
APPENDIX A

UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

SUMMARY ORDER

RULINGS BY SUMMARY ORDER DO NOT HAVE PRECEDENTIAL EFFECT. CITATION TO A SUMMARY ORDER FILED ON OR AFTER JANUARY 1, 2007, IS PERMITTED AND IS GOVERNED BY FEDERAL RULE OF APPELLATE PROCEDURE 32.1 AND THIS COURT'S LOCAL RULE 32.1.1. WHEN CITING A SUMMARY ORDER IN A DOCUMENT FILED WITH THIS COURT, A PARTY MUST CITE EITHER THE FEDERAL APPENDIX OR AN ELECTRONIC DATABASE (WITH THE NOTATION "SUMMARY ORDER"). A PARTY CITING TO A SUMMARY ORDER MUST SERVE A COPY OF IT ON ANY PARTY NOT REPRESENTED BY COUNSEL.

At a stated term of the United States Court of Appeals for the Second Circuit, held at the Thurgood Marshall United States Courthouse, 40 Foley Square, in the City of New York, on the 5th day of January, two thousand eighteen.

**PRESENT: DENNIS JACOBS,
REENA RAGGI,
CHRISTOPHER F. DRONEY,
*Circuit Judges.***

**WILLIAM T. ESREY, RONALD T. LEMAY,
*Plaintiffs-Appellants,***

-v.-

17-1599

**UNITED STATES OF AMERICA,
*Defendant-Appellee.***

FOR PLAINTIFFS-APPELLANTS:

GEORGE M. CLARKE III (*with* Mireille R. Oldak, Allison M. De Tal, and Daniel A. Rosen *on the brief*), Baker & McKenzie LLP, Washington, D.C. and New York, NY.

FOR DEFENDANT-APPELLEE:

ELIZABETH M. TULIS (*with* Christopher Connolly *on the brief*), Assistant United States Attorneys, *for* Joon H. Kim, Acting United States Attorney for the Southern District of New York, New York, NY.

Appeal from a judgment of the United States District court for the Southern District of New York (Oetken, *J.*).

**UPON DUE CONSIDERATION, IT IS
HEREBY ORDERED, ADJUDGED, AND
DECREED** that the judgment of the district court is
AFFIRMED.

William Esrey and Ronald LeMay (“the plaintiffs”) appeal from an order of the United States District Court for the Southern District of New York (Oetken, J.) dismissing for lack of subject matter jurisdiction their complaint against the United States under the Federal Tort Claims Act (“FTCA”), 28 U.S.C. §§2671–80. On de novo review, we affirm. *See Makarova v. United States*, 201 F.3d 111, 113 (2d Cir. 2000). We assume the parties’ familiarity with the underlying facts, the procedural history, and the issues presented for review.

The FTCA’s broad waiver of sovereign immunity for tort claims against the government is subject to several exceptions. *See Kosak v. United States*, 465 U.S. 848, 851–52, 104 S. Ct. 1519, 79 L. Ed. 2d 860 (1984). As relevant here, the FTCA does not waive sovereign immunity for claims “arising out of . . . misrepresentation.” 28 U.S.C. § 2680(h). For purposes of this exception, “a misrepresentation may result from the *failure to provide information*, as well as from [the] provi[sion] [of] information that is wrong.” *Ingham v. E. Air Lines, Inc.*, 373 F.2d 227, 239 (2d. Cir. 1967) (emphasis added). And the exception “applies to claims arising out of negligent, as well as intentional, misrepresentation.” *Block v. Neal*, 460 U.S. 289, 295, 103 S. Ct. 1089, 75 L. Ed. 2d 67 (1983).

The plaintiffs' complaint alleges that the Internal Revenue Service ("IRS"), in violation of the laws of New York, aided and abetted Ernst & Young ("EY") in breaching a fiduciary duty EY owed to the plaintiffs. Essentially, the plaintiffs claim that the IRS took steps to conceal from the plaintiffs the fact that EY was the subject of a criminal investigation that created a conflict of interest for EY in its representation of the plaintiffs in a civil audit before the IRS. The plaintiffs claim that they were injured by this concealment because, if they had known at the time of their audit that EY was under criminal investigation, they could have used that information to (1) convince their then-employer, an EY client that eventually terminated the plaintiffs over concerns arising from the audit, to instead terminate EY; and (2) pursue their arbitration claim against EY for fiduciary-duty breach in a more cost-effective manner.

