

Risk of New, Undisclosed SEC Probe Adds to Valeant Pharmaceuticals' Woes



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Editor's note: This report warning of risk of an undisclosed SEC probe at Valeant, as well as our opinion of the raised potential for a restatement and delayed filings, was already loaded and set for release at the time the Wall Street Journal broke news last evening of a pending restatement. We decided to keep our original report intact, but wanted to acknowledge our awareness of the Journal's story. We remain first on breaking news of data pointing to an undisclosed SEC probe.

Valeant Pharmaceuticals International, Inc. \$VRX

- Possible Undisclosed SEC Investigation of Valeant.
- Salix investigations remain an on-going exposure.
- Restatement and delayed filings risk elevated.
- Added to Watch List

Analyst Summary: With new SEC data pointing to a new and undisclosed SEC investigation of Valeant, and the company's own filings indicating a previously-disclosed, formal SEC investigation of Salix is on-going, the risk for delayed filings and restatements is elevated.

Facts of Interest or Concern: In a letter dated 04-Feb-2016, we received information from the SEC suggesting Valeant Pharmaceuticals was involved in unspecified SEC investigative activity. Other than disclosures pertaining to an SEC investigation of the acquired Salix unit, we

otherwise found no disclosures of an SEC probe of Valeant itself in the past two years. We filed an administrative appeal to challenge the SEC's response. In our experience, over two-thirds of these SEC responses are confirmed on appeal. The fact-set before us strongly suggests this will be one of them.

In a letter dated 30-Sep-2015, we received information from the SEC to suggest the absence of recent SEC investigative activity at Valeant. What's notable is that the company had already disclosed an SEC probe of its recently-acquired Salix unit at the time of the SEC's September letter to us. Starting with an 8-K filed in Feb-2015, Valeant began disclosing an SEC investigation at Salix. Valeant most recently disclosed it in the 10-Q filed 26-Oct-2015. This leaves us comfortable that the response of 04-Feb-2016 is almost certainly related to a new SEC investigation involving the conduct, transactions, and/or disclosures of Valent Pharmaceuticals, and not necessarily Salix.

We remind investors four negative articles were published in rapid succession on Valeant last October, between 19-Oct and 25-Oct-2015. On 23-Oct-2015, in response to the one published by Citron Research, we published our own note saying we expected it to trigger a wide array of investigations, including one from the SEC. (See, Probes Reporter, [What's Next for Valeant Pharmaceuticals](#), 23-Oct-2015).

Analysis and Opinion: It strains us to imagine the basis Valeant management uses to justify not disclosing the SEC probe we are now alerting you to today. Our report may now compel disclosure with the pending 10-K, but the damage to management credibility for having not disclosed on their own is now done.

We are convinced that last October's array of negative reports published on Valeant compelled the SEC to open

a new investigation into the company. The accusations embedded within those negative reports, and attendant stock price volatility triggered by them, is catnip for SEC enforcement officials. They simply could not ignore it.

Conference calls held by Valeant on 26-Oct-2015, and again on 10-Nov-2015, were supposed to repair the company's image and calm nervous investors. Full transparency was supposedly on offer. We have to imagine the company almost certainly heard from the SEC by the time of the Nov-2015 call. Yet not a word was said on either of the conference calls about the SEC opening an inquiry. Why?

At the time of the conference calls, Valeant had already announced receipt of subpoenas from the U.S. Attorney's Office for the District of Massachusetts and a subpoena from the U.S. Attorney's Office for the Southern District of New York. Against this backdrop, disclosing an SEC probe would have been something of a "freebie" for Valeant; that is, investors may not have given it a second thought. To have not done so feels like an opportunity squandered by Valeant management to build up trust with investors, and for no good reason.

Now we come to risk of delayed filings and restatement. The inherent complexity of the underlying accusations against the company surely has the audit committee and outside auditor on high-alert right now. This has to predispose any prudent person valuing their reputation, if not freedom, to at least give serious thought to delaying filings until such time as the smoke clears. Unfortunately, as that smoke clears, so too may it become clear the need for restatement. Even without Philidor-related problems, we contend the festering nature of the Salix exposure could contribute to the risk of a restatement.

Don't Ignore the Salix Investigations

Many studies show most acquisitions fail. We also know that when a company with an SEC investigation gets acquired, the acquirer often stops talking about the underlying exposure. This can be reasonable; that is, what may have been material to the acquired company as a stand-alone entity may not be as big an exposure in

the context of the merged entity. But that's not what happened here with Valeant and Salix.

Even post-merger, Valeant management and their array of experts judged the Salix SEC investigation and involvement by the US Attorney's Office (read: criminal exposure) remains a material exposure to the post-deal company. In this case we say, trust them; that is, you too should view SEC and US Attorney problems at Salix as a material risk to Valeant.

Your best questions for Valeant at this time –

What communications has Valeant had with the SEC's Division of Enforcement in the past two years?

Did the reports published last October trigger a new SEC investigation? If so, when did it start, and, why have you not told us about it sooner? Where does it stand today?

What do you presently see as the risk for delayed filings or restatements?

Until we find out what's really going on between Valeant and the SEC, we suggest you proceed with appropriate caution.

Final thought: We've seen this game played before. For example, on 06-Jun-2014, Hertz had taken a massive restatement as a result of accounting errors. We then wrote a report titled, [If Hertz Wasn't Under Investigation by the SEC Already, It Will be Now](#) (Probes Reporter, 06-Jun-2014). It took all the way until an 8-K filed 14-Nov-2014, for the company to finally disclose the SEC had, in fact, started an investigation ... all the way back in Jun-2014, just as we had warned.

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