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The Honorable Jason S. Patil
Administrative Law Judge
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Dear Judge Patil:

Re: *In the Matter of Laurie Bebo and John Buono, CPA*, AP File No. 3-16293

Respondent Laurie Bebo provides this submission pursuant to the Court's email requesting/authorizing the parties to file letter briefs (not to exceed 5 pages) regarding the potential impact of the United States Supreme Court’s decision in *Liu v. SEC*, No. 18-1501, 2020 WL 3405845 (June 22, 2020).

As set forth in Bebo’s original post-hearing briefing in this matter, even under the then-existing state of the state of the law regarding disgorgement, the Division’s claim that this Court or the Commission could order Bebo to disgorge her entire discretionary bonus paid for work she performed in 2009, 2010, and 2011 was without precedent and legally improper. (*See, e.g.* Bebo’s Post-Hearing Brief at 272-79; Bebo’s Post-Hearing Reply Brief at 96-101.)

This was for many reasons, but namely that, even under pre-*Liu* precedent, the government was required to establish a clear causal nexus between the asserted unjust enrichment or ill-gotten gains and the alleged fraudulent conduct. (*See, e.g.,* Bebo’s Post-Hearing Reply Br. at 96-97 citing *SEC v. Resnick*, 604 F. Supp. 2d 773, 783 (D. Md. 2009) (denying disgorgement where evidence failed to demonstrate that defendant's salary was causally related to unlawful conduct); *SEC v. Jones*, 476 F. Supp. 2d 374, 386 (S.D.N.Y. 2007) (denying request for disgorgement where "the Commission [was] unable to set forth any evidence of specific profits subject to disgorgement"); *SEC v. Todd*, 2007 WL 1574756, at *18 (S.D. Cal. May 30, 2007) ("The SEC's position that Defendants should give up their salaries for the time at issue is untenable—it is basically a statement that because of several business decisions or errors, nothing else they did during that period matters. This is punitive.") overruled on other grounds by *SEC v. Todd*, 642 F.3d 1207 (9th Cir. 2011); *SEC v. Cohen*, 2007 WL 1192438, at *21 (E.D. Mo. Apr. 19, 2007) ("The SEC has not shown that defendant obtained any ill-gotten gains or unjust enrichment from his actions of falsifying the books and records concerning the

[subject] transactions. Furthermore, the Court is not persuaded that defendant benefited through bonuses, salary, or stock sales from such insignificant and immaterial acceleration of revenues."); *SEC v. Better Life Club of Am., Inc.*, 995 F. Supp. 167, 179 (D.D.C. 1998) ("Because disgorgement is so specifically aimed at ill-gotten profits, it is only to be exercised over property 'causally related to the wrongdoing.'").)

Although the Division's argument in favor of imposing a disgorgement remedy related to Bebo's cash bonuses was already balanced on the most slender of reeds, the Supreme Court's *Liu* decision significantly narrowed the scope of the disgorgement remedy available to the Division and the Commission. After *Liu*, disgorgement of generally-described ill-gotten gains or unjust enrichment can no longer be pursued by the government. Rather, "to avoid transforming an equitable remedy into a punitive sanction," courts should, as some have in the past, "restrict[] the remedy to an individual wrongdoer's net profits to be awarded for victims." *Liu*, 2020 WL 3405845, *5. The Court repeatedly stressed that disgorgement remains equitable (and permissible), only where it is employed to recover ill-gotten *profits* directly obtained by the wrong-doer from investors as a result of the alleged fraud:

- "Equity courts have routinely deprived wrongdoers of their net profits from unlawful activity…" *Id.* at *5.
- "No matter the label, this profit-based measure of unjust enrichment, reflected a foundational principle: [I]t would be inequitable that [a wrongdoer] should make a profit out of his own wrong." *Id.* (internal quotations omitted, alterations in original).
- In order to prevent equitable "profits remedies" from becoming a penalty, the "profits remedy often imposed a constructive trust on wrongful gains for wronged victims." *Id.* at *7.
- "Equity courts also generally awarded profits-based remedies against individuals or partners engaged in concerted wrongdoing, not against multiple wrongdoers under a joint-and-several liability theory." *Id.*
- Courts must limit "awards to the net profits from wrongdoing, that is, the gain made upon any business or investment, when both the receipts and payments are taken into the account." *Id.* (internal quotations omitted).
- "[T]he SEC's equitable, profits-based remedy must do more than simply benefit the public at large by virtue of depriving a wrongdoer of ill-gotten gains." *Id*. at *10.