"A plaintiff may not by artful pleading avoid [§ 2680(h) of the FTCA]." *Dorking Genetics v. United States*, 76 F.3d 1261, 1265 (2d Cir. 1996). "In determining the applicability of the § 2680(h) exception, a court must look, not to the theory upon which the plaintiff elects to proceed, but rather to the substance of the claim which he asserts." *Lambertson v. United States*, 528 F.2d 441, 443 (2d Cir. 1976).

Although the plaintiffs style their claim as one for "aiding and abetting a fiduciary-duty breach," the gravamen of that claim is that the IRS wrongfully withheld information from them. Indeed, in their

complaint, the plaintiffs allege that they suffered their principal injuries because the “IRS . . . helped EY to hide information” and “[a]s a result of . . . the IRS’s active concealment” of its criminal investigation and audit of EY’s tax practices. App’x at 8–9. The alleged conduct that was “essential” to the plaintiffs’ claimed injuries was the IRS’s non-communication of information. *Block*, 460 U.S. at 297. Accordingly, the claim “aris[es] out of . . . misrepresentation” under 28 U.S.C. § 2680(h), and no court is statutorily accorded jurisdiction to hear it.

The plaintiffs attempt to evade the misrepresentation exception by identifying two “non-concealment” acts that they allege in their complaint. Appellant’s Br. at 24. First, they point to allegations that the IRS removed the word “penalty” from a press release regarding the IRS’s audit of EY. Second, the plaintiffs contend that the IRS’s failure to prohibit EY from representing them in audit proceedings due to a conflict of interest was not an act involving a representation.

The plaintiffs’ arguments are unavailing. As to the first argument, the allegation that the IRS decided to remove the word “penalty” amounts to an allegation that the IRS misrepresented to the public the nature of the IRS’s concern with EY’s tax shelter practices. This claim centers on the “communication of information on which the recipient relies,” and is therefore barred by the misrepresentation exception. *Block*, 460 U.S. at 296. Similarly, the plaintiffs’ second argument fails, because the plaintiffs’ theory

is that by failing to prohibit EY from representing them, the “IRS . . . helped EY to hide information from [the] Plaintiffs[,] knowing that such information would have been critical to [the] Plaintiffs’ evaluation of whether to trust EY.” App’x at 8. This claim too concerns communicating information to the plaintiffs, and therefore the plaintiffs fail to allege “the breach of a cognizable duty owed to [them] which is ‘distinct from any duty to use due care in communicating information.’” *Dorking Genetics*, 76 F.3d at 1265 (quoting *Block*, 460 U.S. at 297).

We have considered the plaintiffs’ remaining arguments and find them to be without merit. For the foregoing reasons, we **AFFIRM** the judgment of the district court.

FOR THE COURT:
Catherine O’Hagan Wolfe,
Clerk of the Court

APPENDIX B

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

WILLIAM T. ESREY
and
RONALD T. LEMAY,

Plaintiffs,

16-CV-3019 (JPO)

-v-

OPINION AND ORDER

THE UNITED STATES
OF AMERICA,

Defendant.

J. PAUL OETKEN, District Judge:

Plaintiffs William T. Esrey and Ronald T. LeMay initiated this action on April 22, 2016, against the United States of America (the “Government”), alleging wrongdoing by the Internal Revenue Service (“IRS”), under the Federal Tort Claims Act (“FTCA”), 28 U.S.C. §§ 2671-80, for aiding and abetting a breach of fiduciary duty. (*See* Dkt. No. 1 (“*Compl.*”).) The Government moves to dismiss the Complaint for lack of subject matter jurisdiction pursuant to Federal Rule of Civil Procedure 12(b)(1) and for failure to state a claim

upon which relief may be granted under Federal Rule of Civil Procedure 12(b)(6). (Dkt. No. 18.) For the reasons that follow, the Government's motion is granted pursuant to Rule 12(b)(1).

I. Background

The following facts are taken from the Complaint and are presumed true for the purposes of this motion.

