing of her notes and board books.

Finally, Bebo's complaint that these proceedings deprived her of knowing facts disclosed to the Division ignores the *Brady* and *Jencks* obligations imposed on the Division under the Commission's Rules of Practice. These obligations provided Bebo, a respondent in a civil case, with evidentiary disclosure protections analogous to those afforded criminal defendants in district court.

B. Bebo Fails To Establish That Any Of The Court's Evidentiary Rulings Constitute A Denial Of Due Process.

Bebo contends the Court violated due process by admitting certain evidence at the hearing – such as the pre-hearing deposition testimony of David Hennigar or Solari's hearing testimony that waiving occupancy covenants is something he never would have agreed to do. However, the Rules of Practice expressly "favor liberality in the admission of evidence." *Del Mar Fin. Servs.*, 56 S.E.C. 1332 at 1350; 17 C.F.R. § 201.320 (allowing for admission of all evidence except that which is "irrelevant, immaterial or unduly repetitious"). And it is hard to fathom how the mere admission of such evidence – which this Court is free to credit or discredit – possibly constitutes the type of prejudice sufficient to establish a due process violation. *See China-Biotics, Inc.*, AP File No. 3-14581, 2013 SEC LEXIS 3451, *74-75 & n.129 (Nov. 4, 2013) (respondents must show prejudice to establish that evidentiary rulings created due process

violations); *Horning v. SEC*, 570 F.3d 337, 347 (D.C. Cir. 2009) ("In the absence of any suggestion of prejudice, we cannot conclude that Horning was deprived either of procedural due process or of appropriate notice and opportunity for a hearing.") (internal quotation marks omitted).

Moreover, Bebo fails to demonstrate that the Court erred in any of these determinations, that a district court would have ruled differently, or that any of the rulings prejudiced her. First, there was nothing "fundamentally unfair" about the admission of Hennigar's deposition testimony taken during the course of Bebo's employment dispute with ALC. Bebo's current law firm had the opportunity to question Hennigar, and asked detailed questions, about the same topics at issue in this action. (Ex. 492A). Even in district court such testimony would be admissible against Bebo. *See* Fed. R. Evid. 804(b)(1).

The Court also properly admitted the testimony of Ventas witnesses as to their standard practices regarding leasing and covenants, while similarly rejecting Bebo's attempts to impose on Ventas an expensive fishing expedition to obtain contrary evidence. Solari's testimony as to what he would or would not have done or agreed to was crucial to contradict Bebo's claim that he agreed to permit ALC to include employees in the covenant calculations, and allowed Solari to state why he had such conviction in his testimony. Such testimony is routinely allowed in district court cases, and was likewise proper here. *See, e.g., U.S. v. Orr*, 692 F.3d 1079, 1095-97 (10th Cir. 2012) (allowing prosecution to ask investors whether they would have invested had they known certain information); *U.S. v. Dukes*, 242 Fed. Appx. 37, 45-46 (4th Cir. 2007) (same); *U.S. v. Bush*, 552 F.2d 641, 649-51 (7th Cir. 1975) (allowing city aldermen witnesses to testify whether they would have awarded contract to company had they known of defendant public officer's concealed interest in the company), *cert denied*, 424 U.S. 977 (1976).

To the contrary, Bebo's attempt to conduct wide-ranging document discovery on Ventas's general leasing and covenant practices was wholly irrelevant to what was or was not conveyed and known to Bebo. Bebo's discovery request was a speculative fishing expedition given the lack of any indication that Ventas treated ALC differently from its other tenants. The Court's evidentiary rulings in this regard were proper and no different than what a district court would have done. Indeed, just as this Court found when it limited the scope of Bebo's subpoena to Ventas (3/11/15 Order on Mot. to Modify Subpoena), a district court would have quashed any subpoena purporting to require Ventas to search for and produce documents irrelevant to the issues at hand. *See* F.R.C.P. 45(d)(3)(A)(iv) (authorizing courts to quash subpoenas imposing an "undue burden" on respondent). Moreover, because the Court did not limit Bebo's cross examination of Solari or other Ventas witnesses regarding their general leasing and covenant practices, Bebo was not prejudiced by the Court's prehearing rulings.

The Court appropriately sustained objections to questioning of witnesses using sometimes confusing terminology that needed explaining, such as "employee leasing." As discussed above, absent precise terminology, a witness testifying that he knew about "employee leasing" could mean that he merely knew employees were staying at the Ventas facilities in lieu of hotels, as opposed to knowing the details of ALC's covenant practices at issue here. For this reason, the Court properly required precision at certain points of witnesses' testimony. Moreover, when a party properly objected to the use of such terminology, the Court properly sustained it. When a party did not raise an objection, the Court typically permitted the question, as evidenced by the example cited by Bebo. (Resp. Br. at 253-54). Bebo's complaint seems to boil down to the fact that the Division objected to the use of such vague language, while she did

not object, or objected less frequently. This complaint, however, is of Bebo's own making, and does not prejudice her or otherwise establish a due process violation.[35]

C. Bebo's Allegations Of Misconduct By Division Staff Are Baseless And, In Any Event, Do Not Implicate Her Due Process Rights.

