No. 08-836

In the Supreme Court of the United States

DAVID E. WELCH, PETITIONER

v.

HILDA L. SOLIS, SECRETARY OF LABOR, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE FEDERAL RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether petitioner failed to demonstrate that he engaged in protected activity within the meaning of Section 806(a) of the Sarbanes-Oxley Act of 2002, 18 U.S.C. 1514A(a)(1).

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OPINIONS BELOW

The judgment of the court of appeals (Pet. App. 1a-21a) is reported at 536 F.3d 269. The decision and order of the Administrative Review Board (Pet. App. 22a-46a), and the recommended decision and order of the administrative law judge (Pet. App. 47a-203a), are unreported.

JURISDICTION

The judgment of the court of appeals was entered on August 5, 2008. A petition for rehearing was denied on October 3, 2008 (Pet. App. 204a-205a). The petition for a writ of certiorari was filed on January 2, 2009 (Friday following a holiday). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Section 806(a) of the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley), 18 U.S.C. 1514A(a)(1), prohibits a covered entity from retaliating against an employee for providing information to a federal agency, Congress, or his employer, that he reasonably believes is related to a violation of 18 U.S.C. 1341 (mail fraud), 1343 (fraud by wire, radio, or television), 1344 (bank fraud), or 1348 (securities fraud), any rule or regulation of the Securities and Exchange Commission (SEC), or any provision of federal law relating to fraud against shareholders. The Secretary of Labor is responsible for investigating retaliation complaints under Section 806(a). After completion of an investigation, the Secretary either dismisses the complaint because it lacks merit or finds retaliation and orders appropriate relief. 18 U.S.C. 1514A(b)(2)(A).

Under statutory standards governing retaliation claims that were made applicable to Sarbanes-Oxley, the Secretary may find retaliation "only if the complainant demonstrates that [protected activity] * * * was a contributing factor in the unfavorable personnel action alleged in the complaint." 49 U.S.C. 42121(b)(2)(B)(iii). Even if the complainant makes that required showing, the Secretary may not order relief "if the employer demonstrates by clear and convincing evidence that the employer would have taken the same unfavorable personnel action in the absence of [protected activity]." 49 U.S.C. 42121(b)(2)(B)(iv).

The Secretary's regulations provide that either the complainant or the respondent may seek a de novo hearing before an administrative law judge (ALJ) to review the Secretary's decision. The ALJ's decision is subject to discretionary review by the Department of Labor's

Administrative Review Board (Board). 29 C.F.R. 1980.106, 1980.110. The Board's final decision is reviewable in the court of appeals for the circuit in which the violation allegedly occurred or in which the complainant resided on the date of the alleged violation. 49 U.S.C. 42121(b)(4)(A); 29 C.F.R. 1980.112(a). The court of appeals must uphold the agency's factual findings when supported by substantial evidence and the court reviews questions of law de novo. *Platone* v. *United States Dep't of Labor*, 548 F.3d 322, 326 (4th Cir. 2008); *Allen* v. *Administrative Review Bd.*, 514 F.3d 468, 476 (5th Cir. 2008).

2. Respondent Cardinal Bankshares Corporation is a bank holding company and sole owner of the Bank of Floyd. Ronald Leon Moore is the Chief Executive Officer of both entities (hereafter collectively referred to as Cardinal), which share a Board of Directors and managing officers. Petitioner, a certified public accountant in Virginia, began working for Cardinal in 1999 as a part-time accounting officer. Pet. App. 3a. In 2000, Moore hired petitioner as Cardinal's Chief Financial Officer (CFO). *Id.* at 3a-4a. As CFO, petitioner prepared and reviewed entries on Cardinal's general ledger accounts, devised and implemented accounting procedures, and prepared various reports and financial statements including quarterly (Form 10-QSB) and annual (Form 10-K) reports that Cardinal is required to submit to the SEC. *Id.* at 4a.