Plaintiffs are former executives of Sprint Corporation ("Sprint"). (Compl. ¶ 2.) Esrey served as Sprint's Chief Executive Officer from 1985 through 2003, and Sprint's Chairman from 1990 to 2003. (*Id.* ¶ 12.) LeMay served as Sprint's Chief Operating Officer from 1996 to 2003, except for a brief stint as Chairman and Chief Executive Officer of another company. (*Id.* ¶ 13.) As of 2002, Ernst & Young (EY), a global accounting firm, had been tax advisor and financial planner for Esrey for over two decades and for LeMay for over a decade. (*Id.* ¶ 14-15.) EY was also Sprint's certified public accountant while Plaintiffs were employed by Sprint. (*Id.* ¶ 17.)

On EY's advice, Plaintiffs engaged in two transactions relevant to the present dispute: a Contingent Deferred Swap ("CDS") transaction in 1999 and 2000 and a CDS Add-On transaction in 2000 and 2001. (*Id.* ¶ 18.) On February 26, 2001, knowing that Plaintiffs had entered into these transactions, the Sprint Board authorized new employment agreements with Plaintiffs. (*Id.* ¶ 58.)

In March 2002, the IRS initiated an audit of EY's promotion of certain tax shelters (the "Promoter Audit"). (*Id.* ¶ 19.) That same year, the IRS also began to audit taxpayers who had actually participated in those tax shelters (the "Investor Audits"). (*Id.* ¶ 21.) EY represented Plaintiffs before the IRS in connection with the Investor Audits. (*Id.* ¶¶ 22-23.) In June 2003, the IRS agents involved in the Promoter Audit informed EY that the IRS Criminal Investigation Division ("CID") was investigating the conduct of certain EY employees, and that the Promoter Audit team was sharing its documents with CID. (*Id.* ¶¶ 32, 44.) On June 21, 2002, the United States Attorney's Office for the Southern District of New York ("SDNY") informed EY that it was initiating an investigation into EY's conduct in promoting the tax shelters. (*Id.* ¶ 24.)¹ These investigations by the IRS, CID, and SDNY created a conflict of interest between EY and the Plaintiffs. (*Id.* ¶ 3.)

The Sprint Board became concerned about the conflict of interest between Plaintiffs and EY due to the audits of Plaintiffs, and, beginning in 2002,

¹ By May 2004, SDNY initiated a federal grand jury investigation into EY's sales of tax shelters. (*Id.* ¶ 37.) In May 2007, the grand jury indicted four EY employees for participating in a scheme to defraud the IRS by means of fraudulent tax shelters (*id.* ¶ 39), which led to their conviction on multiple charges, including tax evasion in connection with the tax shelters (*id.* ¶ 40). See *United States v. Coplan*, No. 07 Crim.453 (S.D.N.Y. May 7, 2009). The Second Circuit reversed two of the convictions and upheld the other two. (Dkt. No. 1 ¶ 40.) See *United States v. Coplan*, 703 F.3d 46 (2d Cir. 2012).

Sprint required Plaintiffs to certify every quarter that they had no intention to sue EY. (*Id.* ¶ 60.) In December 2002, Plaintiffs presented a solution to the conflict of interest problem to the Sprint Board, recommending that Sprint cease using EY as its auditor in order to resolve the potential conflict of interest between EY and Plaintiffs. (*Id.* ¶ 61.) And though EY knew that it was under criminal investigation for these actions and advice, it also met with the Sprint Board and told the Board that its advice to Plaintiffs was sound and its actions were proper. (*Id.*)

In the end, the Sprint Board agreed with Plaintiffs that the potential conflict of interest was too great, but concluded that firing EY would result in negative publicity. (*Id.* ¶ 63.) As a result, the Sprint Board asked for Plaintiffs' resignations instead. (*Id.* ¶ 64.) LeMay left Sprint in April 2003. (*Id.* ¶ 65.) Esrey left Sprint in May 2003. (*Id.*)