In the end, the Court reasoned that Congress granted the Commission the ability to recover this type of profit-based equitable remedy, but no more. *Id.* at *8 ("By incorporating these longstanding equitable principles into § 78u(d)(5), Congress prohibited the SEC from seeking an equitable remedy in excess of a defendant's net profits from wrongdoing."). However, the Court noted that, at the urging of the Commission, courts had strayed from the

permissible profit-based remedy in a manner that "test[ed] the bounds of equity practice," and ultimately exceeded them. *Id.*

The Division's on-going attempt to seek disgorgement in this case represents one of those efforts to stretch the concept of equity and the concept of a "profit-based remedy" beyond the breaking point. Here, the Division has not shown—and cannot show—that Bebo profited as a direct result of any alleged securities violations. Rather, the Division merely argues that the entire amount of Bebo's bonuses from the years 2009 through 2011 should be disgorged on the theory that earlier discovery of her alleged misconduct would have resulted in her termination, thereby rendering *any compensation* she received the product of her "fraud." (Division Post-Hearing Brief at 57.)

However, under *Liu* this is an improper theory of disgorgement because it is disconnected from any sort of attempt to base it on the amount of "profit" derived from the alleged violations. This is highlighted by the manner in which the bonuses were actually awarded. Under ALC's Cash Incentive Compensation Program, executives like Bebo were eligible for cash bonuses if ALC met a certain threshold of financial targets for "Adjusted EBITDAR"[1] and "Adjusted EBITDAR margin percentage (defined as total revenues divided by 'Adjusted EBITDAR')." (*See, e.g.* ALC's 2011 Definitive Proxy Statement discussion executive compensation for 2010, Ex. 2073-0020). If ALC achieved 90% or greater of the budgeted Adjusted EBIDTAR and Adjusted EBIDTAR margin percentage, Bebo and other executives would be eligible for the cash bonus award. (*Id.*) Based on 2010 reported financial results, ALC came within 99.75% of the targeted profitability measures. (*Id.*) The compensation committee then simply voted to award Bebo and other executives at that level under the plan. (*Id.*) In 2011, ALC achieved 102.5% of the financial metrics and so ALC's compensation committee approved cash payments based on those results in March 2012.[2] (ALC's 2012 Definitive Proxy Statement, Ex. 2074-0015.)

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[1] "Adjusted EBITDAR" is defined as "net income from continuing operations before income taxes, interest expense net of interest income, depreciation and amortization, non-cash equity-based compensation expense, transaction costs, non-cash, non-recurring gains and losses, including disposal of assets and impairment of goodwill and other long-lived assets and impairment of investments, and rent expenses incurred for leased assisted living properties…" (Ex. 2073-0020.)

[2] Notably, ALC's board compensation committee approved the bonus at the same March 6, 2012 meeting where its CFO, John Buono, and Bebo explained (again) the details of the employee leasing program. (Ex. 1229-0003.) In the days following that meeting, the directors received the spreadsheets detailing how ALC room rentals for employees were used to calculate the covenants, including the names associated with those rooms. (Ex. 329; *see also* Tr. 588-89; Ex. 327.) Yet, after receiving this information, the board continued to approve the cash incentive bonus for Bebo and Buono, as reflected in the definitive proxy statement dated March 23, 2012. (*See* Ex. 2074-0003, -0015.)

