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.

RESPONDENT LAURIE BEBO'S SUPPLEMENTAL POST-HEARING REPLY BRIEF

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Respondent Laurie A. Bebo, by and through her counsel, Reinhart Boerner Van Deuren s.c., hereby respectfully submits this Supplemental Reply Brief Pursuant to the Court's August 28, 2019 Order and requests that the Court conclude that the claims set forth in the December 3, 2014 Order Instituting Proceedings ("OIP") filed by the Securities and Exchange Commission's ("SEC's" or the "Commission's") Division of Enforcement (the "Division") be dismissed in their entirety.

INTRODUCTION

The Division's supplemental post-hearing reply brief continues to repeat the same pre-determined narrative and "facts"—the same factual exposition set forth in its original pre-hearing brief, its original post-hearing brief, and its original post-hearing reply brief. Because the Division's theory of liability was a pre-determined one, any facts that do not fit the narrative surrounding the theory—whether in the form of documents, testimony of its own witnesses, or statements made by witnesses like John Buono to the Division in hours of interview sessions—are simply ignored or obfuscated.[1]

On many occasions, the Division's supplemental post-hearing reply brief contains blatantly inaccurate statements of the evidence. By way of example only, here are a few. *First,* the Division asserts that ALC's CFO, John Buono, testified Joe Solari at Ventas "did not agree to anything" regarding employee leasing on the Solari Call. (Div. Supp. Post-Hearing Br. at 9; Div. Post-Hearing Br. at 13, citing Tr. 2344:18-2345:5.) Critically, Buono clarified his testimony, describing how, through is work in the Division's cooperation program, he came to realize that the agreement ALC had was not as good as he initially thought. Consequently, he unambiguously testified that, during the relevant time period (2009 to 2012), that he believed,

[1] For a complete discussion of the various broad assertions and inaccurate factual narrative, *see* Respondent's Post-Hearing Reply Brief at pages 17 through 47, and Respondent's Post-Hearing Brief at pages 9 through 26.

based on the Solari Call and Solari Email, that ALC and Ventas had an agreement to include room rentals related to employees in the covenant calculations. (Resp't Post-Hearing Br. at 78-80, citing Tr. 2489-90, 2495-96, 4645.) Indeed, Buono acknowledged on cross-examination that from 2009 to 2012 he understood ALC and Ventas had an agreement based on the Solari Call and Email, but his impression changed based on his interaction with the Division since: "So there's been additional information after that time [May 8, 2012] that would lead me to believe that maybe this [Solari Email] *wasn't as good of an agreement as we would have hoped.*" (Tr. 4645.)

Second, the Division claims that Ventas "never responded" to the "proposal" that ALC would utilized employee leasing. The notion that it was a "proposal" is contradicted by the Solari Email itself, which states, "we are *confirming* our notification of our rental of rooms to employees." It was not a proposal at all, but confirmation of an ongoing practice and that ALC would engage in broader "room rentals related to employees" going forward. More importantly, Ventas did respond to the Solari Email. The Division misleadingly claims that there was no response at all. The fact is Bebo saw that Ventas circulated the email to various personnel in their asset management department. When Ventas responded, it raised no concerns about the "confirmation" of ALC's use of employee leasing, but asked to discuss a separate aspect of the email. (Resp't Post-Hearing Br. at 86-89.) Thus, from Bebo's perspective, every senior executive and key Ventas employee with direct responsibility for the CaraVita Facilities and the Lease was aware of ALC's confirmation of the company leasing rooms related to employees as occupants.

Third, the Division asserts that Buono corroborated board of director testimony that "including employees in the covenant calculations did not come up at [a February 2009] meeting

and that the board did not approve the practice." (Div. Supp. Reply Br. at 11.) This is false both as to the February 2009 board meeting and the board's knowledge and approval generally, including by the Division's own records of Buono's statements to its lawyers during several proffer sessions. Just a few of these Buono statements, include:

- "JB said the directors who knew about the inclusion of employee occupants in the covenant calculations were Rhinelander ('he knew exactly what was going on'), Hennigar (because Rhinelander and Hennigar spoke frequently), Malen Ng (who had discussed the topic with Melissa Koeppel and JB), Derek Buntain (who as described below asked Bebo and Buono to add additional employees into the covenant calculations to make it appear that ALC was not as close to missing the covenants) and Alan Bell." (Ex. 2117, pp. 1-2.)

- After presenting certain options to meet the covenants in early 2009, "JB said that Rhinelander had a discussion with the BOD [board of directors] and then told Bebo that the BOD preferred including employee occupants in the covenant calculations." (*Id.*)

Buono also testified specifically that Rhinelander, Ng, and Buntain (among potentially others) knew about and approved the fact that ALC was using employee rooms in the covenant calculations. (Tr. 4633-34.) Similarly, Buono testified about an August 2011 board meeting where Bebo, Buono, and the Board discussed the use of employee leasing to meet the Ventas lease covenants. Although Buono feigned he could not recall the specifics (Tr. 4629-35), this discussion was clear in the Division's own notes of his statements in proffer sessions:

> "JB recalls that Bebo told the Board that ALC was good on the employee leasing, that we would have enough going forward to keep it going. JB said he doesn't recall discussing the amount of employees involved. He recalls the conversation was more along the lines of do we have enough employees and are we confident that the [employee leasing program] will continue."

(Ex. 2122, p. 8.)

Fourth, regarding this same meeting where a comment letter from the Commission was discussed, the Division claims it is significant that an alternative draft of ALC's response was not shared with the board, Grant Thornton, or outside counsel and Bebo supposedly "conced[ed]"

that it was not shared. (Div. Supp. Post-Hearing Br. at 19.) This is false again, Bebo did not "concede" that the alternative had not been shared, rather she affirmatively testified that it was her belief that it had been shared but she did not know for sure.[2]

Again, these are just a few of the continued examples of the Division's continued pattern of misconstruing the facts to fit its predetermined narrative. As noted (*supra* note 1) Bebo's original post-hearing briefing has catalogued the other misleading and unsupported statements contained in the Division's briefing. It is unfortunate that the pattern continues to this day with respect to the Milbank interview memoranda that Bebo was able to obtain since the earlier hearing in this matter. As described in section __, below, the Division again misconstrues the statements Bebo made, as set forth in the interview memoranda, and Bebo's prior testimony in order to create inconsistencies that do not exist.

Furthermore, the Division's attempt to use *In re Petrobras Sec. Litig.*, 862 F.3d 250, 255 (2d Cir. 2017) to limit the importance of Bebo's expert's event study on the issue of materiality and bolster the inherent materiality weakness in the Division's case fails. *Petrobras* did not effect a change in the law with respect to the importance of event studies to determine the merits of materiality and other related issues in securities litigation. Indeed, the Division continues to

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[2] Here is the actual testimony:

> Q: So this alternative letter, Quarles & Brady didn't know about the alternative letter, correct?
> A: *I expected they did.*
> Q: ...[Y]ou didn't know one way or the other whether Quarles & Brady knew about the alternative letter, correct?
> A: That's correct...
> Q: And Grant Thornton didn't know about the alternative letter.
> A: I guess I can't – I can't speak to that. I know that we worked with those folks on the – on the letter that we did send, *and presumably John would have worked with those folks on the alternative letter*, but I can't – I can't speak to that.
> Q: Right. You have no personal knowledge of whether or not Grant Thornton got the alternative letter.
> A: I believe that's correct.

(Tr. 2110-11 (emphasis added).)

use event studies and tout the importance of them in other federal court litigation. Moreover, in cases in the Second Circuit since *Petrobras*, event studies continue to be used as the essential, empirical evidence in establishing materiality or the lack thereof.

ARGUMENT

I. The Division's Reliance On *Petrobras* Highlights The Gaping Materiality Hole In Its Case.

In its supplemental brief, the Division argues that the Second Circuit Court of Appeals "roundly rejected" the contention that expert testimony regarding an "event study" is required in a securities fraud case. (Div. Supp. Post-Hearing Br. at 34.) In addition, the Division asserts, without any of its own expert testimony and in direct contradiction of Bebo's expert's unchallenged expert testimony regarding materiality, that his event study actually supports the Division's case. (*Id.*) The Division's argument is erroneous both factually and as a matter of law. Bebo addresses each in turn.

A. Professor David Smith's Event Study.

Professor David Smith is a professor of commerce at the University of Virginia and a Director of the MicIntire Center for Financial Innovation. (Ex. 2186, p. 3.) He earned his doctorate degree of philosophy in finance at the Kelley School of Business at Indiana University. (*Id.*) Prior to becoming a professor at the University of Virginia he was an economist in the International Finance Division of the Federal Reserve Board in Washington, D.C. and, before that, an assistant professor of finance at the Norwegian School of Management in Oslo, Norway. (*Id.*)

Professor Smith's qualifications to conduct the event study, and the methodologies used in his statistical analysis utilized in his report and testimony, are unchallenged. The Division provided no expert testimony of any kind to challenge his opinions.

