



Issue Date: 16 February 2011

CASE NO.: 2010-SOX-00055

IN THE MATTER OF

MARC M. TWYMAN
Complainant

V.

TAXMASTERS, INC.
Respondent

**DECISION AND ORDER GRANTING RESPONDENT'S
MOTION FOR SUMMARY JUDGMENT**

On January 6, 2011, Respondent filed a Motion for Summary Judgment contending first that Complainant failed to show he ever (1) engaged in protected activity under the Sarbanes – Oxley Act of 2002, technically known as the Corporate and Criminal Fraud Accountability Act, P.L. 107-204 at 15 U.S.C. § 1514A *et seq.*, (herein SOX or the Act) or (2) reported anything he reasonably believed constituted a violation of SOX.

SOX is federal legislation designed to protect employees from discharge or other forms of adverse employment discrimination concerning wages, hours, or working conditions because said employee engaged in a protected activity. The Act protects those employees who provide information about corporate fraud against shareholders to supervisors, federal agencies, or members of Congress. Further, the information provided must relate to conduct the employee reasonably believes is a violation of [18 U.S.C.] Section 1341 (mail fraud), 1343 (wire fraud), 1134 (bank fraud), or 1348 (securities fraud); any rule or regulation of the Securities and Exchange Commission; or any federal law relating to shareholder fraud. Respondent argues that Claimant's alleged protected activity, complaints to his supervisors, at most amount to a disagreement with sales practices and the language used in connection therewith and that these actions do not constitute protected activity. Thus, Respondent argues, it is entitled to judgment as a matter of law.

According to Respondent's argument, when reporting such information Complainant must both subjectively and objectively reasonably believe that the conduct complained of constitutes a violation of a law, rule, or regulation as set forth in the Act. Complainant's statements to prospective clients both before and after he made his whistleblower complaint

demonstrate that he did not subjectively believe in the allegations he set forth. Further, Complainant lacked either the training or experience to prove any of his allegations. Moreover, the company's CEO and vice president of quality assurance investigated and found Claimant's allegations to be untrue. After this information was presented to Claimant, he had no objective basis to reasonably believe the truth of said allegations. Respondent also argues that, even assuming Complainant's actions were protected under SOX, Complainant's consistent failure to meet minimum weekly sales justifies his discharge and shows the actions against him would have occurred in the absence of his complaints.

In reply to Respondent's motion, Complainant asserts that the motion relies upon bogus, mischaracterized, and faulty evidence and conclusions. In addition, Complainant argues that the language of Section 1514A is clear and unambiguous and, therefore, should be broadly interpreted to include his complaints. In accord with the intent of SOX, employees are not subject to penalties if they report what they believe to be violations of law. Complainant further asserts he was fired for complaints made in January of 2010 about reports made to the SEC. Specifically, Complainant alleged that Respondent sent inflated and fraudulent information to the SEC by reporting that it had a ninety-seven percent (97%) customer satisfaction rating and that it employed three-hundred (300) tax resolution experts. Complainant also argues that the complaints referenced the impropriety of certain business practices which was confirmed by a lawsuit against Respondent filed by the Texas Attorney General on May 13, 2010. This law suit charged Respondent with violations of Texas State law through misleading customers about service contract terms, about its no refund policy, and about its policy not to start work on cases until customer paid in full for services. (Complainant's exhibit 3 attached to his motion to strike Respondent's first affirmative defense).

Complainant also asserts Respondent engaged in fraud on its shareholders by failing to tell them about the law suit filed by the Texas Attorney General on May 13, 2010, and by permitting employees to tell potential customers that claims could be settled for a few cents on the dollar and by telling the SEC, in August 2009, that it was unaware of any circumstances that would cause a third party to initiate proceedings against it. Complainant then points to the value of Respondent's stock as listed on the NASDAQ as follows: 83.5 cents per share on May 12, 2010; 38 cents per share on August 31, 2010, and 30 cents per share on November 10, 2010.

Concerning his discharge on June 22, 2010, Complainant notes that prior to his complaint to Respondent's CEO in January, 2010, he was written up about once per year for poor sales and compares this to the five month period between his complaint and termination (from January 19, 2010, to June 22, 2010) when he was written up five (5) times for low sales. Claimant asserts he was not allowed to conduct daily prospecting but was micromanaged and limited on the amount and quality of his leads during this time period thereby diminishing his sales. Also, during this period he earned more than the minimum expected of him and when discharged had a better sales record than others who were kept on.