The gravamen of Plaintiffs' claim is that the IRS and EY hid information from Plaintiffs, preventing them from adequately defending themselves to the Sprint Board, which led to their forced resignations from Sprint in 2003. (Dkt. No. 1 ¶¶ 5-7, 58-65.) Plaintiffs did not know about the IRS criminal investigation of EY until May 25, 2004, when the investigation was publicly disclosed. (*Id.* ¶¶ 49-50.) But while EY was under criminal investigation by the IRS and SDNY for promoting fraudulent tax shelters, it was also representing Plaintiffs before the IRS, creating a conflict of interest and breaching its fiduciary duty to

Plaintiffs. (*Id.* ¶¶ 46-48.) Essentially, Plaintiffs’ claim is that the IRS knowingly participated in EY’s breach of its fiduciary duty in violation of the laws of New York (*id.* ¶ 73), through its “active concealment of the criminal investigations,” such that “Plaintiffs were unable to tell Sprint that EY’s tax shelter promotion activities were being criminally investigated” (*id.* ¶ 7). Esrey and LeMay seek \$42,550,000 and \$116,800,000, respectively.² (*Id.* at 12.)

Plaintiffs asserted administrative claims against the IRS, contending, among other thing, that alleged “concealment by the IRS of the criminal investigation [of EY] and the truth regarding the promoter audit of EY prevented Mr. Esrey from defending himself before the Sprint Board of Directors, and ultimately led to the Board choosing to retain EY, it’s [sic] certified public accounting firm, and forcing Mr. Esrey to resign as Chief Executive Officer of Sprint in 2003.” (Dkt. No. 20-1.) The IRS denied Plaintiffs’ administrative claims on October 22, 2015. (*See* Dkt. No. 20-2; Dkt. No. 20-4.)

II. Discussion

Although Defendants move to dismiss for failure to state a claim pursuant to both Rule 12(b)(1) and Rule 12(b)(6), a court presented with motions to dismiss under Rules 12(b)(1) and 12(b)(6)

² In September 2011, Plaintiffs initiated an arbitration action against EY, which led to an interim award in Plaintiffs’ favor on November 11, 2013, and a final award on February 17, 2014. (*Id.* ¶ 57.)

must resolve the former first. *Al Naham v. U.S. Dep't of State*, No. 14 Civ. 9974, 2015 WL 3457448, at *2 n.6 (S.D.N.Y. June 1, 2015) (citing *McKevitt v. Mueller*, 689 F. Supp. 2d 661, 664 (S.D.N.Y. 2010)).

“Generally, a claim may be properly dismissed for lack of subject matter jurisdiction where a district court lacks constitutional or statutory power to adjudicate it.” *Kingsley v. BMW of N. Am. LLC*, No. 12 Civ. 234, 2012 WL 1605054, at *2 (S.D.N.Y. May 8, 2012) (citing Fed. R. Civ. P. 12(b)(1)); *Makarova v. United States*, 201 F.3d 110, 113 (2d Cir. 2000)). In considering a motion to dismiss for lack of subject matter jurisdiction under Rule 12(b)(1), a court must accept as true all the material factual allegations contained in the complaint, but a court is “not to draw inferences from the complaint favorable to plaintiffs.” *See J.S. ex rel. N.S. v. Attica Cent. Sch.*, 386 F.3d 107, 110 (2d Cir. 2004). “A district court properly dismisses an action under Rule 12(b)(1) if the court lacks the statutory or constitutional power to adjudicate it.” *Garcia v. Lasalle Bank NA.*, No. 16 Civ. 3485, 2017 WL 253070, at *3 (S.D.N.Y. Jan. 19, 2017) (quoting *Cortlandt Street Recovery Corp. v. Hallas Telecommns. S.A.R.L.*, 790 F.3d 411, 416-17 (2d Cir. 2015)).

The scope of the Court’s jurisdiction over suits against the Government or its agencies is defined by “the terms of [the United States] consent to be sued in any court.” *F.D.I.C. v. Meyer*, 510 U.S. 471, 475 (1994) (alteration in original and internal quotation mark omitted) (quoting *United States v. Sherwood*,

312 U.S. 584, 586 (1941)). “Absent a waiver, sovereign immunity shields the Federal Government and its agencies from suit.” *Id.* The Government argues that the Court lacks subject matter jurisdiction over the present action because Plaintiffs’ claim does not fall within the FTCA’s limited waiver of sovereign immunity.