An event study is a well-established method used by financial economists to determine whether public release of new, firm-specific information is important to market participants—*i.e.*, investors—and whether it is important in a positive or negative way. (Ex. 2186, pp. 10-11.) It is based on the economic theory that stock prices rapidly adjust to reflect new and unexpected information relevant to the value of the stock. (*Id.* at 13-14.) If the new information is, in the eyes of investors, positive for the value of the company, the market will cause the price of the stock to increase in a statistically significant manner. (*Id.* at 13.) If the new information is, in the eyes of investors, negative for the value of the company, then the market will cause the price to decline in a statistically significant manner. (*Id.*)

Professor Smith concluded that disclosure of allegations of improper calculations of occupancy rates and coverage ratios under the Ventas Lease (referred to by Professor Smith as the "Financial Covenant Allegations") in ALC's Form 8-K on May 14, 2012 did not cause a statistically significant change in ALC's stock price after accounting for market and industry factors through his event study. (*Id.* at 16.) This is the first time that investors learned of the allegation that ALC may have "submitted fraudulent information [to Ventas] by treating units leased to employees as bona fide rentals by third parties and, therefore, may not have been in compliance with the minimum occupancy covenant and coverage ratio covenants."[3] (*Id.*; *see also* Ex. 2076, p. 2.)

Following the disclosure of the Financial Covenant Allegations for the first time on May 14, 2012, "ALC's stock price declined $0.37 or 2.26%. Measured relative to the benchmark based on the returns of the NYSE and Peer Group, the abnormal return on ALC stock on this day was -0.40% and was not statistically significant." (Ex. 2186, p. 16.) Consequently, "the lack of

[3] The Division's expert, John Barron, confirmed that, in his review of the materials in this case, this is the first time he observed this allegation by Ventas about ALC fraudulently treating units leased to employees as bona fide rentals to third parties. (Tr. 1666.)

a statistically significant price impact is inconsistent with the market interpreting the Financial Covenant Allegations as negative news." (*Id.*) And Professor Smith "conclude[d] that there is no evidence that the information disclosed on May 14, 2012, including the Financial Covenant Allegations, had an impact on the ALC stock price." (*Id.* at 17.)

B. The Division's baseless attempt to twist Professor Smith's conclusion, without an expert or event study of its own.

In its Supplemental Post-Hearing Brief, and as it has tried (and failed) previously to do, the Division seems to endorse Smith's expertise, credibility and event study methodology, but attempts to twist the conclusion of his study by focusing on the wrong date. The Division contends that a different date—May 4, 2012—should be looked at. On that day, ALC disclosed the Milbank investigation into "irregularities" pertaining to the Ventas Lease. But ALC also made several other significant disclosures, as Smith testified, that resulted in a statistically significant decline the following day. Only by substituting their own layman's judgment for that of the expert, Smith, does the Division claim that his event study somehow demonstrates that the disclosure about compliance with certain "operating and occupancy covenants" in the Lease was material. (Div. Supp. Br. at 34.)

However, at trial, Smith provided his expert opinion and reasoned basis for the opinion that the May 4, 2012 date is not relevant to the analysis. The unsupported statement by the Division's counsel in a post-hearing brief cannot trump the uncontradicted and reliable testimony of Professor Smith.

Here, the first and only public, corrective disclosure occurred on May 14, 2012. Various public disclosures and interactions between Ventas and ALC in the period leading up to May 14th confirm this. On April 26, 2012, Ventas filed a lawsuit against ALC. (Ex. 2075.) The lawsuit alleged that notices from state regulators to ALC had identified numerous deficiencies

with the respective CaraVita Facility's operations which are "jeopardizing the health, safety, and welfare of the residents." (Ex. 2186, p. 9.) It contained no allegation related to Financial Covenant Violations.

On May 3, 2012, approximately ten minutes before the market closed, ALC put out a one line press release that it would delay its Q1 2012 earnings announcement and conference call with analysts.[4] (Exs. 2081; 2186, p. 16.) ALC's stock shot up 8.31% in the last seven minutes of trading on May 3 because it was well-established in the market that ALC was trying to sell the company. (Ex. 2186, p. 16 n.59; Ex. 2130 (January 4, 2012 e-mail from CEO of Washington assisted living company stating "news around town is ALC is going to dispose all of their assisted living assets across the country"; Bebo, Tr. 4495.) The following morning ALC issued the May 4 disclosure upon which the Division focuses. In that Form 8-K, ALC disclosed: (a) the fact that it had not postponed its earnings release because there was good news about the sale of the company; (b) the Ventas lawsuit related to alleged defaults for regulatory violations; and (c) that ALC's Board had decided "to investigate possible irregularities in connection with the Company's lease with Ventas." (Ex. 2075 (May 4, 2012 Form 8-K).)

On May 4, 2012, Ventas sent another non-public default notice to ALC alleging that it violated the reporting obligations under Section 25 of the Lease because it failed to timely provide actuarial reports, regulatory deficiency reports, regulatory notices, and cost reports. (Pet. for Review, Ex. A.) The default notice was not made public, but, in any event, there was no allegation in the letter that any of the reporting violations related to the financial covenants in any way.

[4] Unbeknownst to the market, ALC had received the whistleblower letter from Dan Grochowski regarding his concerns about ALC's Lease compliance reporting to Ventas. Although Bebo also did not know about Grochowski's letter, she was concerned that the market would misinterpret the press release as an indication that ALC had reached a deal to sell the company. (Resp't Post-Hearing Br. at 150-52.)

On May 9, 2012 Ventas sent another non-public default notice to ALC asserting a host of new alleged breaches of the Lease. (Ex. 355; Doman, Tr. 347-50.) The default notice alleged that ALC improperly attempted to surrender a state license, regulators were acting to revoke CaraVita Facility licenses, ALC failed to give timely notice of a fire, and proceeded with repairs from the fire without pre-approval from Ventas, and "[a]s described in our letter dated May 4, 2012, Tenant has not complied with all of its reporting obligations pursuant to Section 25 of the Lease." (Ex. 355 at 5-6; Tr. 348-49.)

In the same non-public notice, Ventas included a separate allegation related to alleged violations of the financial covenants for fraudulently including in the covenant calculations "treating units leased to employees as bona fide rentals by third parties." (Ex. 355 at 5.) In connection with the financial covenant allegation, the default notice contains no reference to this constituting a violation of Section 25 reporting requirements.[5]

The next day, on May 10, 2012, Ventas filed a motion to amend its complaint against ALC, with the proposed amended complaint attached. (Ex: 2186 at 10.) Ventas included all of the allegations from the May 9 letter described above, *except* for the financial covenant allegation. (Ex. 1194; Ex. 2076; Division Pre-hearing Br. at 18 n. 5 (stating "[r]ather than referencing the May 9 letter alleging fraud against ALC, paragraph 53 of the OIP incorrectly alleges that, after receiving ALC's request for the release, Ventas moved to amend its complaint against ALC to include allegations of fraud relating to ALC's inclusion of employees in the covenant calculations. The Division apologizes for this mistake.").)

[5] Notably, when this letter was received by ALC, its auditor had a discussion with two board members about the financial covenant allegations. In that conversation those board members stated that ALC's "position is that this letter is posturing. Quarles & Brady [ALC's outside counsel] has drafted a letter in response. [Ventas] Statements are false and misleading but has not been mailed yet due to ongoing negotiations." (Tr. 3459-60; Ex. 1880 at 4.)

Even though the amended complaint did not include Financial Covenant Allegations, ALC included a description of the Financial Covenant Allegations from the May 9 default notice in its Form 8-K disclosed to the market on May 14, 2012. For the first time, ALC publicly disclosed that Ventas had alleged that ALC had been fraudulently calculating the financial covenants by treating units rented to employees as bona fide rentals to third parties. (Ex. 2076.)