Bebo generally complains about the manner in which the Division approached, interviewed, and prepared witnesses. First, as Bebo concedes, there is nothing improper with the Division speaking to witnesses during the investigation or in preparation for trial, and such practice would have been no less extensive if this case were in district court. Indeed, even with the heightened due process protections afforded in criminal cases, government attorneys routinely meet with witnesses in advance of their trial or grand jury testimony. *See, e.g., U.S. v. Lieberman*, 608 F.2d 889, 897-99 (1st Cir. 1979) (claim that "suggestive remarks" were made to witnesses off the record did not involve due process violation); *U.S. v. Lee*, 815 F.2d 971, 974 (4th Cir. 1987) ("In short, the government may have prepared and presented the witness for maximum dramatic effect, but it did nothing improper."); *see also, U.S. v. McClintock*, 748 F.2d 1278, 1286 n.5 (9th Cir. 1984) (the fact that FBI agents met with witnesses late at night or at bars, while not condonable, did not constitute "overreaching").

Second, as is typical of her prejudice and due process claims, Bebo's arguments are short on substance. Bebo makes vague claims about improper coaching and rehearsing with witnesses. However, the examples of Buono and Solari cited in her brief (pp. 245-46) fail to establish any improper preparation by the Division. Bebo's claim that these witnesses "lack credibility" is a factual question for the Court to decide. The above examples cited in Bebo's

[35] The Division's use of the term "employee leasing" in investigative testimony is also irrelevant. Such testimony took place well before the initiation of these proceedings and while the Division was still investigating the case. Further, to the extent the Division's use of the term during investigative testimony limited impeachment at the hearing, given the evolution and often confusing nature of the term, this impacted both parties equally.

brief, as well as her attorneys' lengthy cross-examinations, establish that she had ample opportunity to attempt to undermine the credibility of the Division's witnesses. Bebo also does not explain how a pretrial deposition or some other rule or procedure available in district court would have assisted her in further challenging the credibility of any witness.

Bebo further argues the Division improperly influenced witnesses by referencing criminal referrals, Fifth Amendment privileges, and the SEC's cooperation program. She ignores that the Commission's Form 1662, *which the Division provides as a matter of policy to witnesses prior to their investigative testimony*, also refers to criminal referrals and the Fifth Amendment. Nor can Bebo explain how or why these references in any way improperly influenced a witness or prejudiced her. And she cites no authority for these propositions. Moreover, each witness called by the Division was represented by sophisticated attorneys, and would not be unduly influenced by any such statements by the Division. To the extent any witness was improperly influenced (which the Division disputes), Bebo had full opportunity to cross-examine the witnesses and establish any improper influence or credibility issues.

Bebo's remaining complaints about the Division's purported improper influencing of Buono are equally without merit. As to whether the Division told Buono that Bebo "threw him under the bus," Buono testified that he merely got that impression during his on-the-record testimony, of which Bebo has a verbatim transcript. (Tr. 2434:23-2435:24).[36] Despite her complaints, Bebo fails to point to any improper statements made by the Division to Buono. Regardless, Bebo had ample opportunity to question Buono about this issue, which she did. (Tr.

[36] Even if Division attorneys did make a statement to that effect to Buono, it would not constitute a due process violation. *See Lieberman*, 608 F.2d at 897-99.

2401-02, 2404-06). And, as discussed above, Bebo's allegation that the Division never provided Buono with Bebo's investigative testimony transcript is patently false. (Tr. 2502:11-25).

Moreover, Bebo fails to establish that she was prejudiced by these alleged acts, which is fatal to her due process claims. *See, e.g.*, *China-Biotics, Inc.*, 2013 SEC LEXIS 3451, *74-75 & n.129; *James E. Franklin*, AP File No. 3-12228, 2007 SEC LEXIS 2420, *15 (Oct. 12, 2007) (respondent failed to demonstrate "how any of his allegations of misconduct, even if true, might have prejudiced him in his defense").

D. Bebo Was Not Denied Adequate Time To Prepare Her Case.

Bebo contends she was afforded insufficient time to prepare her defense. Here too, however, she fails to establish a due process violation.

Pursuant to Rule of Practice 360(a)(2), when instituting these proceedings the Commission adopted a 300-day deadline for the Court's initial decision. In so doing, the Commission determined that such a deadline was appropriate based on the "nature, complexity, and urgency of the subject matter, and with due regard for the public interest and the protection of investors." *Id.* Bebo does not argue that such determination was improper. Rather, her complaint seems to be that this Court improperly denied her requests for continuances.[37]

The Supreme Court in *Ungar v. Sarafite*, 376 U.S. 575 (1964), articulated the standard for analyzing a due process challenge to the denial of a continuance. The Court noted that "[t]here are no mechanical tests for deciding when a denial of a continuance is so arbitrary as to violate due process. The answer must be found in the circumstances present in every case, particularly in the reasons presented to the trial judge at the time the request is denied." *Id.* at 589–90. The Commission has adopted *Ungar*'s framework and has instructed that such denials

[37] To the extent Bebo intends to challenge, generally, the propriety of Rule 360(a), the Commission has expressly held that the rule does not violate due process. *Dearlove*, 2008 SEC LEXIS 223, *131-33.

are improper only when they "constitute[] 'an unreasoning and arbitrary insistence upon expeditiousness in the face of a justifiable request for delay.'" *Dearlove*, 2008 SEC LEXIS 223, at *132-133 (quoting *Richard W. Suter*, A.P. File No. 3-6038, 47 S.E.C. 951, 963 (Oct. 17, 1983)); *see also Harding Advisory LLC*, AP File No. 3-15574, 2014 SEC LEXIS 4546, *4-6 (Mar. 14, 2014) (discussing policy of disfavoring adjournments of administrative proceedings).

