

IN THE UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF VIRGINIA
ROANOKE DIVISION

DAVID E. WELCH,)
)
Plaintiff)
)
v.)
)
CARDINAL BANKSHARES) Case No. 7:06CV00407
CORPORATION,)
)
Defendant.)
)

MEMORANDUM OF LAW OF AMICUS CURIAE AMERICAN
ASSOCIATION OF BANK DIRECTORS IN SUPPORT OF MOTION TO DISMISS

Amicus Curiae American Association of Bank Directors ("AABD"), by counsel, submits this memorandum of law in support of the Motion to Dismiss filed by Defendant Cardinal Bankshares Corporation ("Cardinal").

STATEMENT OF AMICUS INTEREST

AABD is an organization which represents the interests of directors of financial institutions. It is devoted to serving the information, education and advocacy needs of directors of financial institutions. Specifically, AABD represents the interests of directors of financial institutions before judicial bodies in order to advance the cause of eliminating directors' personal liability for damages resulting from events that are beyond the control of directors. AABD also seeks to minimize limitations on the authority of boards of directors to supervise their institutions effectively.

As stated in AABD's previously filed motion for leave to participate as amicus, this case involves a number of issues that are of vital importance to AABD's membership. With respect to the jurisdiction issue now before the Court, AABD is

concerned that enforcement of interim orders of reinstatement by the Department of Labor (“DOL”) would create a “revolving door” of discharge and reinstatement in sensitive positions at financial institutions. This, in turn, would disrupt the stability needed in such positions, and would impair the ability of bank directors to effectively supervise their institutions. Small public institutions, of which many are community banks like Cardinal, would be particularly disadvantaged by this revolving door. AABD therefore submits this brief in support of Cardinal’s Motion to Dismiss.

ARGUMENT

The question now before the Court is whether Section 804 of the Sarbanes Oxley Act of 2002 (“SOX”), 18 U.S.C. § 1514A, confers jurisdiction on federal district courts to enforce preliminary orders of the Secretary of Labor (“Secretary”). AABD agrees with Defendant Cardinal that it does not. AABD will not, however, repeat the arguments made by Cardinal on brief and at the hearing conducted on September 25, 2006 on this question. Rather, it writes separately to emphasize the public policy reasons that support Cardinal’s position, that counsel against enforcement of non-final orders of the Secretary, and that support the reasons why we believe Congress chose not to have such orders enforceable by the Federal courts in the context of SOX.¹

At the outset, is important to recognize the nature of the positions likely to be involved in SOX whistleblowing cases. Section 804 of SOX protects employees at public companies who complain about perceived violations of federal securities laws. 18 U.S.C. § 1514A. But in order to be in the position to “blow the whistle,” the employee

¹ While not at issue here, the AABD also opposes the reinstatement of a Chief Financial Officer of a public company by the DOL in a final order where such reinstatement is opposed by the board of directors who have responsibility to shareholders for the company’s financial reporting practices and who will lose their statutory immunity from personal liability when they rely on the imposed CFO’s work product.

first must have access to the financial data and reporting procedures involved in the claim. Such access is typically restricted to persons occupying positions of special trust and responsibility. In the context of financial institutions, this is likely to be senior accountants or executives. The present case underscores this fact. Plaintiff David Welch is the former Chief Financial Officer of Cardinal.

Such positions at financial institutions are not ones that can be filled overnight. This is particularly applicable to small banking institutions like Cardinal without backup staff to step in while the complaint winds its way through the various stages of DOL revisions. Such companies must go outside to fill these sensitive positions, and must do so as quickly as possible to preserve their ability to comply with accounting and reporting duties. It can be difficult to find a qualified replacement. The process includes significant involvement of the board of directors. In smaller markets, the candidate may need to relocate from a different geographic area. Even after commencing work at the financial institution, the transition period is not over. Such positions generally have a steep learning curve. An incoming senior accounting or financial officer such as a CFO, for example, must become knowledgeable about the policies and procedures of the institution. This process can take a significant amount of time. It may be months before the new officer is operating at anywhere near full strength.