“The FTCA waives sovereign immunity—and thus authorizes claims for damages against the United States—where federal employees commit torts while acting within the scope of their employment.” *Asmah v. US Consulate Accra Ghana*, No. 15 Civ. 3742, 2016 WL 2993203, at *4 (S.D.N.Y. May 23, 2016) (citing 28 U.S.C. § 1346(b)(1)); *see also Kosak v. United States*, 465 U.S. 848, 851-52 (1984). But the FTCA contains a number of exceptions to the waiver, two of which the Government argues are relevant here: the exception for claims arising out of misrepresentation or deceit, *see* 28 U.S.C. § 2680(h); and the exception for claims arising in respect of the assessment of collection of taxes, *see id.* § 2680(c).

The FTCA’s waiver of sovereign immunity does not extend to “claim[s] arising out of . . . misrepresentation” or “deceit.” 28 U.S.C. § 2680(h). “[Section] 2680(h) applies to claims arising out of negligent, as well as intentional, misrepresentation.” *Block v. Neal*, 460 U.S. 289, 295 (1983). And, as is relevant here, it applies to cases alleging concealment, which “fall within the ‘misrepresentation’ or ‘deceit’ exceptions to the FTCA.” *Lipkin v. U.S. S.E.C.*, 468 F. Supp. 2d 614, 624 (S.D.N.Y. 2006); *see also Regnante v. Sec. &*

Exch. Officials, 134 F. Supp. 3d 749, 770 (S.D.N.Y. 2015) (“[A]llegations of . . . concealment . . . are barred by the doctrine of sovereign immunity.”). “In determining the applicability of the § 2680(h) exception, a court must look, not to the theory upon which the plaintiff elects to proceed, but rather to the substance of the claim which he asserts.” *Lambertson v. United States*, 528 F.2d 441, 443 (2d Cir. 1976).

Here, the Government argues that at “the heart of the complaint” is a “claim of improper concealment of material facts.” (Dkt. No. 19 at 11.) And while the claim is styled as “aiding and abetting a breach of fiduciary duty,” it is based on allegations that the IRS did so by helping EY “hide information” or “conceal” material facts, which led to Plaintiffs’ resignation from Sprint. (Compl. ¶¶ 6-7, 36, 42.) The Court agrees. The claims in the present case are analogous to those in *Regnante*, where the plaintiff alleged that the Securities and Exchange Commission’s “failure to disclose the actual amount of [a relevant] Sanction misrepresented material facts, concealed material facts, and was deceitful.” 134 F. Supp. 3d at 769. The court found that those claims against the Government that are “based on allegations of misrepresentation, concealment, deceit, and fraud,” are “barred by the doctrine of sovereign immunity” as within the § 2680(h) exception to the FTCA. 134 F. Supp. 3d at 770. *See also Thompson v. Peace Corps*, 159 F. Supp. 3d 56, 62 n.3 (D.D.C. 2016) (finding that defendant’s alleged failure to “disclose all relevant information regarding the anti-malarial drug, mefloquine,” even

where plaintiff “detrimentally relied on these omissions,” falls within § 2680(h)’s misrepresentation exception).

Plaintiffs attempt to distinguish this case by framing the Complaint as arising from the Government’s alleged knowing participation in EY’s breach of fiduciary duties and not based on any misrepresentation. (Dkt. No. 23 at 9.) But “[a] plaintiff may not by artful pleading avoid the statutory exceptions to the FTCA.” *Dorking Genetics v. United States*, 76 F.3d 1261, 1265 (2d Cir. 1996). Upon inspection, Plaintiffs’ claim that the Government participated in EY’s breach of fiduciary duty collapses into a claim that the IRS’s alleged concealment prevented Plaintiffs from learning about and then utilizing information that may (or may not) have changed the outcome of the Sprint Board meetings that led to their forced resignations.