Here, in denying Bebo's requests, the Court appropriately considered the relevant factors to correctly determine that Bebo's requested continuances were not warranted. (*See* Order Denying Renewed Motion for Relief From Rule 360(a)(2) (Apr. 7, 2015); Jan. 5, 2015 Prehearing Conf. Tr. at 16:14-21:1). Although Bebo complains about the size of the Division's production, the Commission has explicitly rejected arguments that large or complex case files inherently warrant extraordinary relief. *John Thomas Capital Mgmt. Grp.*, AP File No. 3-15255, 2013 SEC LEXIS 3860, *21-23 (Dec. 6, 2013) (the Division need not provide a "roadmap" of material exculpatory evidence, even if it was "not feasible for [respondents] to go through all of the [700 GB of electronic data produced by the Division] in advance of the hearing"); *Dearlove*, 2008 SEC LEXIS 223, *136-144 (rejecting argument that time-frame for administrative proceeding and size and complexity of record constituted a due process violation). Indeed, as the Court observed in denying Bebo's initial request to delay these proceedings, the size of the Division's investigative file was significantly smaller than the productions at issue in the *John Thomas Capital* and *Harding Advisory* cases, in which large investigative files did not warrant deviation from Rule 360(a)(2)'s timeframes. (Jan. 5, 2015 Prehearing Conf. Tr. at 17:6-14)

As to Bebo's complaints about the manner in which documents were produced, the Division produced electronic databases in the manner in which they were maintained by the Division: an electronic, text-searchable format. (Jan. 5, 2015 Prehearing Conf. Tr. at 7:16-22).

Such productions satisfy the Division's obligations. *John Thomas Capital Mgmt. Grp.*, 2013 SEC LEXIS 3860, *23 ("open file" production adequate). Bebo's protests to the format of the Division's production are further unfounded given that, prior to the production, Bebo confirmed to the Division that its proposed production format was acceptable and compatible with Bebo's law firm's IT systems. (Jan. 5, 2015 Prehearing Conf. Tr. at 7:23-8:3, 11:24-25).

Finally, Bebo's claims that she had insufficient time to prepare for the hearing are refuted by the fact that, prior to this action being instituted: (a) she had previously been sued for securities fraud based on allegations similar to the OIP and had already considered and developed her arguments in response; (b) she engaged in substantial discovery, and received voluminous documents, in her litigation with ALC involving issues similar to the ones presented in these proceedings; and (c) she was fully availed of the Wells process and tendered three submissions – totaling nearly 90 single-spaced pages – to the Division presenting detailed arguments against the Division's proposed claims. (*See,* Division's Resp. to Mot. to Delay Hearing, pp. 1-2 (Apr. 6, 2015). For these reasons, Bebo and her counsel understood the relevant universe of documents and were capable of mounting their defense.

V. COMMISSION ADMINISTRATIVE PROCEEDINGS ARE CONSTITUTIONAL

A. Section 929P(a) Of The Dodd-Frank Act Is Not Facially Unconstitutional.

Bebo contends that Section 929P(a) of the Dodd-Frank Act – which authorized the Commission to impose civil penalties against non-regulated persons in administrative proceedings – is facially invalid. Her arguments are premised on the notion that Congress improperly authorized the Commission to choose between bringing an enforcement action in federal court (which it was permitted to do prior to Dodd-Frank) and initiating an administrative proceeding.

1. Section 929P(a) Does Not Violate the Non-Delegation Doctrine.

To the extent Bebo intends to challenge the administrative proceedings on non-delegation grounds because Section 929P(a) gave the Commission a choice of forum, that claim fails.

"In a delegation challenge, the constitutional question is whether the statute has delegated legislative power to the agency." *Whitman v. Am. Trucking Ass'n, Inc.*, 531 U.S. 457, 472 (2001). The prosecution of violations of federal law, however, is a quintessentially *executive* function, *Morrison v. Olson*, 487 U.S. 654, 706 (1988); *Buckley v. Valeo*, 424 U.S. 1, 138 (1976), which includes broad discretion to select the appropriate forum in which to sue. *See U.S. v. Dockery*, 965 F.2d 1112, 1117 (D.C. Cir. 1992); *U.S. v. I.D.P.*, 102 F.3d 507, 511 (11th Cir. 1996). Under these settled principles, the Commission's decision whether to enforce the securities laws in an administrative forum or in a federal court does not involve the exercise of legislative power and therefore does not contravene the non-delegation doctrine.

2. Section 929P(a) Does Not Violate Equal Protection.

Bebo's equal protection challenge fares no better. She claims that by allowing the Commission a choice of forum, Section 929P(a) treats "unequal[ly]" defendants charged in district court actions (who may elect a jury trial),[38] and respondents in administrative proceedings (who may not). Resp. Br. at 223-24. But the Supreme Court has made clear that the exercise of prosecutorial discretion to select a forum, standing alone, does not violate equal

[38] To the extent Bebo argues that administrative proceedings contravene the Seventh Amendment, such a claim fails. The Supreme Court has long recognized that "the Seventh Amendment is not applicable to administrative proceedings." *Tull v. U.S.*, 481 U.S. 412, 418 n.4 (1987); *Grafinanciera, S.A. v. Nordberg*, 492 U.S. 33, 48-49 (1989). Thus, Congress "may assign th[e] adjudication [of such cases] to an administrative agency with which a jury trial would be incompatible, without violating the Seventh Amendment's injunction that jury trial is to be 'preserved' in 'suits at common law.'" *Atlas Roofing v. OSHRC*, 430 U.S. 442, 455 (1977).

protection. *U.S. v. Batchelder*, 442 U.S. 114 (1979). Moreover, prosecutorial decision-making is accorded a strong "presumption of regularity," *Hartman v. Moore*, 547 U.S. 250, 263 (2006), and the Commission can rationally determine, in accordance with the authority conferred by Congress, that some cases are better resolved through administrative proceedings than in district court.