The standard for granting summary judgment or decision is set forth at 20 C.F.R. §18.40(d) which is derived from Federal Rule of Civil Procedure (FRCP) 56. Section 18.40(d) permits an Administrative Law Judge to enter summary decision "if the pleadings, affidavits, material obtained by discovery or otherwise, or matters officially noticed show there is no

genuine issues as to any material fact and that a party is entitled to summary decision.” 20 C.F.R. §18.40(d) (1994). A “material fact” is one whose existence affects the outcome of the case. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986). And, a “genuine issue” exists when the non-movant produces sufficient evidence of a material fact so that a fact finder is required to resolve the parties’ differing versions at trial. *Id.* at 249.

In deciding a motion for summary decision, the Court must consider all the material submitted by both parties, drawing all reasonable inferences in a matter most favorable to the non-movant. *Adickes v. S.H. Kress & Co.*, 398 U.S. 144, 158-159 (1970). In other words, the Court must look at the record as a whole and determine whether a fact-finder could rule in the non-movant’s favor. *Matsushita Elec. Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587. The movant has the burden of production to prove that the non-movant cannot make a showing sufficient to establish an essential element of the case. *Celotex Corp. v. Catrett*, 477 U.S. 317, 322 (1986). Once the movant has met its burden of production, the non-movant must show by evidence beyond the pleadings themselves that there is a genuine issue of material fact. *Id.* at 324. If the non-movant fails to sufficiently show an essential element of his case, there can be “no genuine issue as to any material fact,” since a complete failure of proof concerning an essential element of the non-movant’s case necessarily renders all other facts immaterial.” *Id.* at 322-323. In a SOX case, there are four essential elements which a Complainant must prove by a preponderance of evidenced; (1) engagement in protected activity; (2) employer knowledge of protected activity; (3) adverse employment action upon complainant by employer; and (4) circumstances showing protected activity to be a contributing factor to the adverse employment action.

The purpose of the employee protection provisions of SOX is to protect employees of publicly traded companies who provide information or assist in an investigation regarding any conduct which the employee reasonably believes constitutes a violation of various federal fraud provisions, including Sections 1341 (fraud and swindles), 1342 (fraud by wire, radio, or television), 1344 (bank fraud), or 1348 (securities fraud), or 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; 29 C.F.R. §1980.102(a); *Hendrix v. American Airlines, Inc.*, 2004-AIR-00010 and 2004-SOX-00023 (ALJ Dec. 9, 2004).

The information or assistance must be provided to or the investigation must be conducted by a federal regulatory or law enforcement agency, any member of Congress, or any committee of Congress, or a person with supervisory authority over the employee (or such other person working for the employer who has the authority to investigate, discover, or terminate misconduct.). 18 U.S.C. §1514A(a)(1); See also, 29 C.F.R. §1980.102(a)(1). An employer may not discharge, demote, suspend, threaten, harass, or in any other manner discriminate against an employee in the terms and conditions of employment because of any lawful act done by the employee under the Act’s protection. *Id.*

Protected activity under SOX is defined as reporting an employer’s conduct which the employee reasonably believes constitutes a violation of the laws and regulations related to fraud against shareholders. *Marshall v. Northrup Gruman Synoptics*, 2005-SOX-00008 (ALJ June 22, 2005). The employee’s belief must be scrutinized under both subjective and objective standards. *Id.*, citing *Melendez v. Exxon Chemicals Americas*, ARB No. 96-051 (July 14, 2000). The

employee does not need to show that the employer's conduct actually caused a violation of the law, but must show that he reasonably believed the employer violated one of the laws or regulations enumerated under SOX or any rule or regulation of the Securities and Exchange Commission, or any provision of federal law relating to fraud against shareholders. *Id.*; See also, 18 U.S.C. §1514A; 29 C.F.R. §1980.102(a); *Hendrix v. American Airlines, Inc.* at 9. In addition, the communicated information must “‘definitively and specifically relate’ to one of the six enumerated categories found in § 1514A.” *Allen v. Administrative Review Board, U.S. Dept. of Labor*, 514 F.3d 468, 475 (5th Cir. 2008) (quoting *Platone v. FLYI, Inc.*, ARB Case No. 04-154, 2006 WL 3246910, at *8 (ARB Sept., 2006).

Protected activity under SOX is thus essentially comprised of three elements: (1) report or action that involves a purported violation of a federal law or SEC rule or regulation relating to fraud against shareholders; (2) complainant's belief concerning the activity must be subjectively and objectively reasonable; and (3) complainant must communicate his concern to either his employer, the federal government or a member of Congress. See, *Harvey v. Safeway, Inc.*, 2004-SOX-21 at 29 (ALJ Feb. 11, 2005).