The Division errs by conflating public disclosure of allegations of financial covenant violations with facts and circumstances out of the public view. Smith appropriately conducted his analysis from the point of view of what the investing public would or would not have known during this time period. Specifically, he concluded that there was no public indication that the May 4 disclosure of an investigation into "irregularities" in connection with the Lease related to Financial Covenant Allegations. Under cross-examination, he testified:

A	There's no public disclosure that connects that statement of possible irregularities with the company's lease to the financial covenant allegations. There's no -- certainly it's not in the [May 4th] 8-K. If you look at the press analysis, you look at the analyst reports that follow this, everybody that's looking at that sentence is not making any connection to anything having to do with financial covenants. And if anything, they make the natural connection that the investigation into the lease irregularities have to do with the allegations and the alleged breaches under the Ventas lawsuit. There's nothing here that says, hey, financial covenant allegations. Nothing.
Q	You are aware that is what that's a reference to?
A	I've had the -- you know, the luxury of, you know, knowing what -- seeing that there was a whistleblower letter behind the scenes that may have prompted this investigation. I don't know for sure that that's the prompting, but the more important point is from an investor's perspective, that—those irregularities probably have to do with the—an investigation into the—the pieces of the Ventas lawsuit.... *All I can do is look at every press report, look at every analyst's report,*

	look at the disclosures by the companies themselves including Ventas, who has never disclosed at any filing alleging there was a financial covenant allegation, that there was a financial covenant allegation particularly that there was a link between the financial covenant allegations and this investigation. The natural way—and also the analysts that commented on this tied the investigation to the Ventas lawsuit.

(Tr. 3645-47 (emphasis added).) Smith went on to describe the "copious information" in the public realm discussing the May 4 disclosure, and "nobody makes that connection" of the investigation to Financial Covenant Allegations. (Tr. 3645-47.) The Division's opposite conclusion must be rejected as it is contrary to the evidence presented, and entirely speculative.

Furthermore, Professor Smith explained that most of the decline on May 4 cannot be tied in any way to the disclosure of an investigation into "irregularities" pertaining to the Ventas Lease. Rather, the decline was caused by the correction of the market's perception that good news about a sale of the company was going to be released:

Q	And you opined -- turning to the next page, Byron, that there were essentially two factors that caused this stock price drop [on May 4th]; is that right?
A	Yes.
Q	One, which you talk about in the first three or four paragraphs here, was the delay in releasing the Q1 2012 earnings late in the day on May 3rd; is that right?
A	That's correct.
Q	And then the other factor you said drove the stock price decline was the actual content of the Form 8-K itself that was filed; is that right?
A	It's the -- well, it's the information that investors get from the content of that lawsuit, yes.
Q	And that 8-K and the information the investors got from that 8-K included this disclosure revealed the Ventas lawsuit, as well as ALC disclosing its internal investigation into irregularities with the Ventas lease; is that right?
A	Yes.
Q	And to support that, you even cited, going to the next page, page 17, in paragraph 58, you cite The Senior Care Investor newsletter that made reference to that 8-K; is that right?
A	Yes.

Q	And that Senior Care Investor Newsletter basically stated that the delay in the earnings release and the subsequent negative disclosure of the lawsuit and the internal investigation was not expected by investors and caused that stock price drop.
A	Yeah, and let's be careful that we have to set this up based on our understanding of what happened on May 3rd and what happened to the stock price on May 3rd. So to judge the magnitude of the fall on May 4th, we first have recognize that there is a big bump in the stock price on May 3rd in the last seven minutes of the trading day following the disclosure of -- following the fact that -- following the announcement by ALC that they are going to suspend their earnings announcement. So what happened at the end of the day on May 3rd was when the company announced that they were suspending their earnings announcement, the market understood that they were -- the reason they were suspending is because they had news, and the market believed this to be really good news. The stock price shot up by eight percent in a matter of minutes. We can see -- in fact, if we want to turn to Exhibit 8, we can see it very starkly, the stock price doesn't move at all, and then it shoots up. And so when the -- right before the market opened the next day, 9:27 a.m. when the 8-K comes out with the news about the Ventas lawsuit, investors find out it wasn't good news, and so the stock price dropped back down. And this is -- the Senior Care Investor quote actually highlights that. It says, Investors were not expecting negative news, they were expecting positive news, and sent the shares down by 15 percent. And Senior Care Investors, they're speculating, because I think they've already seen there's a decent amount of evidence out there that there's a merger -- or a strong potential that ALC would be acquired, and there were interested bidders out there, and now what Senior Care Investor is saying in that quote is it would seem highly unlikely that a buyer for the company will step forward at this point. That's significant, Mr. Stockwell, for two reasons. One, first, a big part of the observed drop you see on May 4th is just the fact that what investors were expecting on May 3rd didn't happen, didn't transpire. Stock price drops back down at least to the level it was before the announcement occurred, which was I think around $17.70. And then Senior Care Investors is saying now that this lawsuit has come out, there's even less of a chance of there being a merger, and my

	experience with the literature on how stock price reactions -- or how stock prices move around merger rumors is that once the likelihood of a merger declines, the stock price will decline further. So a lot of the -- a substantial part of the stock price movement we see on May 4th is because of the disappointment in what investors thought was going to happen the day before sent stock prices up eight percent; didn't transpire.

(Smith, Tr. 3638-41.)

Even Ventas did not think that the disclosure of irregularities pertaining to the Lease had anything to do with the financial covenants, and the Division's statement to the contrary at page 42 of its brief is false. The Division relies on a motion for expedited discovery that Ventas filed on May 15, 2012 in the lawsuit for the proposition that "Ventas understood [the irregularities] to involve the occupancy covenants." (Div. Br. at 42 (citing Ex. 357).) However, the motion for expedited discovery confirms the opposite of the Division's statement and tracks Professor Smith's testimony:

> To this day, ALC has failed to provide Ventas with any details regarding the scope or subject matter of this investigation or the irregularities concerning the Ventas Lease. Because of the increasing reports of ALC's mismanagement of the facilities, *Ventas fears that the "irregularities" are related to deficiencies in Defendants' operation of the assisted living and/or independent care facilities and the care for the residents therein.*

(Ex. 357, p. 3 (emphasis added).)

The pleading never mentions the financial covenants or ALC's reporting obligations more generally under the Lease. Based on Exhibit 357, it is clear that Ventas believed what they described as "opaque disclosures" (*Id.* at p. 1) did not relate to covenant calculations, but to the under-staffing, problems with resident care and safety, a fire at a facility, and other operational issues that were described in Ventas' complaint.[6] (*See* Ex. 1194, p. 2 (Ventas' amended

[6] The Division also simultaneously impeaches its own witness, Mr. Doman, by eliciting testimony from him on re-direct (and citing it in its Post-Hearing Brief) that the purpose of the motion seeking expedited discovery was to find

complaint alleging that "notices identify numerous deficiencies with the respective ALC Entity's operations which are jeopardizing the health, safety, and welfare of the residents...").)

Finally, the Division posed a hypothetical to Professor Smith, who explained, in response to that hypothetical, why May 4 is irrelevant and May 14, when there was no statistically significant share price decline, was the appropriate date for this case:

Q	And you agree, based on your analysis, that if this 8-K had disclosed the financial covenant allegations, that that would have been a factor in the stock price drop.
A	So the nice thing is I don't have to engage in that hypothetical because there's another day when they actually do disclose the financial covenant allegations and there isn't a negative -- there is not a stock price drop.
Q	Well, let me ask the question again. If this 8-K had disclosed the financial covenant allegations, that would have been a factor in the stock price drop from May 3rd to May 4th?
A	My answer is no because we now know that -- so the problem with distinct -- between separating these three -- four -- if you think about it, two factors. First, the big return, and if not, return dropped below where the price level was the day before they suspended the earnings and shot the stock price up eight percent, one factor. The second factor is the Ventas lawsuit, but contained in the Ventas lawsuit is lots of information about how they're -- how ALC was mismanaging these residential facilities, all right? And then there's the discussion about the internal investigation. I cannot separate how much -- I can give you a very good guess of how big the impact was, the stock price going back down to where it was the day before. That seems pretty reasonable and probably would have dropped further because the likelihood of a merger has declined. Disentangling the other pieces is hard but I don't have to do that because the hypothetical you're asking about was not the facts. The facts were the disclosure -- the financial covenant allegations occurred on May 14th. There were other disclosures on May 14th as well, but the stock price

out more about the use of employees in the covenant calculations. (Div. Br. at 42 citing Doman, Tr. 386.) As there is no indication of the same in the pleading, Mr. Doman testified falsely at trial.

	did not move on that date. So I can sort of say -- take the whole idea of the financial covenant allegations, their impact on stock prices off the table because they weren't part of that May 4th disclosure.

(Smith, Tr. 3643-44.)

Put simply, for the reasons explained by Professor Smith, there is no basis to conclude that any investor could or did interpret the May 4 disclosure of the investigation into "irregularities" with respect to the Ventas Lease as having anything to do with financial covenant allegations. *See also Meyer v. Greene*, 710 F.3d 1189, 1201 (11th Cir. 2013) (holding that disclosure of an investigation is generally not a corrective disclosure because "[t]he announcement of an investigation reveals just that — an investigation — and nothing more"); *In re Almost Family, Inc. Sec. Litig.*, 2012 WL 443461, at *13 (W.D. Ky. Feb. 10, 2012) ("Numerous federal district courts have held that a disclosure of an investigation, absent an actual revelation of fraud, is not a corrective disclosure.") (collecting cases).