Bebo's reliance on *Baxstrom v. Herold*, 383 U.S. 107 (1966), and *Humphrey v. Cady*, 405 U.S. 504 (1972), is unavailing and only underscores her misunderstanding of the doctrine. Those cases examined state civil commitment schemes that treated persons convicted of crimes differently from the population generally. They reflect the principle that "the equal protection clause forbids the [S]tate to treat one group, including a group of prison inmates, arbitrarily worse than another." *Anderson v. Romero*, 72 F.3d 518, 526 (7th Cir. 1995). But Section 929P does not treat any group worse than another similarly situated group. Indeed, it makes no distinction at all among groups. Thus, Bebo's equal protection challenge fails.

3. Section 929P(a) Does Not Violate Due Process.

Finally, Bebo contends that Section 929P(a) allows the Commission to "preemptive[ly] punish[]" a "citizen's exercise of her constitutional right" to a jury trial, because it allows the Commission to take into account how a jury might decide a case when selecting the forum in which to proceed. Resp. Br. at 226-27. As support, Bebo cites *U.S. v. Jackson*, 390 U.S. 570 (1968), which struck down a statutory provision exposing defendants to greater penalties if they exercised their right to a jury trial. She also cites *Blackledge v. Perry*, 417 U.S. 21 (1974), which held that it was unconstitutional "for the State to respond to [the defendant's] invocation of his statutory right to appeal by bringing a more serious charge against him." *Id.* at 28-29. The Court cautioned that defendants must be permitted to pursue their rights "without apprehension that the

State will retaliate" against them. *Id.* at 28. *Jackson* and *Blackledge*, therefore, stand for the proposition that individuals may not be "penalize[d]" for exercising a constitutional right or privilege. *Jackson*, 390 U.S. at 583; *see also* Resp. Br. at 226 (citing *Griffin v. California*, 380 U.S. 609 (1965), and *Miranda v. Arizona*, 384 U.S. 436 (1966), for the same principle).

Here, however, Bebo is not being penalized for the exercise of any constitutional right or privilege. Indeed, it is unclear what constitutional right she believes is at issue. Bebo does not have a constitutional right to choose the forum in which she is charged with violating the securities laws, nor does she have a Seventh Amendment right to a jury trial in cases where, as here, the Commission chooses to initiate an administrative proceeding. *Atlas Roofing*, 430 U.S. at 455. Bebo's citation to *Wymelenberg v. Syman*, 328 F. Supp. 1353, 1355 (E.D. Wis. 1971), also does not advance her claim because the case involved a state's infringement of the "constitutional right to travel to and settle in the state of [their] choice," a right that is not at issue here. *Id.* For all of these reasons, Bebo's due process challenge fails.

B. The Commission's Use Of ALJs Does Not Violate Article II Of The Constitution.

Bebo contends that this proceeding violates the Appointments Clause of Article II both because the presiding ALJ was not properly appointed and because his "multiple-layer tenure protection impedes the President's ability to exercise executive power over him." Resp. Br. at 228. Both of those claims fail because Commission ALJs are employees, not constitutional officers, and thus are not subject to the strictures of Article II.[39]

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[39] Two district court judges have preliminarily enjoined, on Article II grounds, Commission administrative proceedings. The government has appealed those decisions. *See Hill v. SEC*, No. 1:15-cv-1801, Docket No. 32 (N.D. Ga. June 24, 2015), *appeal pending*, No. 15-12831 (11th Cir.); *Gray Fin. Group, Inc. v. SEC*, No. 1:15-cv-492, Docket No. 60 (N.D. Ga. Aug. 19, 2015), *appeal pending*, No. 15-13738 (11th Cir.); *Duka v. SEC*, No. 1:15-cv-357, Docket No. 61 (S.D.N.Y. Aug. 12, 2015), *appeal pending* (2d Cir.). The Seventh Circuit, however, denied Bebo's motion for an injunction following the district court's dismissal of her suit to enjoin these

1. Commission ALJs Are Employees, Not Constitutional Officers.

The Appointments Clause mentions two categories of officers: principal officers and inferior officers. U.S. Const. art. II, § 2, cl. 2. Principal officers are selected by the President with the advice and consent of the Senate, while Congress may "by law vest the appointment" of "inferior Officers" in "the President alone, in the Courts of Law, or in the Heads of Departments." *Id.* The Clause does not speak to the power to appoint employees who are not officers, and the requirements of the Clause are therefore not applicable to these individuals. *See Buckley*, 424 U.S. at 126 n.162; *Tucker v. Comm'r*, 676 F.3d 1129, 1132 (D.C. Cir. 2012).

The Supreme Court has said that whether government personnel are officers or employees is determined by "the manner in which Congress has specifically provided for the creation of the . . . positions, their duties and appointment thereto." *Burnap v. U.S.*, 252 U.S. 512, 516 (1920); *see also Freytag v. Comm'r*, 501 U.S. 868, 880 (1991). "Inferior officers," like principal officers, are persons who "exercis[e] significant authority pursuant to the laws of the United States," a category that excludes "lesser functionaries subordinate to officers of the United States." *Buckley*, 424 U.S. at 125-26 & n.162; *see Free Enterprise Fund v. PCAOB*, 561 U.S. 477, 506 n.9 (2010). All relevant considerations demonstrate that the Commission's ALJs are such "lesser functionaries."