While employed at Cardinal, petitioner became concerned that the company's accounting practices were deficient in several respects. Pet. App. 4a. According to petitioner, although generally accepted accounting practices (GAAP) require that only persons who have accounting expertise be permitted to make ledger entries,

Moore would make entries himself or direct others with no special accounting expertise to make entries. *Ibid.* Petitioner was particularly concerned that in the third quarter of 2001, Moore recorded in Cardinal's ledgers two recoveries of written-off loans, totaling $195,000, as income rather than listing the amounts on the company's loan reserve account as required by GAAP. Petitioner believed that by misclassifying those loan recoveries, Cardinal overstated its year-to-date income in its 2001 third-quarter 10-QSB report. *Ibid.* During the year-end audit Cardinal's independent auditor, Larrowe & Company, PLC (Larrowe & Co.) changed the entries to conform to petitioner's recommendations, but Cardinal did not correct its 2001 third-quarter 10-QSB report to the SEC. *Id.* at 4a-5a. Petitioner also was concerned that he was being excluded from communications between Moore and Larrowe & Co. on financial issues. *Id.* at 5a. Petitioner believed that such restricted access to Larrowe & Co. prevented him from performing his tasks as CFO and from confirming the accuracy of Cardinal's financial reports. *Ibid.*

Petitioner communicated his concerns to Cardinal on several occasions, both orally and in memoranda to Moore and others. Pet. App. 5a. On August 2, 2002, petitioner informed Larrowe & Co. that he would not sign a representation letter to the auditor from Cardinal confirming the accuracy of the company's financial position because Moore and others had made ledger entries without his review and because he had been excluded from communications between Moore and the auditors on financial issues. *Ibid.* On August 14, 2002, petitioner refused to certify the accuracy of Cardinal's 2002 second-quarter 10-QSB report to the SEC, a requirement under the newly-enacted Sarbanes-Oxley Act, be-

cause of his concerns about the ledger entries, including the misclassification of loan recoveries as income. *Id.* at 5a-6a. Moore ultimately certified the reports himself. *Id.* at 6a. On September 13, 2002, petitioner sent Moore another memorandum insisting that Cardinal needed to change its accounting practices before petitioner could certify the pending 2002 third-quarter 10-QSB report. *Ibid.*

On September 17, 2002, Moore called a meeting of Cardinal's Board of Directors to discuss his dissatisfaction with petitioner. Pet. App. 6a. Moore informed the Board of Directors about the content of petitioner's memoranda and reported that in August 2002, state examiners had found numerous errors in a quarterly call report that petitioner had prepared and submitted to the Federal Reserve and the Virginia State Corporation Commission. *Id.* at 6a-7a. The Board of Directors asked its Audit Committee's legal counsel, Douglas Densmore, and Michael Larrowe of Larrowe & Co., to conduct an investigation and prepare a report on petitioner's allegations. *Id.* at 7a.

On September 20, 2002, petitioner held a briefing on Sarbanes-Oxley for senior personnel of Cardinal, at which he alleged that Cardinal's accounting practices violated Sarbanes-Oxley and that three Cardinal employees were "parties to fraudulent acts." Pet. App. 7a. Petitioner also proposed leaving Cardinal quietly in exchange for a generous severance package. *Ibid.* Following the meeting, Densmore and Larrowe attempted to meet with petitioner to discuss his allegations, but petitioner refused to meet without his personal attorney being present. *Ibid.*

On September 25, 2002, Cardinal's Board of Directors voted to suspend petitioner without pay pending the

results of Densmore and Larrowe's investigation. Pet. App. 7a. The Board of Directors ordered petitioner to meet with Densmore and Larrowe without his attorney, but petitioner again refused. *Id.* at 7a-8a.