Fraud is an integral element of a SOX claim, which necessarily includes an implicit element of deceit that would impact shareholders or investors. *Marshall v. Northrup Gruman Synoptics* at 4. Materiality is likewise an integral element of a SOX claim. Section 302 of SOX specifically “establishes a requirement for the accuracy of material facts relating to finances.” *Harvey v. Safeway, Inc.* at 31 (emphasis in original). This provision particularly “demonstrates Congress’ intention to protect shareholders by requiring accurate reporting of significant information concerning a corporation’s financial condition.” *Id.* (emphasis in original). Stated differently, the Act “was not intended to capture every complaint an employee might have as a potential violation of the Act.” *Id.* at 4. Instead, the “goal of the legislation was to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws.” *Id.* In order to successfully maintain an allegation of a violation of SOX, a complainant's belief as to a violation of SOX must be reasonable from the outset, (*Bechtel v. Competitive Industries, Inc.* at 31), or complainant may show that he actually believed the activity to be violative of SOX at the time of his complaint. *Lerbs v. Buca Di Beppo, Inc.*, 2004-SOX-8 (ALJ June 15, 2004). SOX does not apply to generic allegations of accounting violations, violations of GAAP, or general allegations of fraud. See, *Marshall v. Northrup Gruman Synoptics* at 5 (stating that, “The fact that the concerns involved accounting and finances in some way does not automatically mean or imply that fraud or any other illegal conduct took place.”). Rather, applicability of SOX is limited to specifically enumerated laws or regulations related to fraud against shareholders. *Id.* at 3.

A review of the communications sent by Complainant to his supervisors shows that Complainant reported the following activities (1) fraudulent sales practices, (CX-15, p. 11); (2) posting misleading information on the company website, (CX-15, p. 11); (3) managerial incompetence including dismissing complaints, threats, and taunts, (CX-15, p. 5); and (4) false and misleading information included on an SEC filing FORM K-8 disclosure, (CX-16, pp. 2-5).¹

¹ Complainant refers to FORM K-8, but it appears he is referring to SEC FORM 8-K. Further, there is no listing of such a form filed on 8/24/09 as stated by Complainant. As a result, the undersigned will assume for purposes of this decision Complainant is referring to an actual filing and the foregoing is simply a clerical error.

Moreover, in his response motion Complainant avers his actions constitute protected activity as defined by Section 1514A because he reported (1) “‘companywide’ fraud within a publicly traded company”; (b) “that there was a conspiracy to commit fraud”; (c) “that the fraud was creating a risk factor that was not being disclosed to investors”; (d) “materially false and misleading statements being made on the company website which would in fact be a violation of ‘Rule 10b-5’”; and (e) materially false and misleading statements being made on SEC Submissions which would in fact be a violation of ‘Rule 10b-5.’”

Disagreements between an employee and employer regarding matters such as sales practices, managerial incompetence, and information contained in advertisements directed at consumers even if deliberate, intentional, and widespread do not constitute fraud on shareholders but at most consumer deception. Complainant’s reporting of managerial incompetence is clearly outside the intended scope of the SOX act. In addition, I find reporting a disagreement over proper sales techniques, methods, and terminology; any other alleged fraudulent sales practices; and the posting of misleading information on a company website to be outside of activity protected by SOX. In these situations, even if true, the fraud alleged by Complainant is directed at consumers not shareholders and does not relate to the financial condition of the company. Therefore, Complainant’s reporting of these activities cannot be considered protected activity under the Act as he cannot establish the reasonableness of a belief that a SOX covered violation occurred.

Regarding Complainant’s reporting of alleged violations of SEC Rule 10b-5, I also find Complainant has failed to establish this constitutes protected activity. Even assuming the information was intentionally misstated on the SEC filings SEC Rule 10b-5 provides as follows:

- It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
- (a) To employ any device, scheme, or artifice to defraud,

 - (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

 - (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5 (2005).

In a cause of action for securities fraud, such as a violation of Rule 10b-5, the basic elements include a material misrepresentation, scienter, a connection with the purchase or sale of

a security, reliance, economic loss and a causal connection between the loss and the material misrepresentation. *Platone v. FLYI, Inc.*, ARB Case No. 04-154, 2006 WL 3246910, at *16 (ARB Sept., 2006) (citing *Dura Pharm. Inc. v. Broudo*, 544 U.S. 336, 341-41 (2005)). A fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote. *Id.* (citing *Basic v. Levinson*, 485 U.S. 224, 231-32 (1998)). The statements made by Complainant to Respondent simply do not relate to the purchase or sale of a security, nor do the statements reference any fraudulent, or even intentional, misstatements that could in any reasonable manner be considered material.