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proceedings, *Bebo v. SEC*, No. 15-1511, Docket No. 9 (7th Cir. Apr. 1, 2015), and this week affirmed the district court's dismissal for lack of jurisdiction. *Id.*, Docket No. 28 (7th Cir. Aug. 24, 2015). The Seventh Circuit's ruling is consistent with several other district court decisions holding that district courts lack jurisdiction to reach plaintiffs' Article II claims. *Tilton v. SEC*, No. 15-cv-2472, 2015 U.S. Dist. LEXIS 85015 (S.D.N.Y. June 30, 2015), *appeal pending* (2d Cir.); *Spring Hill Capital Partners, LLC v. SEC*, No. 15-cv-4542 (S.D.N.Y. June 26, 2015); *Chau v. SEC*, 72 F. Supp. 3d 417, 425 (S.D.N.Y. 2014), *appeal pending*, No. 15-461 (2d Cir.); *Jarkesy v. SEC*, 48 F. Supp. 3d 32, 37-38 (D.D.C. 2014), *appeal pending*, No. 14-5196 (D.C. Cir.).

a. The history of the ALJ system and the relevant statutory provisions demonstrate that Congress intended ALS to be employees.

The Commission has made use of employees as hearing examiners throughout its existence. *See Charles Hughes & Co. v. SEC*, 139 F.2d 434 (2d Cir. 1943) (reviewing Commission order following proceedings before hearing examiner). Hearing examiners were originally subject to the Classification Act of 1923 and dependent on their agency's ratings for compensation and promotion. *Ramspeck v. Federal Trial Exam'rs Conference*, 345 U.S. 128, 130 (1953). In order to address complaints about hearing examiners' partiality toward their employing agencies, when Congress enacted the Administrative Procedure Act in 1946, it "separat[ed] adjudicatory functions and personnel from investigative and prosecution personnel in the agencies," by placing hearing examiners under the jurisdiction of the Civil Service Commission, which Congress vested with control of the ALJs' compensation, promotion, and tenure. *See id.* at 131-32. Congress, however, gave no indication that it meant to elevate ALJs' status above that of the investigative and prosecution personnel of the agency.

Indeed, in enacting the APA, Congress envisioned that an ALJ's "initial decision" would be "advisory in nature" and preserved for the agency "complete freedom of decision—as though [the agency] had heard the evidence itself." U.S. Dep't of Justice, *Attorney General's Manual on the Administrative Procedure Act* 83-84 (1947) (Manual).[40] Thus, in reviewing an ALJ's initial decision, the agency "retains 'all the powers which it would have in making the initial decision[.]'" *Nash v. Bowen*, 869 F.2d 675, 680 (2d Cir. 1989) (quoting 5 U.S.C. § 557(b)).

[40] The Manual, as "a contemporaneous interpretation [of the APA]," *Vermont Yankee Nuclear Power Corp. v. Natural Res. Def. Council, Inc.*, 435 U.S. 519, 546 (1978), is "give[n] 'considerable weight,'" *Brock v. Cathedral Bluffs Shale Oil Co.*, 796 F.2d 533, 537 (D.C. Cir. 1986) (citation omitted).

At the Commission, as throughout the federal government, ALJs are civil service employees in the "competitive service." 5 C.F.R. § 930.201(b). As such they are subject to the provisions of the Civil Service Reform Act of 1978, 5 U.S.C. § 1101 *et seq.*, which, among other things, establishes merit systems principles to guide agency personnel management, *id.* § 2301, and specifies the administrative and judicial remedies available in response to prohibited personnel practices described in the statute, *id.* §§ 1204, 1212, 1214, 1215, 1221.

The Office of Personnel Management (OPM), which oversees federal employment for ALJs and other civil servants, administers a detailed civil service system for selecting ALJs that includes examinations for ALJ candidates, *see id.* §§ 1104, 1302; 5 C.F.R. §§ 930.201(d)-(e), 930.203; ranking ALJ applicants for placement on a register of eligible candidates according to their qualifications and numerical ratings, 5 U.S.C. § 3313; 5 C.F.R. § 332.401; and issuing "certificate[s] of eligibles" from which federal agencies—including the Commission—may select individuals to fill ALJ vacancies, 5 U.S.C. §§ 3317, 3318; 5 C.F.R. §§ 332.402, 332.404; *see also id.* § 930.204(h) (providing for transfer of ALJs from one agency to another). OPM oversees each agency's "decisions concerning the appointment, pay, and tenure" of ALJs, *id.* § 930.201(e)(2), and establishes classification and qualification standards for the ALJ positions, *id.* § 930.201(e)(3).

b. Commission ALJs are subject to the plenary authority of the Commission and do not exercise the requisite "significant authority" to be constitutional officers.

The Commission's regulations and governing statutes make clear that ALJs are simply employees of the Commission, which has retained its decision-making authority in every respect. The Commission employs ALJs in its discretion, and all final agency determinations belong to the Commission, not its ALJs. Congress does not require the Commission to use its ALJs to

conduct its administrative proceedings, and Commission regulations provide that a "[h]earing officer" can be an ALJ, a panel of Commissioners, an individual Commissioner, or any other person duly authorized to preside at a hearing. 17 C.F.R. § 201.101(a)(5). The Commission may at any time during the administrative process "direct that any matter be submitted to it for review." *Id.* § 201.400(a). The presiding ALJ prepares only an "initial decision," and, if no further review is sought or otherwise ordered by the Commission, then the Commission issues an order of finality, specifying "the date on which sanctions, if any, take effect." *Id.* §§ 201.360(a)(1), 201.360(d)(2).[41]

The Commission reviews the ALJ's decisions *de novo*, and "may affirm, reverse, modify, [or] set aside" the initial decision, "in whole or in part," and it "may make any findings or conclusions that in its judgment are proper and on the basis of the record." *Id.* § 201.411(a). The Commission may also "remand for further proceedings [or] for the taking of additional evidence," or "hear additional evidence" itself. *Id.* § 201.452. And if "a majority of participating Commissioners do not agree to a disposition on the merits," the ALJ's "initial decision shall be of no effect." *Id.* § 201.411(f).