On October 1, 2002, Densmore and Larrowe informed the Board of Directors that, based on their investigation, petitioner's allegations regarding Cardinal's accounting practices lacked merit. Pet. App. 8a. They also informed the Board of Directors that petitioner had breached his fiduciary duty to Cardinal by refusing to meet with them to discuss his allegations without his personal attorney. *Ibid.* The Board of Directors voted unanimously to accept Densmore and Larrowe's recommendation that Cardinal discharge petitioner. *Ibid.*

Following his discharge, petitioner filed a complaint under Section 806(a) of Sarbanes-Oxley with the Department of Labor, alleging that Cardinal had retaliated against him because of his complaints to Moore and others about Cardinal's accounting practices. After an investigation, petitioner's complaint was dismissed, and he requested a hearing before an ALJ. Pet. App. 9a; 29 C.F.R. 1980.106.

3. The ALJ concluded that petitioner had demonstrated by a preponderance of the evidence that Cardinal terminated his employment in violation of Section 806(a) of Sarbanes-Oxley. Pet. App. 47a-203a. The ALJ determined that three of petitioner's complaints were protected under Section 806(a): (1) that two loan recoveries were improperly recorded as income in Cardinal's ledger entries; (2) that his access to Larrowe & Co. was restricted: and (3) that Cardinal had inadequate internal accounting controls because individuals lacking necessary auditing expertise made ledger entries without his knowledge or review. Pet. App. 141a-156a. The ALJ

further determined that the proximity in time between petitioner's protected activity and his termination created an inference of retaliation and established a causal connection between his protected activity and subsequent adverse actions. *Id.* at 157a-164a. The ALJ also determined that Cardinal had failed to establish by clear and convincing evidence that it would have taken the same action in the absence of retaliation. *Id.* at 164a-172a.

4. The Administrative Review Board reversed. Pet. App. 22a-46a. The Board concluded as a matter of law that petitioner failed to demonstrate that he had engaged in protected activity within the meaning of Section 806(a) of Sarbanes-Oxley. *Id.* at 33a-46a. First, the Board held that petitioner's complaints regarding the two loan recovery entries did not allege conduct that he reasonably could believe constituted a violation of the federal securities laws. *Id.* at 36a-37a. The Board stated that because Cardinal had recovered $195,000, "an experienced CPA/CFO like [petitioner] could not have reasonably believed that the third quarter SEC report presented potential investors with a misleading picture of Cardinal's financial condition." *Id.* at 37a. Second, the Board concluded that petitioner failed to provide legal authority to support his argument that the failure of Cardinal's financial records to comply with GAAP or other federal auditing standards constituted a violation of any law listed in Sarbanes-Oxley. *Id.* at 38a. Similarly, with regard to petitioner's complaints concerning his restricted access to Larrowe & Co. and Cardinal's inadequate internal accounting controls, the Board held that petitioner did not present any legal authority to explain how his concerns related to any violations of the federal securities laws. *Id.* at 40a-42a.

5. The court of appeals affirmed. Pet. App. 1a-21a. The court first held that the Board erred in concluding that misclassifying items in a financial statement could never mislead potential investors about a company's financial condition if the misclassification does not affect the "bottom line." *Id.* at 15a. The court, nevertheless, held that the Board appropriately dismissed petitioner's complaint based on the court's determination that petitioner "utterly failed to explain how Cardinal's alleged conduct could reasonably be regarded as violating any of the laws listed in § 1514A." *Id.* at 17a. The court of appeals accordingly held that the Board properly ruled that petitioner had failed to establish that his complaints constituted protected activity. *Ibid.*

ARGUMENT

The court of appeals' decision is correct and does not conflict with any decision of this Court or any other court of appeals. Further review therefore is not warranted.