These facts distinguish SOX from other whistleblowing statutes. A government employee who blows the whistle on a \$1000 toilet seat need not be in a position of great authority or responsibility. An employee of a trucking company who blows the whistle on a falsified driving log need not be a senior executive. And an employee who points out an OSHA violation might simply be a line worker. By contrast, an employee who

reports about a suspected securities law violation likely **does** occupy a more senior position at the respondent company—a position not easily re-filled, particularly if it is subject to the potential revolving door of DOL interim orders.

This is relevant to the jurisdiction issue because it shows that **Congress did not intend courts to enforce the DOL’s interim orders at each stage of the agency’s multi-tiered review of the case.** Congress contemplated that SOX cases would be in and out of the DOL within approximately one year. Within that one-year period, there are at least three points in time where the DOL issues orders regarding reinstatement: (1) in the preliminary order, issued after the initial investigation by the DOL, (2) in the Administrative Law Judge’s recommended decision and order, and (3) in the Administrative Review Board’s final order. These orders may contain conflicting rulings. Thus, as in this case, the “preliminary order” might find no liability. Of necessity, the respondent company fills the position in question. As in this case, the ALJ order—issued months after the order of the initial investigation—later might find liability. If enforced, the respondent company would then be required to change senior personnel. And this could change again upon a final decision from the ARB which could, in turn, reverse the reinstatement order.

In his opinion in Bechtel v. Competitive Technologies, Inc., 448 F.3d 469 (2d Cir. 2006), Judge Jacobs noted that immediate enforcement at each level of DOL review (such as that described above) would create a “ridiculous state of affairs:”

Given these successive levels of review, the absence of federal judicial power to enforce preliminary orders reasonable could serve to ensure that appeals work their way through the administrative system before the federal courts become involved. Moreover, if the result changes from one level of review to the next, immediate enforcement

at each level could cause a rapid sequence of reinstatement and discharge, and a generally ridiculous state of affairs.

Id. at 474. Accordingly, he found that there was no jurisdiction to enforce preliminary orders of the Secretary.

AABD submits that, in addition to being “ridiculous,” the state of affairs described by Judge Jacobs could have disastrous results for a respondent company and its board of directors. It simply is not feasible to expect a public company to turn over a CFO—or similar position of senior financial reporting or accounting responsibility—three times within the space of a single year. Doing so would leave the company without an effective CFO for most of that period. Furthermore, it would be difficult to attract suitable candidates for a CFO-type position if their tenure was subject to the ever-shifting opinions of the DOL about the former CFO’s whistleblowing case.

This is of great concern to AABD. In carrying out their oversight duties, Boards of Directors need to be able to rely upon senior officers of the corporation, particularly the CFO. And there needs to be continuity and stability in such positions—both to assure competence and to attract suitable candidates. This is particularly the case after the impact of SOX which underscores the importance of the effectiveness of the company’s financial reporting processes and disclosures. Enforcement of interim orders of the DOL would undermine these objectives by creating a potential “revolving door” for CFOs. It would deprive a public company of effective accounting personnel during the course administrative proceedings. This, in turn, would harm the company’s shareholders—the very persons for whose benefit Congress enacted SOX. AABD believes that Congress appropriately weighed the costs and benefits of enforcing interim reinstatement orders under SOX and concluded that they should not be

immediately enforceable. (The DOL, for its part, failed to cite **any** jurisdictional basis—either in its briefs or at oral argument—for this court to enforce the DOL’s interim orders.)

For all these reasons, Amicus Curiae American Association of Bank Directors respectfully prays that this Court grant Defendant Cardinal Bankshares Corporation’s Motion to Dismiss, and dismiss this action with prejudice.

American Association of Bank Directors

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CERTIFICATE OF SERVICE

I hereby certify that the foregoing Memorandum of Law of Amicus Curiae American Association of Bank Directors in Support of Motion to Dismiss is being filed electronically on September 28, 2006. Notice of this filing will be sent to all parties by operation of the Court's electronic filing system. Parties may access this filing through the Court's system.

s/ Arthur P. Strickland