C. *Petrobras* is distinguishable, but supports the importance of event studies in securities fraud claims in any event.

Although it may not be the *only* indicator of materiality, it is well-established that the *best* indicator of whether an alleged misrepresentation or undisclosed information is material is to assess the effect disclosure of the information has on the company's share price. *See United States v. Schiff*, 602 F.3d 152, 171-72 (3d Cir. 2010) (noting drop in stock price is widely used as evidence of materiality when the market is efficient); *SEC v. Mangan*, 598 F.Supp.2d 731, 735 (W.D.N.C. 2008) (same). That is because the market "is the most accurate and unbiased measure of whether reasonable investors found the information to be material." *Mangan*, 598 F.Supp.2d at 73.

Indeed "[m]any courts have held that information may be deemed immaterial as a matter of law when the public disclosure of such information has a negligible effect on the price of a

stock." *Id.*; *see also Greenhouse v. MCG Capital Corp.*, 392 F.3d 650, 660-61 (4th Cir. 2004); *Oran v. Stafford*, 226 F.3d 275, 282-83 (3d Cir. 2000); *In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1425 (3d Cir. 1997) (citations omitted); *Grimes v. Navigant Consulting, Inc.*, 185 F.Supp.2d 906, 914 (N.D. Ill. 2002). To be a "corrective disclosure" the disclosure has to reveal the falsity of the prior statements. *Katyle v. Penn Nat'l Gaming, Inc.*, 637 F.3d 462, 473 (4th Cir. 2011) (holding that, to be a corrective disclosure, the new disclosure "must reveal to the market in some sense the fraudulent nature of the practices about which a plaintiff complains"); *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 175 n. 4 (2d Cir. 2005).

Realizing Smith's expert analysis supports a finding of no materiality, the Division argues that the *Petrobras* decision somehow walked back the well-established principle that event studies are the gold standard for evaluating materiality of disclosures about public companies. It did nothing of the sort. *Petrobras* was a private securities fraud class action lawsuit alleging that one of the largest oil companies in the world fraudulently inflated the price of its securities because it hid a multi-year, multi-billion dollar money-laundering and kickback scheme from investors. *c.* The district court certified a class of investors in the case, and the defendants challenged whether that was appropriate. The defendants argued that investors failed to demonstrate that class-wide reliance based on the "fraud on the market" theory established in *Basic, Inc. v. Levinson*, 485 U.S. 224 (1988). *Id.* at 257.

Consequently, unlike the precedent cited above by Bebo, *Petrobras* did not even involve the role of event studies as they pertain to evaluating materiality. Instead, the court was evaluating whether the plaintiff class had satisfied a multi-factor test to establish that the Petrobras securities traded in an "efficient market" such that the fraud-on-the-market presumption of reliance would apply on a class-wide basis. *Id.* at 275-76. Most of the factors

(generally called *Cammer* factors) involve unscientific indicators of market efficiency, such as the size of the daily trading volume, the extent of analyst coverage, whether there are multiple market makers for the stock, the size of the market capitalization of the company. *Id.* at 276. The last factor, "invites plaintiffs to submit direct evidence, consisting of 'empirical facts showing a cause and effect relationship between unexpected corporate events or financial releases and an immediate response in the stock price." *Id.* This, in turn, is almost always done through event studies. *Id.*

The defendants in *Petrobras* argued that the class's expert failed to conduct an adequate event study, and that their own expert's event study showed the stock did not move in an anticipated direction based on good or bad news about the company. Although the plaintiff's study demonstrated that Petrobras's stock reacted to new information about the company, he did not establish that the share price went up based on good news and down based on bad news. *Id.* at 277. In finding the class demonstrated market efficiency and fraud-on-the market reliance, the court reasoned that their "burden is not an onerous one." *Id.* at 278. The court rejected a new rule of law proposed by the defense: that "plaintiffs would only be entitled to the *Basic* presumption after making a substantial showing of market efficiency based on directional empirical evidence alone, irrespective of any other evidence they may have offered." *Id.* at 278-79. The court reasoned that defendants' position would constitute a wholesale re-write of the law, effectively eliminating the other non-scientific, indirect, evidence of market efficiency.

It is within this context, that the court noted that there can be "methodological constraints" and "methodological challenges" in conducting event studies which "counsel against imposing a blanket rule requiring district courts to, *at the class certification stage*, rely on directional event studies and directional event studies alone." *Id.* at 278-79 (emphasis added).

The Second Circuit was not questioning the importance of continued use of event studies, in particular at the merits stage of the litigation, and simply found that where there is conflicting expert testimony and conflicting event studies, at the class certification stage, the district court did not err in certifying the class based on the overwhelming evidence that the other indirect factors supported a finding of market efficiency.

Accordingly, *Petrobras* provides the Division with no support in its attempt to fill the gaping materiality hole in its case. First, unlike *Petrobras*, there is no conflicting expert testimony or conflicting event study evidence in this case. Rather, Smith was the only expert to provide this empirical, "direct" evidence of materiality. His report and testimony were unchallenged, other than the improper attempt by the Division to substitute the layman opinion of its lawyers for the persuasive and reliable expert testimony of Smith, as described above. No thorny methodological challenges have been identified, and Smith clearly and persuasively testified without challenge. Second, as noted, the court did not call into question the importance of event study evidence at the merits stage of the case, and specifically noted "this determination is limited to the district court's class certification order, and is not binding on the ultimate finder of fact." *Id.* at 279. The court clearly contemplated that event studies would be used at the merits stage of the case.

Moreover, the Second Circuit since *Petrobras* continues to emphasize the importance of event studies in proving materiality. *See In re Barclays Bank PLC Sec. Litig.*, 756 Fed. App'x 41 (2d Cir. 2018). In that case the Second Circuit affirmed summary judgment on the merits, based exclusively on the defendant's event study which showed that Barclay's stock did not decline in a statistically significant manner to "the revelation of over £21 billion of what [Plaintiff] characterize[d] as 'hidden' assets." *Id.* at 48. The court then rejected the plaintiff's attempt to

point to other potential corrective disclosures, without "rebut[ting]" the Barclay's expert with expert testimony if his own, and affirmed the grant of summary judgment based on the unrebutted expert testimony and event study.[7] *Id.* at 49.

Similarly, the Division continues to itself utilized and endorse the importance of event studies in proving or disproving the materiality of statements made by public companies. For example, in *SEC v. Aly*, 2018 WL 1581986 (S.D.N.Y. Mar. 27, 2018), the Division offered an expert event study to prove materiality on a motion for summary judgment. In response to the Division's filing, the court noted "event studies such as that performed by [the Division's expert] constitute 'a well established method for calculating the effect of an event on stock prices,' and are 'an accepted method for evaluating materiality."[8] *Id.* at *15 quoting 26A Michael J. Kaufman, Securities Litigation: Damages § 25B:1 (2017); *SEC v. ITT Edu. Servs., Inc.*, 311 F.Supp.3d 977, 992-93 (S.D. Ind. 2018) (stating "The SEC asserts that 'event studies are a widely used methodology for measuring the effect of an event ... on a company's stock price..."). The court found the Division's expert's event study reliable and relied upon it in granting summary judgment as to materiality as a matter of law. *Id.* at *20.

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[7] Although the *Barclay's* case granted summary judgment to the defense on the issue of loss causation, the court's analysis and continuing recognition of the importance of event studies is equally applicable to the materiality context, which was recognized in the *Barclay's* opinion itself. *Barclay's*, 756 F. App'x at 49-50 (relying on earlier precedent affirming "a grant of summary judgment where defendants, by means of statistical evidence 'met their burden... by establishing that the misstatement was barely material and that the public failed to react adversely to its disclosure.'")

[8] This decision also demonstrates that *Petrobras* worked no major change on the law with respect to the importance of event studies to the assessment of materiality. The the court in *SEC v. Aly* wrote: "When used to assess materiality, an expert's event study will look[ ] to the movement, in the period immediately following disclosure, of the price of the firm's stock.... *[I]f a company's disclosure of information has no effect on stock prices, it follows that the information disclosed ... was immaterial....*" *Id.* at *15 (quotations omitted; alterations in original).

D. The Division Failed To Adduce Any Reliable Or Persuasive Evidence Of Materiality Of The Boilerplate Lease Disclosure.

The Division's argument with respect to materiality relies on a host of incredible evidence and strained inferences. For its lead argument, the Division contends that a finding of materiality is supported by the simple fact that ALC included the statements in its Commission filings and also stated that breach of the Lease covenants *could* have a material adverse impact. (Div. Supp. Post-Hearing Br. at 35 citing Div. Post-Hearing Reply Br. at 30-32.) This is tantamount to saying that *any* disclosure is material because it is included in a periodic filing. This should be rejected for the circular reasoning that it is.