1. Sarbanes-Oxley was enacted on July 30, 2002, to restore investor confidence in the nation's financial markets after the financial scandals of such corporations as Enron and WorldCom. To further the purposes of promoting corporate responsibility and public disclosure and improving the quality and transparency of financial reporting and auditing, Sarbanes-Oxley provides whistleblower protections to employees of publicly traded companies who report corporate fraud. *Procedures for the Handling of Discrimination Complaints Under Section 806 of the Corporate and Criminal Fraud Accountability Act of 2002, Title VIII of the Sarbanes-Oxley Act*, 69 Fed. Reg. 52,104 (2004); *Carnero* v. *Boston Scientific Corp.*, 433 F.3d 1, 9 (1st Cir.), cert. denied,

548 U.S. 906 (2006). Under Section 806(a), publicly traded companies are prohibited from retaliating against an employee who provides information "regarding any conduct which the employee reasonably believes constitutes a violation of section 1341 [mail fraud], 1343 [fraud by wire, radio, or television], 1344 [bank fraud], or 1348 [securities fraud], any rule or regulation of the Securities and Exchange Commission, or any provision of Federal law relating to fraud against shareholders." 18 U.S.C. 1514A(a)(1).

To prevail on a retaliation complaint under Section 806(a), a complainant must prove by a preponderance of the evidence that (1) he engaged in protected activity; (2) the employer was aware of the protected activity; (3) he suffered an adverse employment action; and (4) the protected activity was a contributing factor in the unfavorable action. 18 U.S.C. 1514A(b)(2)(C); 49 U.S.C. 42121(b)(2)(B)(iii)-(iv); *Allen* v. *Administrative Review Bd.*, 514 F.3d 468, 475-476 (5th Cir. 2008).

To establish that he engaged in protected activity, the employee must demonstrate that he had both a subjective and an objectively reasonable belief that the conduct of which he complained constituted a violation of one of the laws listed in Section 806. *Livingston* v. *Wyeth, Inc.*, 520 F.3d 344, 352 (4th Cir. 2008); *Allen*, 514 F.3d at 477. The employee also must demonstrate that his communications "definitively and specifically" related to one of the relevant laws. *Platone* v. *United States Dep't of Labor*, 548 F.3d 322, 326 (4th Cir. 2008); *Allen*, 514 F.3d at 476-477.

2. Petitioner argues (Pet. 16-22) that this Court's review is warranted because the court of appeals' decision conflicts with the plain language and remedial purposes of Sarbanes-Oxley and "constricts the 'protected

activity' cognizable under Section 806 to such an extent as to repeal the statute altogether." Pet. 22. Petitioner also argues (Pet. 23) that this Court should grant review to send a signal "to the corporate community about responsible, transparent financial reporting in the post-Enron era." Neither contention has merit.

a. Contrary to petitioner's suggestion, the court of appeals' narrow, fact-bound holding does not nullify the remedial purposes of Sarbanes-Oxley's whistleblower provision. The court of appeals correctly upheld the Board's conclusion that petitioner failed to demonstrate that he provided information to his employer that he reasonably believed constituted a violation of one of the enumerated laws under Section 806(a). Pet. App. 15a-18a. In so holding, the court clarified that it was not suggesting "that a whistleblower must identify specific statutory provisions or regulations when *complaining of conduct to an employer*." *Id.* at 17a-18a (emphasis added). Rather, the court agreed with the Board that petitioner had failed to articulate *to the Board* any basis for an objectively reasonable belief that the concerns that he raised to Cardinal about the company's accounting practices constituted violations of the securities laws. The court of appeals explained that petitioner, before the Board, cited "irrelevant and inapposite authority" and "made conclusory, general statements" in support of his arguments. *Id.* at 17a.

The Board rejected petitioner's suggestion that "accounting errors were ipso facto violations of the federal securities laws." Pet. App. 38a. Because not every misapplication of GAAP or another accounting standard will constitute a violation of SEC rules, it was incumbent upon petitioner to articulate to the Board that he had a reasonable belief that Cardinal's failure to comply with

