

SEC Opens up the Toolbox to File First Stand-alone Whistleblower Retaliation Case



David Smyth

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Welcome back to Whistleblower Week here at *Cady Bar the Door*. It is a glorious time. Today we discuss [In re International Game Technology, Inc.](#), filed on September 29th. While it has [done this before](#) alongside other charges, here the Commission has filed its first stand-alone action enforcing the anti-retaliation provisions in Section 21F(h) of the Exchange Act.

Allegations

Here's [what the SEC alleges](#)

The WB's History

The Whistleblower joined International Game Technology ("IGT") in 2008. From September 2011 until October 2014, the Whistleblower's first-level supervisor was a vice-president (the "VP Supervisor") and his second-level supervisor was a c-level executive (the "Executive Supervisor"). He received positive written evaluations throughout his six-year run at the company, and his bonuses and grants were at or near the highest awarded for employees within his supervisor's group. In approving a retention bonus for the Whistleblower on July 24, 2014, the VP Supervisor wrote, "[The Executive Supervisor] and I both feel [the Whistleblower] is a flight risk. . . . He is very strategic to our whole . . . [p]rocess and the results we have had to date." The Whistleblower also had not been disciplined in any way before he was terminated in October 2014. By then, IGT had made him director of a division responsible for a spending budget of over \$700 million and supervising up to eleven direct reports.

IGT's Accounting Methodology

The Whistleblower's concerns at issue related to IGT's accounting for costs associated with refurbished used parts. Starting in June 2013, the Whistleblower led several projects concerning the profitability of IGT's used parts business. In particular, the Whistleblower evaluated whether it was cheaper to refurbish used parts using outside vendors or through internal refurbishment (the "Refurbishment Project"). The Whistleblower became concerned that the standard cost model for internally refurbished parts was arbitrarily inflated because the 35% standard cost did not consider actual costs, which may have been lower than the assigned 35% percentage cost of new parts. Though the Whistleblower was primarily focused on cost savings, he also concluded that the inflated costs were transferred between IGT's business segments and could result in inaccuracies in IGT's financial statements.

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Ultimately, the Whistleblower estimated that the discrepancy between the actual cost to refurbish the used parts and the standard cost allocated to Gaming Operations' cost of sales was approximately \$10 million, that these inaccuracies were material, and may have persisted for many years.

On July 30, 2014, the Whistleblower gave a presentation on the Refurbishment Project, during which he discussed the used parts cost model. According to the Whistleblower, he raised the possible impact of the cost model on the accuracy of the company's financial statements and had a heated disagreement with the Executive Supervisor on the issue. The Executive Supervisor then emailed the VP Supervisor, "I can't allow [the Whistleblower] to place those inflammatory statements into presentations, if there is no basis in fact." Two weeks later, the Executive Supervisor recommended that the Whistleblower be terminated. On August 19th, the Executive Supervisor notified IGT's then-CEO that he would terminate the Whistleblower.

WB's Complaint and Termination

On August 20th, the Whistleblower submitted a complaint on IGT's Integrity Action Line ("IAL"), an internal hotline for reporting grievances. The Whistleblower said, among other things: "Our internal game operations is paying more than the market rate for the repaired parts for the parts and more than the internal cost for the parts. Conversely, the depot is charging more for parts than it costs to repair them. In most cases, this would not be a problem, but the primary customer is internal. . . . The current system distorts the real accounting and reporting." The Whistleblower also later claimed he was retaliated against for raising these concern. Following the Whistleblower's IAL complaint, an HR representative directed the Executive Supervisor to put a "hold" on the existing plan to terminate the Whistleblower.

IGT conducted an internal investigation between August 20, 2014 and October 30, 2014. The investigation found that IGT's cost accounting model for used parts was appropriate and did not cause its reported financial statements to be distorted because IGT had a process to reconcile estimated repair costs with actual costs such that only actual costs were realized by the ultimate recipient.

During the investigation the Whistleblower was removed from two significant opportunities. The first was a project associated with IGT's integration with GTECH in anticipation of the merger of those two companies. The second was an annual global gaming industry convention attended by IGT's major vendors and suppliers. On October 30, 2014, IGT terminated the Whistleblower.

The SEC found that this conduct violated Section 21F(h) of the Exchange Act, the anti-retaliation provision of Dodd-Frank, and IGT was forced to pay a \$500,000 penalty to resolve the matter.

Hmmm.

It's easy to jump on IGT after the fact and say it shouldn't have done what it did to the Whistleblower here. And the "facts" above are only allegations, so maybe the truth was somewhat different from that described above. But the Whistleblower's profile here was that of a pretty strong employee. His performance reviews were good. Even more importantly, in my view, he had also just gotten a retention bonus in July 2014. *The company wanted him to stay*. With that backdrop, it's hard to see his recommended termination less than a month later, and his actual termination within three months, as anything but retaliation for raising the accounting issues to management's attention. If you're a company facing a similar situation, tread very carefully. Doing otherwise could prove to be very expensive.