For these reasons, the D.C. Circuit's conclusion in *Landry v. FDIC*, 204 F.3d 1125 (D.C. Cir. 2000), with respect to ALJs of the Federal Deposit Insurance Corporation applies equally here: The Commission's ALJs are not constitutional officers but employees, whose appointments do not implicate Article II, because they "can never render the decision of the [agency]." *Id.* at 1133; *see also Tucker*, 676 F.3d at 1134 (*Landry* "found the absence of any

[41] It is of no consequence that the federal securities laws and Commission regulations refer to ALJs as "officers" or "hearing officers." There is no indication that Congress or the Commission intended "officers" or "hearing officers" to be synonymous with "Officers of the United States," U.S. Const. art. II, § 2, cl. 2. Indeed, this Court reached the same conclusion in rejecting a respondent's Article II challenges. *Paul Edward Lloyd, Jr.*, AP File No. 3-16182, 2015 SEC LEXIS 3050, *81-82 (July 27, 2015).

authority to render final decisions fatal to the claim that the administrative law judges at issue there were Officers rather than employees"). In *Landry*, the D.C. Circuit held that the FDIC's ALJs are not constitutional officers because they issue only recommended decisions and proposed orders and "can never render the decision of the FDIC"; "final decisions are issued only by the FDIC Board of Directors." 204 F.3d at 1133. Similarly here, the Commission has plenary authority over all administrative proceedings and only the Commission can issue a final decision.

Freytag, which Bebo cites, does not compel a different conclusion. There, the Supreme Court held that special trial judges of the Tax Court are inferior officers. 501 U.S. at 880. But, as *Landry* expressly found, special trial judges are distinguishable from FDIC—and, by extension, Commission—ALJs because special trial judges are able to issue final decisions in certain categories of cases. 204 F.3d at 1134. In *Freytag*, it was undisputed that the special trial judges acted as inferior officers in one category of cases. 501 U.S. at 882. The government's argument was that the judges did not act as inferior officers in the specific category of cases at issue in *Freytag*. The Court found this reasoning unpersuasive, concluding that "[s]pecial trial judges are not inferior officers for purposes of some of their duties under [the statute], but mere employees with respect to other responsibilities." *Freytag* at 882.

In contrast, an ALJ can never render a final decision of the Commission. The Commission need not involve ALJs in its administrative proceedings at all, and is not bound by anything an ALJ decides. Rather, the Commission "retains plenary authority over the course of its administrative proceedings and the rulings of its law judges—both before and after the issuance of the initial decision and irrespective of whether any party has sought relief." *Michael Lee Mendenhall*, AP File No. 3-16104, 2015 SEC LEXIS 1071, *3 (Mar. 19, 2015). Indeed, the

Commission may review initial ALJ decisions on its own initiative, even where no review is sought. *E.g., Dian Min Ma*, AP File No. 3-15544, 2015 SEC LEXIS 1725, *1 (May 6, 2015); *Mendenhall* at *1; *Raymond J. Lucia Cos.*, AP File No. 3-15006, 2013 SEC LEXIS 3856, *5 (Dec. 6, 2013).

Although *Freytag* did cite to the significant discretion exercised by special trial judges in cases over which they do not have final decision-making authority, the D.C. Circuit observed in *Landry,* that this discussion "would have been quite unnecessary if the purely recommendatory powers were fatal in themselves." *Landry*, 204 F.3d at 1134. And, in any event, Commission ALJs' discretion differs significantly from those of the Tax Court's special trial judges. As the D.C. Circuit noted in *Landry,* "even for the non-final decisions of the type made by the [special trial judges] in *Freytag,* the Tax Court was required to defer to the [special trial judges'] factual and credibility findings unless they were clearly erroneous." *Id.* at 1133 (citations omitted).

By contrast, neither the Commission nor the FDIC Board that reviewed the ALJ decisions at issue in *Landry* defers to ALJs' factual findings. *Id.*; *see* 17 C.F.R. 201.411(a); *see also JCC, Inc. v. CFTC*, 63 F.3d 1557, 1566 (11th Cir. 1995) ("agencies" are generally not bound by their ALJ's fact finding).[42] And whereas special trial judges have the power, for example, to issue subpoenas, 26 U.S.C. § 7456(a); Tax Court Rule 181, and "to enforce compliance with discovery orders," *Freytag*, 501 U.S. at 881-82, the Commission's ALJs may issue subpoenas, but an order would need to be obtained from a district court to compel compliance, *see* 15 U.S.C. § 78u(e). As Commission's ALJs wield no more power than FDIC ALJs, *Landry*'s reasoning is fully applicable here.

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[42] The Commission similarly does not accept an ALJ's credibility determinations "blindly" and is not bound by such determinations. *Kenneth R. Ward*, AP File No. 3-9327, 56 S.E.C. 236, 260 (Mar. 19, 2003). The Commission can also choose to hear the witnesses' testimony itself. 17 C.F.R. § 201.452.