a particular standard constituted a violation of one of the laws enumerated in Section 806.[1] Cf. *Day* v. *Staples, Inc.*, No. 08-1689, 2009 WL 294804, at *12 (1st Cir. Feb. 9, 2009). Because petitioner failed to explain his legal argument in that regard, the Board appropriately determined that he had not demonstrated that he had engaged in protected activity. See *Viking Supply* v. *National Cart Co.*, 310 F.3d 1092, 1099 (8th Cir. 2002) ("[I]t is not this court's job to research the law to support an appellant's argument.") (citations omitted); *APS Sports Collectibles, Inc.* v. *Sports Time, Inc.*, 299 F.3d 624, 631 (7th Cir. 2002) ("[I]t is not this court's responsibility to research and construct the parties' arguments.") (citations omitted); see also *Hall* v. *United States Dep't of Labor*, 476 F.3d 847, 861 n.8 (10th Cir.) ("The [Board] cannot be charged with reviewing the entire record to glean and *sua sponte* raise legal theories referenced only obliquely by a party but not clearly articulated in its briefs or ruled on by the ALJ."), cert. denied, 128 S. Ct. 489 (2007).[2] Moreover, as the court of appeals recog-

[1] Petitioner argued before the Board that when Cardinal misclassified its loan recoveries as income rather than crediting the loan reserve account, it failed to adhere to GAAP, generally accepted auditing standards (GAAS), and accounting rules established by the Financial Institutions Examination Council (FIEC) for banks. See 12 U.S.C. 3301 *et seq.* Pet. App. 37a-38a. Petitioner, however, never articulated how, under the circumstances of this case, he had a reasonable belief that Cardinal's failure to comply with GAAP, GAAS, or FIEC constituted a violation of the federal securities laws. *Ibid*.

[2] The court of appeals rejected an alternative conclusion of the Board that petitioner could not have had an objectively reasonable belief that reporting the $195,000 in recovered loans as income violated one of the laws enumerated in Section 806. Pet. App. 14a-15a. With regard to the loan recoveries, the Board had suggested that a misclassification on a financial statement cannot present potential investors with a misleading

nized (Pet. App. 17a), to the extent that petitioner explained his position and cited relevant authority for the first time in his filings before the court, he forfeited the arguments by failing to raise them to the Board. *Taylor* v. *United States Dep't of Labor*, 440 F.3d 1, 8-9 (1st Cir. 2005).[3]

b. Petitioner does not argue that the unanimous court of appeals' decision conflicts with the decision of any other court of appeals or any decision of this Court. Petitioner nonetheless contends (Pet. 23) that this Court's review is warranted because the decision below "weakens" whistleblower protections under Sarbanes-Oxley and sends a "troublesome" signal to the corporate community concerning its responsibilities for transparent financial reporting in the post-Enron era. The

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picture of a company's financial condition as long as the company in fact recovered more money than it had previously. *Id*. at 37a. In an amicus brief to the court of appeals, the SEC expressed some concern with that suggestion. *Id*. at 15a. As the court of appeals indicated, however, the Department of Labor has conceded that "communications about misclassifications in financial statements *may*, in some circumstances, form the basis for a Sarbanes-Oxley whistleblower action." *Ibid*. Accordingly, petitioner's concerns (Pet. 22-23) that the court of appeals' decision will frustrate Congress's intent to protect whistleblowers who expose corporate fraud are unfounded.

[3] Similarly, in this Court petitioner generally argues that banks must follow GAAP and that the securities laws prevent the filing of reports that misrepresent the financial condition of the company. Pet. 10, 19. But the Board concluded in this case that there was no reasonable basis to conclude that Cardinal's failure to follow GAAP in the third-quarter report rendered the report misleading, because "Cardinal had in fact recovered $195,000 that it previously did not have." Pet. App. 37a. Petitioner does cite to an SEC rule that presumes that filed financial statements not prepared in compliance with GAAP are presumed to be misleading, 17 C.F.R. 210.4-01(a)(1), but petitioner failed to cite that rule before the Board.

court's decision, however, simply affirms the unremarkable principle that in proving a retaliation case, a complainant must adequately explain to the tribunal before which his case is being heard the legal basis for his claim that he engaged in protected activity. The court's decision does not merit this Court's review.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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