Second, the Division relies on its audit expert John Barron, who also testified that a default under the lease *could* be material. (*Id.*) For the reasons stated in Bebo's opening brief, on cross-examination it was established that Barron's opinions were unreliable and did not support any finding of materiality. (Resp't Br. at 163-67.)

The principal reason that it is unreliable is because it relies on the false assumption that every event of default would necessarily result in the imposition of the worst-case scenario of acceleration of all future rent and termination of the Lease. Indeed, as a legal proposition, the Division's failure to establish the critical assumption upon which Barron relied—that an event of default would *necessarily* result in imposition of the acceleration of rent and write-off of the lease intangible—should cause this Court to disregard his materiality opinion entirely.

As demonstrated in Bebo's earlier briefing, tt is well-established that an expert can base his opinion on underlying facts or assumptions he did not find on his own only if competent evidence is also presented to prove the truth of those underlying assumptions. (Resp't Post-Hearing Reply Br. at 78-79 citing *Dura Auto. Sys. of Ind., Inc. v. CTS Corp.*, 285 F.3d 609, 615 (7th Cir. 2002); *Target Mkt. Publ'g, Inc. v. ADVO, Inc.*, 136 F.3d 1139, 1144-45 (7th Cir.

1998) (affirming exclusion of expert opinion on expected revenues using unrealistic assumptions); *Fail-Safe, L.L.C. v. A.O. Smith Corp.*, 744 F. Supp. 2d 870, 891 (E.D. Wis. 2010) (excluding expert testimony of future damages because expert relied on assumptions "without providing any explanation for such an assumption other than general platitudes about the strength of [the company]."); *Loeffel Steel Prods., Inc. v. Delta Brands, Inc.*, 387 F. Supp. 2d 794, 810 (N.D. Ill. 2005); *Victory Records, Inc. v. Virgin Records Am., Inc.*, 2011 WL 382743, at *2 (N.D. Ill. Feb. 3, 2011) (stating "when an expert premises his opinions on an assumption, the assumption must be reliable" and striking expert opinion based on unsupported assumptions) (citations omitted)..).

Third, the Division's attempts to rely on ALC's alleged payment for the CaraVita Facilities for a price in excess of the appraised value does not support the assertion of materiality. (Div. Supp. Post-Hearing Br. at 35.) For the reasons stated in Bebo's opening Post-Hearing Brief (at pages 152-56), the great weight of the evidence demonstrates that any losses recorded by ALC were not related to anything having to do with the employee leasing arrangement. Indeed, the evidence establishes that this was a highly favorable transaction for ALC, that it added approximately $2.40 of value per share to the company, and ALC's stock price went up in response to the announcement that it had purchased the CaraVita Facilities for $100 million and would be recording the one-time write-offs. (*Id.* (citing evidence).)

Fourth, the Division makes the desperate and unsupportable claim that it offered "investor testimony that ALC's covenant compliance was important to them." (Div. Supp. Post-Hearing Br. at 35.) But the Division does not tell this Court that it failed to offer testimony from any public investor. Instead, it relies on the arbitration testimony of ALC's controlling

shareholder, David Hennigar, and the testimony of another director and member of the audit committee, Derek Buntain. (*Id.*)

Putting aside the facially meritless contention that corporate insiders could stand in as a proxy for a public, reasonable investor (they cannot),[9] the credible evidence demonstrates that ALC directors Hennigar and Buntain did know that ALC was meeting the Lease covenants by including rooms for employees in the covenant calculations. Furthermore, it was established at the hearing that Buntain provided a false declaration where he swore under penalty of perjury that he had exercised stock options and would have wanted to know more information about ALC's compliance with the Lease covenants in connection with the exercise of those options. (*See* Resp't Br. at 244 n.71; Tr. 1437-40.) He admitted at trial that he never exercised those options. (*Id.*) The Division's continued reliance on Buntain's supposed desire to know whether ALC was in compliance with the covenants because that information was important to him as an investor (which was tied to his false testimony that he actually made an investment decision to exercise options) should be rejected.

II. The Substance Of The Milbank Interview Memoranda Would Be Admissible Under The Federal Rules For Evidence Of Prior Inconsistent Statements Because They Demonstrate Key Division Witnesses Changed Their Accounts.

A. The contents of the Milbank interview memoranda constitute the recorded recollection of Milbank attorneys that can be used to establish the prior inconsistent statements of the Division's Witnesses.

With respect to the Milbank interview memoranda submitted as Joint Supplemental Exhibit 1 to this court, the Division first claims that they contain hearsay and would be inadmissible in federal court for any purpose. This is incorrect. Under the Federal Rules of

[9] *See* Tom C.W. Lin, *Reasonable Investor(s)*, 95 B. U. L. Rev. 461, 466-68 (2015) (summarizing literature with respect to the current understanding of a "reasonable investor" and concluding that "the reasonable investor, the central character of financial regulation, is frequently envisioned as a rational human being of average wealth and ordinary financial sophistication that invests passively for the long term."). That does not describe an insider.

Evidence, the Milbank interview memoranda would be admissible to establish prior inconsistent statements made by witnesses at trial.[10]

The hearsay rules would not be an impediment to the admission of the Milbank interview memoranda either. As noted the statements made by the witnesses to Milbank would be admissible as prior inconsistent statements under Rule 613(b). The Division appears to complain that the interview memoranda themselves are hearsay, and that Milbank should have to testify in person. But this is not the case. As demonstrated in a June 15, 2015 filing in this matter, the Milbank witnesses confirmed that they would be "generally unable to recall the specific statements: (1) witnesses made to Milbank in their investigative interviews" without the "benefit of using their reports and/or notes to either refresh their memory or read their notes into the record as past recollection recorded." (Resp't Laurie Bebo's Notice Regarding Milbank, Tweed, Hadley & McCloy LLP Witnesses, filed June 15, 2015). As a result the Milbank interview memoranda constitute the recorded recollection of the attorneys conducting the interviews under Rule 803(5).[11]

But all of this is preempted by the stipulation of the parties and order of this Court adopting it. In her order of July 24, 2019, Judge Foelak adopted the "July 19, 2019 Supplemental Term Sheet" of the parties "Regarding Further Evidentiary Matters and Procedures for New Proceedings on Remand". (*See* 7/24/2019 Order and Attachment A thereto) Paragraph 3 of that adopted stipulation is dispositive of the permitted use of the Milbank interview memoranda.

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[10] Normally, Rule 613 requires confronting the witness with the prior inconsistent statement so the witness can explain or deny it before extrinsic evidence of the prior statement—here testimony from Milbank or their recorded recollection in the form of the interview memoranda—is admissible. However, it would be waste of this Court's resources, the parties' resources, and the witnesses' resources to convene a new hearing solely for this purpose.

[11] Statements do not constitute hearsay if it is a record of a "matter the witness once knew about but now cannot recall well enough to testify fully and accurately," was made or adopted by the witness when the matter was fresh in their memory, and accurately reflects the witness's knowledge. All of these criteria are satisfied here.

> The parties agree that attorney interview memoranda for those witnesses that testified live at the prior hearing may be admitted into evidence and utilized by the parties for the purposes of identifying impeachment or corroboration material and supplemental briefing (*See* ¶ 5, below), without the need to call a sponsoring witness from Milbank. The parties further stipulate that the interview memoranda were prepared by Milbank lawyers in the course of conducting an internal investigation into a May 2, 2012 [redacted] letter and are not, unless explicitly stated herein (i.e. through quotation marks) verbatim statements of the witness. For avoidance of doubt the interview memoranda which may be used for these purposes are as follows: [list of witnesses omitted].

(*Id.*) Consistent with the adopted stipulation contained in the July 24 order, Bebo cites those interview memoranda here.

As demonstrated in Bebo's opening supplemental post-hearing brief, numerous key Division witnesses provided highly inconsistent statements to Milbank on the critical issues in this case. For example:

- Despite claiming at trial that covenant calculations were never discussed with Solari, Buono told Milbank Bebo told Solari that the covenant calculations were "getting tight." (Resp't Supp. Post-Hearing Br. at 19.)

- "Buono's recollection was that Bebo informed Solari that the prior operator had *used employee leases in its covenant calculations* and that ALC intended to do the same thing." (*Id.* (emphasis added).)

- Contrary to testimony during his direct examination by the Division, Buono confirmed his understanding that ALC reached an "agreement" with Ventas about employee leasing. (*Id.* at 19-20.)