As the ARB has held, “the mere possibility that an act or omission could adversely affect [Respondent’s] financial condition and thus affect shareholders is not enough to bring the Complainant’s concerns under [SOX] protection.” *Allen v. Stewart Enterprises, Inc.*, ARB No. 06-081, ALJ Nos 2004-SOX-60, 61, 62 (ARB July 27, 2006). Further, Complainant has failed to show or explain how his complaints “provided information he reasonably believed constituted a violation of the federal fraud statutes, or an SEC rule or regulation, or any other federal law relating to shareholder fraud.” *Reddy v. Medquist, Inc.*, ARB No. 04-123, ALJ No. 2004-SOX-35 (ARB Sept. 30, 2005).

Therefore, I find Complainant has not shown and cannot show a reasonable belief that the information he reported constituted a violation of a provision enumerated in SOX and, thus, has not alleged an activity protected under SOX. Accordingly, I **GRANT** Respondent’s claim for summary judgment as Complainant has failed to allege an essential element of his case. However, under the circumstances of this case, I **DENY** Respondent’s request for monetary claims against Complainant as his action in bringing this complaint was not frivolous.

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**CLEMENT J. KENNINGTON
ADMINISTRATIVE LAW JUDGE**

NOTICE OF APPEAL RIGHTS: To appeal, you must file a Petition for Review ("Petition") with the Administrative Review Board ("Board") within ten (10) business days of the date of issuance of the administrative law judge's decision. The Board's address is: Administrative Review Board, U.S. Department of Labor, Suite S-5220, 200 Constitution Avenue, NW, Washington DC 20210. In addition to filing your Petition for Review with the Board at the foregoing address, an electronic copy of the Petition may be filed by e-mail with the Board, to the attention of the Clerk of the Board, at the following e-mail address: ARB-Correspondence@dol.gov.

Your Petition is considered filed on the date of its postmark, facsimile transmittal, or e-mail communication; but if you file it in person, by hand-delivery or other means, it is filed when the

Board receives it. *See* 29 C.F.R. § 1978.110(a). Your Petition must specifically identify the findings, conclusions or orders to which you object. You waive any objections you do not raise specifically. *See* 29 C.F.R. § 1978.110(a).

At the time you file the Petition with the Board, you must serve it on all parties as well as the Chief Administrative Law Judge, U.S. Department of Labor, Office of Administrative Law Judges, 800 K Street, NW, Suite 400-North, Washington, DC 20001-8002. You must also serve the Assistant Secretary, Occupational Safety and Health Administration and, in cases in which the Assistant Secretary is a party, on the Associate Solicitor for Occupational Safety and Health. *See* 29 C.F.R. § 1978.110(a).

You must file an original and four copies of the petition for review with the Board, together with one copy of this decision. In addition, within 30 calendar days of filing the petition for review you must file with the Board: (1) an original and four copies of a supporting legal brief of points and authorities, not to exceed thirty double-spaced typed pages, and (2) an appendix (one copy only) consisting of relevant excerpts of the record of the proceedings from which the appeal is taken, upon which you rely in support of your petition for review.

Any response in opposition to a petition for review must be filed with the Board within 30 calendar days from the date of filing of the petitioning party's supporting legal brief of points and authorities. The response in opposition to the petition for review must include: (1) an original and four copies of the responding party's legal brief of points and authorities in opposition to the petition, not to exceed thirty double-spaced typed pages, and (2) an appendix (one copy only) consisting of relevant excerpts of the record of the proceedings from which appeal has been taken, upon which the responding party relies, unless the responding party expressly stipulates in writing to the adequacy of the appendix submitted by the petitioning party.

Upon receipt of a legal brief filed in opposition to a petition for review, the petitioning party may file a reply brief (original and four copies), not to exceed ten double-spaced typed pages, within such time period as may be ordered by the Board.

If no Petition is timely filed, the administrative law judge's decision becomes the final order of the Secretary of Labor pursuant to 29 C.F.R. §§ 1978.109(e) and 1978.110(a). Even if a Petition is timely filed, the administrative law judge's decision becomes the final order of the Secretary of Labor unless the Board issues an order within thirty (30) days of the date the Petition is filed notifying the parties that it has accepted the case for review. *See* 29 C.F.R. §§ 1978.110(a) and (b).