As noted in earlier briefing, it is undisputed that all of the financial metrics of ALC reported to investors (and utilized in the Adjusted EBIDTAR calculation), were true and accurate. ALC's use of the 997 account made sure that all outward financial reporting eliminated any of the effects of the intercompany transactions related to the Ventas facilities. (*See also* Tr. 4167:19-4170:12.) Had ALC's actual financials been inflated and, thus, affected the amount of the bonus, that might be the type of profit-based remedy that the Supreme Court had in mind when analyzing the appropriateness of disgorgement in *Liu*.[3]

But the Division's disgorgement theory is a tiger of different (and unactionable) stripes. It has *nothing* to do with an attempt to recover an equitable, profit-based recovery, and instead is precisely designed to impose a penalty on Bebo. With no basis to assert an actual profit-based disgorgement remedy that would serve Congress' original purpose of providing that remedy to the Commission, the Division's theory is unabashedly based on imposing a penalty. This is clear based on the Division's discussion of its disgorgement argument in its August 2015 post-hearing reply brief:

> 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.")

(Div. Post-Hearing Reply Brief at 58 (emphasis added).) The Division's reasoning, and the precedent upon which it is based, cannot be squared with the Court's decision in *Liu*.

As to the second issue identified in the Court's June 24 email, the *Liu* decision does require that any disgorgement be tied directly to the profit obtained and the concurrent loss sustained by an investor victim. But in this case, neither of these conditions are present. As discussed above, Bebo's cash bonus was not effected in any way by the alleged securities law violations. Moreover, she achieved those bonuses based on a host of factors, including how hard she worked at her job on the strategic vision and operational and financial effectiveness of ALC.

[3] Similarly, had Bebo sold ALC stock during the alleged period of wrongdoing, and realized a profit on those sales because the stock was inflated as a result of misrepresentations, disgorging that profit might also be the type of profit-based remedy contemplated by the Supreme Court. But as noted in Bebo's prior briefing regarding scienter, Bebo did not sell any ALC stock during the relevant time period.

There is no way to "net" those types of "expenses" from the cash bonus awarded, as required by *Liu*. Similarly, ALC and its shareholders received the value of those services, hard work, and expertise that resulted in those bonuses being paid. Consequently, there is no "victim" from whom the purported ill-gotten "profits" were obtained in the sense this is discussed in *Liu*. And it would be difficult, if not impossible, for the government to distribute any disgorgement proceeds to ALC's former shareholders, since it has not had public shareholders since it was sold to a private equity firm in 2013.

Finally, and unrelated to the *Liu* decision, the Division's theory is not even consistent with the facts adduced in this case. The Division can point to no evidence showing that any compensation Bebo received was specifically tied to her alleged misconduct in connection with the Ventas lease covenant calculations. That is because Bebo's compensation was not tied to the Ventas Lease or covenant compliance, and there is no evidence that the employee leasing practice inflated her compensation in any way. The best the Division can do is point to the testimony of certain members of ALC's Compensation Committee and Board of Directors, who testified years after the fact that they *personally* would not have voted to award Ms. Bebo a bonus if they had been aware of her conduct at the time. (*See, e.g.,* Div. Post-Hearing Brief at 57 (citing Tr. 653:22-655:1; 2659:11-23; 2850:5-2851:3).)

Of course, as explained in Bebo's Post-Hearing Brief, such claims cannot withstand serious scrutiny in this case, particularly when Buono was not only *not* terminated upon discovery of the employee leasing practices, but was actually provided salary increases and bonuses. (*See* Bebo Post-Hearing Brief at 206 (citing evidence).) ***And this followed completion of the Milbank investigation***. (*See also, supra,* note 2.) Moreover, in settling Bebo's arbitration claim against the company for wrongful termination, it withdrew any termination for Cause and paid Bebo severance owed under her contract, thanking her for her service to the company in the process. (Ex. 1173, 2066.)

For all the above reasons, we think the *Liu* decision ought to represent the death knell to the Division's disgorgement claim—even prior to *Liu*, it rested on a faulty legal theory and unsupported factual assertions. Moreover, the Court need not even address the disgorgement or other issues related to potential sanctions because, for all the reasons explained previously, the Division's claims ought to be dismissed on the merits.

Thank you for your continuing attention to this matter.

Respectfully submitted,

Ryan S. Stippich

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