- Contrary to his trial testimony, ALC's general counsel, Fonstad, had a "general recollection ... that if ALC sent employees to work at a facility and those employees stayed at the facility during the visit, they could be included in the occupancy covenant." (*Id.* at 20-21 quoting Jt. Supp. Ex. 1, MB_BEBO_0000080.)

- Contrary to his trial testimony, Fonstad confirmed that he was aware that ALC was including rooms related to employees in the Ventas covenant calculations. (*Id.* quoting MB_BEBO_0000081.)

- Contrary to his trial testimony, Fonstad told Milbank he was aware that the call with Solari to discuss employee leasing had occurred and "had gone well." (*Id.*)

- Buono confirmed Fonstad was aware that "the purpose of setting aside units for employees was to meet occupancy covenants." (*Id.* at 22 quoting MB_BEBO_0000063.) Fonstad had no issue with this. (*Id.*)

- Buono confirmed that Fonstad reviewed the Solari Email and "did not express any reservations regarding the quality of the notice as reflected in Bebo's February 4, 2009 email to Solari." (*Id.* quoting MB_BEBO_0000065.)

- Although at trial Lucey refused to confirm that ALC's disclosure committee, chaired by Fonstad, explicitly discussed ALC's lease compliance disclosure in light of the Solari Call and Email, he told Milbank that "Buono on one occasion (probably 2009) advised the [Disclosure] Committee that the company was using employee leases to meet the occupancy covenants." (*Id.* at 24 quoting MB_BEBO_0000053.)

B. Bebo's statements to Milbank were generally consistent with the extensive sworn testimony provided in this matter.

The Division's attempt to contradict Bebo's hearing testimony with the Milbank interview memorandum is unsupported at best and deceptive at worst. The majority of the Division's alleged inconsistencies are (i) not even inconsistent as stated and described by the Division, (ii) not inconsistent based on a full review of Bebo's hearing testimony and the Milbank memorandum instead of the Division's selective quotations/citations, or (iii) not an impairment of her credibility since her recollection was refreshed on several issues since her Milbank interview. Finally, as previously established, Bebo is remarkably credible and consistent in light of the 80+ hours of sworn testimony she has provided on the issues and the only minor inconsistencies the Division had identified. *See In the Matter of Thomas R. Delaney II, et al.*, Release No. 755, 2015 WL 1223971, *35-36 (stating "It is telling that the Division, who has had Delaney testify so often, seizes on such minor supposed contradictions. I find all of the purported inconsistencies identified by the Division are either immaterial or have been adequately explained by Delaney. I found, on the whole, Delaney's testimony to be credible, with the exception, noted previously, that he may not recall comparatively minor events and discussions that took place up to six years before the hearing.") (Patil, ALJ).

1. The Division's Statements Were Consistent on their Face.

The Division claims, in its Supplemental Post-Hearing Brief, that "the story Bebo told Milbank was very different than the one" she told at trial, however, the chart that the Division created to support this claim includes several comparisons that are not inconsistent based on the plain language of the Division's statements. (Div. Supp. Post-Hearing Br. at 24.) The following examples and responses will highlight the Division's misguided attempt to create contradictions where none exist.

(a) Former Cara Vita Covenant Calculations

Division's Position: The Division attempted to construct an inconsistency between the Milbank memorandum and Bebo's testimony with respect to how the old CaraVita operator counted employees in covenant calculations. More specifically, the Division contended that it was inconsistent for Bebo to have told Milbank that she did not know if the former CaraVita operator included employees in covenant calculations and then later testify that she believed such employees were included in old CaraVita's covenant reporting to Ventas. (Div. Supp. Post-Hearing Br. at 24.)

Response: The portions of the Milbank memorandum and Bebo's hearing testimony that the Division cites are not inconsistent as presented to the Court by the Division. The statements the Division cites are not inconsistent on their face because the Milbank memorandum speaks to Bebo's actual knowledge of old Cara Vita's covenant calculations whereas Bebo's hearing testimony speaks to her beliefs and understandings of what was included in such calculations. Thus, the Division was not even comparing the same kind of statement. A truly inconsistent statement would exist if Bebo testified at the hearing that she knew for a fact that old CaraVita included employees in its covenant calculations. Bebo, of course, did not make any such statement at the hearing. Instead, she clearly testified (which the Division omitted) that it was her

belief that employees were included in old CaraVita covenant calculations based on her call with Solari and that she never confirmed her understanding. (Tr. 1885 ("Generally speaking, yes. Because of the discussion with Solari in January of '09, *I never go back through to fully determine, you know, what was included, what old CaraVita had included in their numbers . . .* But generally speaking, I was of the *impression* that these folks *may* have been included in their numbers.") (emphasis added); *see also* Tr. 1886 ("I never confirmed that information. Generally speaking, that was my impression, but as I said, I had planned on reviewing that material and following back up with Josh Coughlin through Ms. Bucholtz, and we never -- we never did that because of the discussion with Solari.")

(b) Bebo's Handwritten Notes

Division's Position: There was no mention of handwritten notes documenting the Solari call during the Milbank interview which, according to the Division, is inconsistent with Ms. Bebo's hearing testimony about such notes. (Div. Supp. Post-Hearing Br. at 25)

Response: Nothing in the Division's chart or the Milbank interview notes for that matter is inconsistent with Bebo's hearing testimony about her handwritten notes of the Solari call. The Milbank memorandum being silent on the subject of Bebo's notes may have been attributed to (i) Milbank not asking about the notes whereas others specifically asked Bebo about her notes during the hearing, (ii) Bebo not feeling the need to describe the notes based on an assumption that Milbank would or did have the notes (they were housed at ALC after she was terminated), or (iii) any other multitude of explanations as to why the notes were discussed at one point versus another. A real inconsistency would exist if Bebo told Milbank that she did not take notes of the Solari call. Since Bebo never made any such statement to Milbank, the Division resorted to creating an illusion of inconsistency.

(c) The Solari Call and the Employee Leasing Agreement

Division's Position: The Division claims that the Milbank interview memorandum contradicts Bebo's hearing testimony with respect to the Solari call. More specifically, the Division contends that there is an inconsistency between the Milbank notes which state, according to the Division, that "Bebo's call with Solari focused on whether ALC could rent rooms to its employees (as opposed to including them in the covenant calculations)" and Bebo's hearing testimony about Solari agreeing that rooms could be included for covenant calculations in certain circumstances. (Div. Supp. Post-Hearing Br. at 25.)

Response: Again, the Division's juxtaposed propositions are not inconsistent and the Division's attempt to impugn Bebo's credibility is misguided for several reasons. First, the Milbank notes and Bebo's hearing testimony are not facially inconsistent. Just because aspects of the employee leasing program were not focused on during the Milbank interview does not mean that it is inconsistent for Bebo to testify about those aspects later on during the hearing. Further, it is not surprising that the Milbank memorandum does not focus on whether rooms could be included in covenant calculations because, as the Division's key witness, Buono, recognized, the inclusion of rooms in covenant calculations was obvious from the nature of ALC's request. (Tr. 2489-90 (Buono testified that "[i]n 2009, my understanding was that Ventas was aware we were going to put employees into the -- into the properties, and it was my interpretation of that that -- those employees, we would only do that – a reasonable person would only think we'd do that in order to meet covenants.").) Second, the Division attempted to craft the impression that Bebo testified about some new facts regarding the Solari call at the hearing (*e.g.*, Solari agreeing that there was no cap on the size of the employee leasing program) when such facts were also included in the Milbank notes. (*See* Jt. Supp. Ex. 1 at MB_BEBO_0000020-21 ("Bebo said she asked if Solari if he cared how many employees could

rent units at the facilities and Solari said he did not"). Finally, the Division's comparison is not an apples to apples comparison because the Milbank interview notes compare what was discussed on the Solari call, and the cited hearing testimony, in the Division's points (1)-(2) in the comparison chart, clarifies what Bebo understood and interpreted the employee leasing agreement to be with Ventas based on the "reason to go" standard discussed on the Solari call. (*Id.*)

(d) Non-Employees on Employee Leasing Lists

Division's Position: The Division claims that the Milbank memorandum states that "[t]he only non-employee names on the lists Bebo recognized were Bebo's parents, her husband, and her Husband's friend." The Division further argues that the previously mentioned aspect of the Milbank notes is inconsistent with Bebo's hearing testimony which the Division summarized as "Bebo's list included non-employees such as *Bucholtz's* parents, brother and sister-in-law, and [redacted]." (Div. Supp. Post-Hearing Br. at 26.)