Further, if doubt exists as to the ALJs' status, the Commission should defer to Congress's own assessment of its statutory creations. *See Weiss v. U.S.*, 510 U.S. 163, 194 (1994) (Souter, J., concurring). In addition to treating ALJs like most other federal employees within the civil service system, in enacting the APA, Congress specified that it is the "agency" – not the President, the department head, or the Judiciary – that appoints ALJs. 5 U.S.C. § 3105; *see also Ramspeck*, 345 U.S. at 133 (in the APA, Congress "retained the [hearing] examiners as classified Civil Service employees"). Congress knew how to comply with the Appointments Clause, and at the time, the Supreme Court had long characterized appointments pursuant to the methods prescribed in the Appointments Clause as a "well established definition of what it is that constitutes [an officer of the United States]." *U.S. v. Mouat*, 124 U.S. 303, 307 (1888). In other words, Congress intended them to be employees. With rare exceptions for particular agencies, in the seven decades since creating the position of ALJ, Congress has not changed the method of ALJ appointment.

2. Even If The Commission's ALJs Are Inferior Officers, Their Tenure Protections Do Not Violate The Separation of Powers.

Because the Commission's ALJs are employees, not constitutional officers, the Commission need not reach the question whether its ALJs' tenure protections violate the separation of powers. But, even if the Commission determines that its ALJs are inferior officers, Bebo's separation of powers argument still fails. Congress may constitutionally place restrictions on the removal of inferior officers so long as the restrictions do not unduly "interfere with the President's exercise of the 'executive power' and his constitutionally appointed duty to 'take care that the laws be faithfully executed' under Article II." *Morrison*, 487 U.S. at 689-90; *Myers v. U.S.*, 272 U.S. 52, 161 (1926); *U.S. v. Perkins*, 116 U.S. 483, 485 (1886). The President exercises adequate control over the Commission, *see Humphrey's Executor v. U.S.*, 295 U.S. 602,

628-29 (1935), and Commission ALJs possess only the limited adjudicatory functions delegated to them by the agency. Their tenure protections therefore do not violate the separation of powers.

Relying on *Free Enterprise*, Bebo nonetheless argues that Commission ALJs' tenure protections deprive the President of the ability to execute the laws. But *Free Enterprise* did not announce a blanket rule that a removal framework is *per se* unconstitutional if more than one layer of tenure protection separates the President from an inferior officer. 561 U.S. at 506. Indeed, the Court explicitly *excluded* ALJs from its holding. *Id.* at 507 n.10. And, here, the President retains adequate control.

First, the constitutionality of limits on the President's removal power "depend[s] upon the character of the office" at issue. *Humphrey's Ex'r*, 295 U.S. at 631. Here, the functions the Commission has assigned to its ALJs are limited in scope and fall outside core executive authority. They involve the application of the law to a discrete set of facts in a particular case. Unlike the PCAOB in *Free Enterprise*, the ALJ here will not promulgate standards applicable to an entire sector of the economy or make policy-laden decisions about enforcement priorities. *Cf.* 561 U.S. at 484, 508. Rather, the ALJ will issue an initial decision, subject to review by the Commission, about whether Bebo violated the securities laws. *See id.* at 507 n.10.

Second, while the Supreme Court's "removal cases [are] designed . . . to ensure that Congress does not interfere with the President's exercise of the 'executive power,'" *Morrison*, 487 U.S. at 689-90 (footnote omitted), there has been no encroachment by Congress here. Congress has not imposed ALJs on the Executive Branch. Rather, the Commission has elected to employ ALJs to carry out certain limited functions. That Congress has permitted executive agencies to use, or not to use, ALJs as the agencies see fit is not an encroachment on executive authority.

Third, because the Commission retains ultimate authority over administrative proceedings, the Commission exercises sufficient control over its ALJs regardless of the limitations placed upon their removal. ALJs do not choose the cases they adjudicate; rather, the Commission decides whether a matter will initially be heard before an ALJ. And, as already discussed, the Commission has plenary authority over its ALJs. In *Free Enterprise*, by contrast, the Supreme Court concluded that the Commission lacked such power over the PCAOB's activities, certain of which were, for all practical purposes, entirely outside of the Commission's control. 561 U.S. at 504-05. Moreover, the tenure protections applicable to Commission ALJs are less robust than those that were applicable to the PCAOB. Commission ALJs enjoy ordinary "good cause" tenure protection, 5 U.S.C. § 7521, whereas the standard for removing a member of the PCAOB was "unusually high" and thus more threatening to the President's authority. *Free Enterprise* at 502-03.

Finally, the Executive Branch's use of tenure-protected ALJs for nearly seventy years establishes a "gloss" on the Constitution that supports the current removal framework. *See Dames & Moore v. Regan*, 453 U.S. 654, 686 (1981). Unlike the PCAOB, which was only a few years old when first challenged, Commission ALJs have operated under a removal framework similar to that which currently applies for almost seven decades.

For all of these reasons, these proceedings do not violate Article II.

VI. SIGNIFICANT SANCTIONS ARE IN THE PUBLIC INTEREST

Significant sanctions against Bebo are warranted to penalize her for her fraud and to deter other corporate executives from engaging in misconduct. The relevant factors support substantial sanctions given that Bebo: acted with scienter, engaged in an egregious scheme for over three years, did so from the highest possible corporate position, and has refused to

recognize *any* wrongful nature to her conduct. *See Steadman v. SEC*, 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds,* 450 U.S. 91 (1981).