Response: The Division's "contradiction" is flawed because these statements are not inconsistent and because the Division mischaracterized the Milbank notes on this issue. First, put simply, the Division's claim that Bebo recognized certain non-employees on a list (*i.e.*, the Division's characterization of the Milbank notes) is an entirely different and not inconsistent statement than who was actually put on such a list (*i.e.*, the Division's characterization of Bebo's hearing testimony). Second, the Milbank interview memorandum does not even discuss who Bebo recognized on the employee leasing list, so it is unclear what the Division is even referencing. The only reference to specific family members on the page cited by the Division states that "Bebo stated that the non-employees on the list whom she recalled were her mother and father, her husband, and a family friend named Kevin Schweer . . ." (Jt. Supp. Ex. 1 at MB_BEBO_0000026.) There is no reference in the Milbank memorandum about who Bebo did

or did not recognize and, more importantly, the notes seemed to be based on who she could recall being on the employee leasing list. (*Id.*) Thus, the fact that Bebo did not recall specific names on a list that she gave little attention to is not surprising or inconsistent with the fact that other non-employees were actually on the employee list.

2. Bebo's Statements Were Not Inconsistent Based on a Complete Review of Bebo's Hearing Testimony and the Milbank Memorandum.

In addition to attempting to challenge Ms. Bebo's credibility with statements that were not facially inconsistent, the Division also, in some instances, omitted material statements of Ms. Bebo's hearing testimony or the Milbank notes to try to impeach Ms. Bebo. (*See also supra*, Section 1(a).) For example:

(a) Reason to Go Policy

Division's Position: The Division argues that Bebo testified at the hearing that she "selected employees who had a 'reason to go' to the properties, even if they did not actually visit or stay there" and such testimony is inconsistent with a phrase in the Milbank memorandum indicating that Bebo "stated that her practice was to add employees who would be likely to go to these properties." (Div. Supp. Post-Hearing Br. at 26.)

Response: The Division's claim of inconsistency with respect to Bebo selecting employees for the employee leasing list is misleading and baseless for several reasons. First, although Bebo had a practice of adding people to the list who would be likely to travel to the properties, she also conveyed to Milbank other aspects of who could be on the lists and those additional considerations are consistent with the "reason to go" standard that Bebo testified about. (Jt. Supp. Ex. 1 at MB_BEBO_0000026.) Further, the Division conveniently did not cite the following excerpts of the Milbank memorandum when paraphrasing it on this issue: (i) "she described the list of employees as an internal document of who 'woulda, coulda, or shoulda'

spent time at these properties in connection with the conduct of ALC's Business", (ii) "[s]he stated that the list bore the names of employees who 'should or could' have spent time at the facilities", (iii) "she stated that when she added names to the list, she endeavored to include employees who were likely to use the property at some point in the future", (iv) "she acknowledged that there were some employees on the list who had never visited the properties", and (v) "she did not spend a great deal of time trying to perfect the list". (*Id.* at MB_BEBO_0000025-26.) When the Milbank memorandum is viewed as a whole and not in a misleading piecemeal fashion, it is clear that Bebo tried to find people who would be likely to travel to the properties but in any event found people that would, could, or should (*i.e.*, people who had a reason to go) go to the properties. Thus, the Milbank interview memorandum and Bebo's hearing testimony are not inconsistent on this matter.

(b) Grant Thornton's Knowledge of the Employee Leasing Program

Division's Position: The Division argues that Bebo's testimony about speaking with Melissa Koeppel about the employee leasing practice in early 2009 is inconsistent with the Milbank memorandum that indicates that, according to the Division, "Bebo *did not* speak with Grant Thornton in late 2008 or early 2009 about the inclusion of employees in the covenant calculations." (Div. Supp. Post-Hearing Br. at 26.)

Response: The purported contradiction is faulty because the Division mischaracterizes the Milbank notes. The Milbank memorandum does not indicate that Bebo told Milbank she did not speak to Grant Thornton during 2008 or early 2009. Rather, the Milbank memorandum indicates that Bebo:

> [D]id not *recall* speaking with Grant Thornton in late 2008 or early 2009. Asked if any colleagues had spoken to Grant Thornton about this issue, Bebo did not recall. She recalled at one point Buono told her he had spoken to Grant

Thornton and had reviewed the issue with them. She believes that Buono made Grant Thornton aware of this practice sometime in 2009.

(Jt. Supp. Ex. 1 at MB_BEBO_0000026 (emphasis added).) When you correct the Division's improper attempt to change Bebo's statement about her recollection to an affirmative statement (*e.g.*, I did not speak to . . .) then the Division's alleged inconsistency disappears. In other words, there is no inconsistency between the Milbank notes and Bebo's hearing testimony because she simply remembered more details about her interaction with Grant Thornton at a later time. Finally, it is unsurprising that Ms. Bebo's recollection was refreshed on this issue between the date of the Milbank interview (May 8, 2012) and the date she testified about these issues (April 30, 2015), considering the amount of documents she reviewed in connection with this proceeding, and the number of times she testified relating to these matters.

(c) The Employee Leasing Lists

Division's Position: The Division claims that Bebo's hearing testimony about her selecting names for the employee list that went to Grant Thornton is inconsistent with the portion of the Milbank memorandum which states that Bebo did not know how the employee list was compiled. (Div. Supp. Post-Hearing Br. at 26.)

Response: The Division's position with respect to the employee list is unfounded and deceptive. The Milbank memorandum actually matches Bebo's hearing testimony with respect to this issue. It is true that during the Milbank interview Bebo stated that she did not know how the employee list was put together (*i.e.*, created),[12] which is completely consistent with Bebo's position and testimony that she was not a part of establishing various procedures relating to the employee leasing process. (Resp't Post-Hearing Br. at 99-103; Tr. 4128-29.) Further, the notion that Bebo did not know how the list was created is no way inconsistent with her testimony that

[12] Bebo did tell Milbank what the genesis of the employee list was. (Jt. Supp. Ex. 1 at MB_BEBO_0000026.)

she selected names for the employee list after the list was put together. In fact, the Division's brief ignores statements on the very same page of the Milbank notes that the Division cites recounting how Bebo stated that she added names to the existing employee list. (Jt. Supp. Ex. 1 at MB_BEBO_0000026.) Thus, the Division omitted part of the Milbank notes that matched Ms. Bebo's hearing testimony that was cited by the Division as being inconsistent. This is improper.

3. Differences Between the Milbank Notes and Ms. Bebo's Hearing Testimony is Attributable to Ms. Bebo's Refreshed Recollection.

A final category of "inconsistencies" that the Division focused on in their Supplemental Post-Hearing Brief can be best described as "inconsistencies" that are attributable to Bebo's recollection being refreshed after the Milbank interview. For example, the Division tries to make much out of the following "discrepancies" that can be explained by the simple fact that Bebo's recollection of the minute details of this case has amplified as she was subpoenaed for several days of investigative testimony, testified in a related arbitration proceeding against ALC, and was provided hundreds of thousands of new documents as part of the Division's and third party's productions in this case.

(a) Contact With Quarles and Brady

Division's Position: The Division attempts to reveal an inconsistency between the Milbank memorandum and Bebo's testimony about when she spoke with Quarles & Brady about employee leasing. (Div. Supp. Post-Hearing Br. at 26.) The Division argues that the Milbank notes indicate that Bebo reached out to Quarles & Brady in 2012, which contradicts her hearing testimony that she spoke to Quarles & Brady in 2011. *Id.*

Response: The discrepancy that the Division identified can be reconciled by the simple fact that Bebo's recollection was refreshed on this issue between the Milbank interview and her

hearing testimony. Indeed, she was able to review documentation that indicated that Quarles & Brady was consulted with respect to the SEC comment letter.[13] (*See, e.g.* Ex. 1563, 3159.)

(b) Board Knowledge of Employee Leasing

Division's Position: The Division argues that Bebo's hearing testimony and the Milbank memorandum is inconsistent with respect to her contact with the Board as it relates to the employee leasing program. (Div. Supp. Post-Hearing Br. at 24-26.)

Response: The alleged discrepancies with respect to her contact with the Board and Board members about the employee leasing program should not impugn Bebo's credibility because her recollection was refreshed since the Milbank interview and, importantly, the general principle that she disclosed and repeatedly discussed employee leasing with the Board remains uncontradicted throughout this proceeding.

It is unsurprising and understandable that Bebo's recollection of her interactions with Board members has been refreshed over time since she has reviewed materials (*e.g.*, Board minutes, phone records, e-mail correspondence, other people's testimony, etc.) and testified extensively with respect to this issue since her Milbank interview in 2012. For example, the Division tries to make much out of the fact that Bebo testified at the hearing that she spoke with Mel Rhinelander the day after the Solari call and that she neglected to mention this conversation during her Milbank interview. Of course, the Division does not highlight the fact that Bebo testified at the hearing that her recollection was refreshed on this issue after obtaining phone records. (Tr. 1952-53.) Additionally, Bebo's recollection being refreshed with respect to this issue is consistent with her statements to the Division and testimony that she had several conversations with Mel Rhinelander about this issue and that she would not be able to provide

[13] The Division's claim that Bebo was properly impeached at the hearing regarding her conversations with Quarles & Brady is also incorrect. (*See* Resp't Post-Hearing Reply Br. at Appendix A, pp. 12-17.)

exact dates for the multitude of conversations. (*See* Ex. 496, p. 128.) Other examples of the Division's alleged impeachment are diluted when it is understood that Bebo's hearing testimony clarified concepts and dates after the Milbank interview which (i) was the first time Bebo was interviewed in-depth about these issues, (ii) occurred over three years after she contacted the Board and its members about employee leasing, (iii) was conducted prior to Bebo having the benefit of having her recollection refreshed with a multitude of materials, (iv) was focused on events (*e.g.*, the Ventas lease and employee leasing) that were generally immaterial from her and ALC's perspective and thus unlikely to be at the forefront of her recollection, and (v) focused on events and conversations that occurred in an extremely condensed time period.[14] Thus, the Division's attempt to impugn Bebo's credibility with respect to her contact with the Board and its members should be rejected as it is less of a contradiction and more of a clarification of a theme (*e.g.*, the board knew about and approved of the employee leasing program) that has been consistent throughout this proceeding.

The Division's attempt to highlight contradictions in Bebo's statements about Board knowledge of employee leasing does not undermine the undeniable fact that the Board knew about the employee leasing program, which is a fact that Bebo and others have consistently and credibly testified about throughout this proceeding. Further, it is clear in the record that the

[14] Although the Division highlights differences between the Milbank memorandum and Bebo's hearing testimony as to what was said to the Board during the Q2 2009 Board meeting about employee leasing, the Court should be aware that Bebo probably conflated the Q2 2009 Board meeting and the Q3 2009 Board meeting during her Milbank interview. More specifically, Bebo may have confused the Q2 2009 Board meeting where there was little or no discussion of employee leasing at the board level (it occurred with Mel Rhinelander immediately prior to the meeting who then discussed it with David Hennigar) with the Q3 2009 Board meeting where there was a more robust discussion of employee leasing. (Resp't Post-Hearing Br. at 121-24.) Similarly, the Division claims that, when talking to Milbank, Bebo said she spoke with Hennigar by phone soon after the Solari Call about the decision to include employees in the covenant calculations, but did not speak to Rhinelander about it at that time. At trial, she testified that she spoke to Rhinelander soon after the Solari Call about how Ventas had agreed to include rooms for employees in the covenant calculations, but not Hennigar. This simply appears she misspoke during the Milbank interview, and the basic statement is the same—soon after the Solari Call she informed the Chair or Vice-Chair of the Board about Ventas's agreement and obtained their endorsement to meet the covenants through employee leasing.

Board or its members (i) approved the Ventas lease, (ii) were consulted with about the employee leasing arrangement prior to it being implemented, (iii) approved the program around the time of the Q2 2009 Board meeting, and (iv) were apprised of or discussed the employee leasing program after the Q2 meeting (*e.g.*, Board discussions with Grant Thornton, discussions during the Q3 2009 Board meeting, and discussions in connection with the SEC comment letter). (Resp't Post-Hearing Br. at 45-47, 96-100, 121-134.) The Division's attempts to muddy the waters surrounding Board knowledge and Bebo's contacts with the Board is an attempt to distract the Court from questioning how the Division can argue that the Board did not know about employee leasing prior to *March 2012* when there are e-mails between management and Board members like the following in the record:

Yesterday's discussion

From:

"Buono, John" <"/o=assisted living concepts/ou=alc/cn=recipients/cn=jbuono">

To:

malen_ng@wsib.on.ca

Date:

Thu, 05 Nov 2009 13:16:09 -0600

I owe you a few answers from our discussion yesterday. I wasn't sure if you want to talk again or I can just answer in this email.

The Cara Vita properties will lose the impact of quarter 4 of 2008 in the next reporting period. The occupancy reported in Q4 08 was 80.7% so not much different from Q3 09. The quarter that is helping us is Q1 09 at 83%. So we will need to improve slightly in the fourth quarter but not drastically.

The Winterville EBITDAR looks out of line with the occupancy for a couple of reasons. We use our system generate financials for the EBITDAR schedule. This particular property has both some employees with rooms and several less than current payers. We make adjustments top side to pay for our employee rooms and the people who have not paid and would fall into bad debts. We do this because we can not afford to exit them at this time.

I spoke with Melissa this morning. GT had all the information they had requested, it just had not rose to Melissa's level yet. This morning they did ask for several additional pieces of information which we have now provided.

If you want to talk today or before the meeting tomorrow, let me know. Otherwise, safe travels and we will see you in the morning.

John Buono
Sr. V.P., Chief Financial Officer and Treasurer
Phone 262-257-8999

(Ex. 1115 (emphasis added).)

* * *

The fact that the Division feels the need to stretch the statements made to Milbank and the hearing testimony to find inconsistencies where none exist demonstrates how consistent Bebo actually has been during the approximately 80 hours of sworn testimony (filling 2,807 pages of transcripts) relating to the issues presented at the hearing of this matter. (Resp't Post-Hearing Reply Br. at 60-61.) In light of all the circumstances and the high degree of consistency with respect to the basic facts of this case, Bebo's testimony is highly credible. *See In the Matter of Thomas R. Delaney II*, 2015 WL 1223971, *35-36.

III. The Division's Supplemental Brief Confirms That Scheme Liability Does Not Add Anything To This Case.

The Division continues to invoke "scheme" liability in this matter, although that theory adds nothing to this case under these circumstances. As the Supreme Court's decision in *Lorenzo v. SEC*, 139 S. Ct. 1094 (2019) makes clear, any scheme must be directed at investors—typically through false or misleading statements—to be actionable. And scheme liability generally exposes those to liability where they may have not been the "maker" of the misrepresentation to investors, but participated in a scheme to make the misrepresentation and defraud investors. Scheme liability does not convert the Section 10(b) to a general prohibition of fraud or mis-management by corporate executives.

The Division seems to acknowledge this in its Supplemental Post-Hearing Brief, where it states "repeated false statements about compliance with the Ventas covenants in ALC's Forms 10-K and 10-Q" give rise to scheme liability. Thus, as Bebo has previously argued (Resp't Post-Hearing Reply Br. at 87-89), this case arises (and falls) on the traditional elements of a Section

10(b) claim: the falsity and materiality of the alleged misstatements and whether they were made with scienter.[15]

CONCLUSION

For the reasons stated in this Supplemental Post-Hearing Reply Brief and in Bebo's prior post-hearing briefs, the OIP's allegations are unsupported and the OIP should be dismissed in its entirety.

Dated this 1st day of November, 2019.

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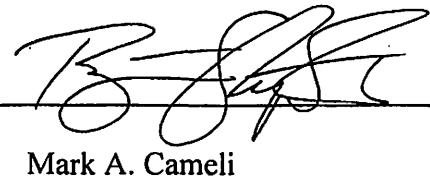
[15] The Division also cites *SEC v. Jensen*, 835 F.3d 1100 (9th Cir. 2016), for the proposition that it may pursue an independent claim for a violation of Rule 13a-14. (Div. Supp. Post-Hearing Br. at 35.) *Jensen* appears to be the first circuit court to decide this issue, finding an independent claim even though it largely duplicates a Section 10(b) claim based on the same allegedly false or misleading periodic filings with the Commission. However, whether there is an independent claim pursuant to Rule 13a-14 is still an open question in other circuits. Moreover, like the resort to scheme liability the Rule 13a-14 claim fails because the Division cannot establish that ALC's periodic filings were false or misleading, or if, they were, the misstatements were made with scienter.

CERTIFICATE OF COMPLIANCE

Pursuant to Commission Rule of Practice Rule 450(d), incorporated in to this Court's August 28, 2019 order governing supplemental briefing, I hereby certify that the Respondent Laurie Bebo's Supplemental Post-Hearing Brief complies with the length limitation set forth in Commission Rule of Practice 450(c). According to the Word Count function of Microsoft Word, this brief contains 12,680 words, exclusive of the table of contents, table of authorities, cover page, signature block and this certification.

Dated: November 1, 2019

REINHART BOERNER VAN DEUREN S.C.
Counsel for Respondent Laurie Bebo

By: 

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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

Ryan S. Stippich of Reinhart Boerner Van Deuren s.c. certifies that on November 1, 2019, he caused a true and correct copy of Respondent Laurie Bebo's Supplemental Post-Hearing Reply Brief to be served on the following by e-mail and overnight courier:

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Dated this 1st day of November, 2019.

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