The Court should order disgorgement of Bebo's discretionary bonuses to prevent Bebo from being unjustly enriched and for "the deterrent impact this action might have in furthering future compliance with the Securities Exchange Act." *SEC v. Teo*, 746 F.3d 90, 108 (3d Cir. 2014). Disgorgement is appropriate so long as Bebo's misconduct was one cause of her pecuniary gains. *Id.* ("[W]hether the Appellants' profit resulted directly—from a causal perspective—from the wrongdoing or from the operation of dumb luck is not dispositive on the question of whether it is proper and fair to regard those profits as tainted by the wrongdoing.").

At the hearing, the director witnesses, who were responsible for determining Bebo's salary and bonus, consistently testified they would not have awarded her a discretionary bonus had they known she was engaged in fraud. (Tr. 653:22-655:1, 2659:11-23, 2850:5-2851:3). Thus, Bebo's deception allowed her continue to reap discretionary bonuses that would have been withheld had her scheme been revealed. In *SEC v. Black*, which Bebo cites in support of her legal arguments, (Resp. Br. at 215), the court ordered disgorgement in these very circumstances. 2009 U.S. Dist. LEXIS 37309, *5-15 (N.D. Ill. Apr. 30, 2009).

In an attempt to avoid third-tier penalties, Bebo claims that substantial losses have not been incurred. That is untrue. ALC incurred the following multi-million dollar losses stemming from Bebo's conduct:

- ALC paid $34 million above fair value to purchase the Ventas facilities, which Grant Thornton verified were "damages as a result of occupancy rates falling significantly below required covenant occupancy rates." (Ex. 3369, pp. 7-8).

- ALC paid Milbank approximately $1 million to investigate the whistleblower allegations that Bebo's use of employees in the covenant calculations was a "sham." (Tr. 671:4-9).

- ALC paid $12 million when it settled with the investors who sued it and Bebo for the false statements in ALC filings that ALC was in compliance with the Ventas covenants. *Pension Trust Fund for Operating Eng'rs v. Assisted Living Concepts, Inc.*, Case No. 12-C-884-JPS, Docket No. 70-1 (E.D. Wis. Sept. 6, 2013).

- Pursuant to the indemnification provisions of its bylaws, ALC has paid the significant legal expenses incurred by ALC's officers and directors, including Bebo, in the course of this litigation and the investigation that preceded it. (Ex. 137, pp. 13-18).

Beyond directly causing ALC to incur many millions of dollars in actual losses, Bebo also created the risk of substantial loss to ALC and its investors. Indeed, had the full scope of Bebo's fraud been known to Ventas or investors prior to ALC's 2013 acquisition, the losses incurred could have been much greater.[43]

Similar considerations support the imposition of an officer and director bar. Bebo committed her multiyear fraud from the highest possible corporate position. While Bebo claims that she has "effectively been barred from her profession for years," there has been no evidence that Bebo has even *attempted* to find a job since collecting her multimillion dollar settlement from ALC in late 2013. Nor would a bar prohibit Bebo from being employed in the assisted living industry, or any other industry. Rather, a bar would serve to protect investors by ensuring that Bebo cannot hold a leadership position at a publicly traded company.[44]

In summary, disgorgement, substantial penalties, and an O&D bar are warranted because Bebo violated the high standards to which public company CEO's are rightfully held, and to indicate to other executives that similar misconduct will not go unpunished.

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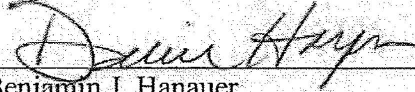
[43] To the extent Bebo asserts that any penalty should be mitigated by a purported inability to pay, the Court should consider Bebo's receipt of nearly a million dollars a year in compensation during the relevant period, and an additional multi-million dollar payment from ALC when it settled Bebo's employment suit in 2013. (Ex. 1173; Stipulations filed Apr. 15, 2015, ¶¶ 13-15).

[44] The primary case Bebo cites in arguing against an O&D bar, *SEC v. Nocella*, is inapposite. In that case, the court found that the defendants conduct was not egregious, they lacked an intent to defraud, and there was "no extreme departure from business judgment." 2014 U.S. Dist. LEXIS 111554, *5 (S.D. Tex. Aug. 11, 2014). The same cannot be said about Bebo.

Dated: August 28, 2015

Respectfully submitted,



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UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-16293

In the Matter of **LAURIE BEBO, and** **JOHN BUONO, CPA,** **Respondents.**	**CERTIFICATE OF SERVICE**

Daniel J. Hayes, an attorney, certifies that on August 28, 2015, he caused a true and correct copy of the foregoing The Division of Enforcement's Post-Hearing Reply Brief to be served on the following by overnight delivery and email:

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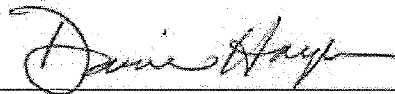

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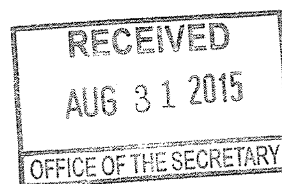

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August 28, 2015

VIA UPS NEXT DAY AIR

Brent J. Fields, Secretary
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Re: ***In the Matter of Laurie Bebo and John Buono, CPA***
(AP File No. 3-16293)

Dear Mr. Fields:

Enclosed please find the paper copies of the Division's Post-Hearing Reply Brief for filing in the above-referenced matter, including the Certificate of Service.

Sincerely,

Daniel J. Hayes

Enclosures

Copies to: Hon. Cameron Elliot, ALJ
Mark Cameli, Esq.
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