Plaintiffs point to two non-concealment acts to form the basis for the claim of aiding and abetting a breach of fiduciary duty. First, Plaintiffs allege that the IRS initially insisted on using the word “penalty” in a press release announcing the settlement of the Promoter Audit. (*Id.* ¶¶ 33-34.) Fearing that this would be “discovered by clients,” in June 2003, EY offered to “sweeten the deal” if the IRS would remove the term “penalty” from the press release. (*Id.* ¶¶ 34-35.) EY paid a \$15 million penalty, where \$1.4 million was paid in exchange for the promise not to call the settlement a “penalty.” (*Id.* ¶ 36.) However, it is logically impossible for this act, which occurred in June 2003, to have harmed Plaintiffs’ ability to

defend themselves to the Board months earlier. (*See id.* ¶ 65 (“LeMay and Esrey left Sprint in April and May 2003, respectively.”).) Second, Plaintiffs argue that the IRS failed to follow its own procedures to resolve the conflict of interest between EY and Plaintiffs. (*See* Dkt. No. 23 at 17-20.) But internal agency guidance documents confer no rights on taxpayers. *See, e.g., Johnson Home Care Servs. v. United States*, No. 04 Civ. 0129, 2005 WL 2210661, at *7 (E.D.N.Y. Sept. 13, 2005) (“[T]he Internal Revenue Manual confers no rights on taxpayers.” (quoting *Olsen v. United States*, 326 F. Supp. 2d 184, 188 n.2 (D. Mass. 2004), *aff’d*, 414 F.3d 144 (1st Cir. 2005))).

Because Plaintiffs’ claim rests on allegations of concealment, it falls squarely within the § 2680(h) exception to the FTCA. *See Regnante*, 134 F. Supp. 3d at 770. And because the Court concludes that the Government prevails under § 2680(h), it does not undertake an analysis pursuant to § 2680(c). Nor is it necessary to address the parties’ argument regarding timeliness of the claims where the Court determines it lacks subject matter jurisdiction. *See Leskinen v. Halsey*, No. 12 Civ. 0623, 2013 WL 801128, at *5 (E.D.N.Y. Mar. 5, 2013) (“As this Court lacks subject matter jurisdiction, it does not address defendants’ other arguments in support of dismissal.”)

Because the Court grants the Government’s motion to dismiss for lack of subject matter jurisdiction, it is unnecessary to address its motion to dismiss for failure to state a claim.

III. Conclusion

For the foregoing reasons, the Government's motion to dismiss the Complaint pursuant to Rule 12(b)(1) is GRANTED.

The Clerk of Court is directed to close the motion at Docket Number 18 and close this case.

SO ORDERED.

Dated: March 23, 2017
New York, New York

/s/

J. PAUL OETKEN
United States District Judge

APPENDIX C

**UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW
YORK**

WILLIAM T. ESREY
and
RONALD T. LEMAY,

Plaintiffs,

-v-

THE UNITED STATES
OF AMERICA,

Defendant.

Civil Case No.:
1:16-cv-03019

COMPLAINT

INTRODUCTION

1. In 2002, the Internal Revenue Service (“IRS”) Criminal Investigation Division (“CID”) and the United States Attorney’s Office for the Southern District of New York (“SDNY”) began to investigate the promotion of tax shelters by Ernst & Young LLP (“EY”) to its clients. The IRS also began a civil audit of EY’s promotion of tax shelters to those same clients.

2. EY’s clients who had been sold these tax shelters included plaintiffs William T. Esrey (“Esrey”)

and Ronald T. LeMay (“LeMay”) (collectively, the “Plaintiffs”). At the time, Esrey was the Chief Executive Officer (“CEO”) of Sprint Corporation (“Sprint”), and LeMay was Sprint’s Chief Operating Officer (“COO”). In addition to the criminal and civil investigations of EY’s conduct, the IRS began audits of Esrey and LeMay in the 2002 timeframe.

3. EY knew during 2002 and 2003 that its conduct was under investigation by SDNY, CID, and/or IRS. These investigations created a conflict of interest between EY and the Plaintiffs.

4. In July 2003, EY settled the civil audit of its tax shelter promotion activities for \$15 million, which – unbeknownst to Esrey and LeMay at the time – included a \$1.4 million additional payment to induce the IRS not to call the \$15 million a “penalty” in the IRS press release.

5. EY withheld material information from Esrey and LeMay about the civil and criminal investigations of EY and EY’s agreement to resolve the IRS tax shelter promoter audit. As their long-standing tax advisor, EY owed the Plaintiffs fiduciary duties, including duties of candor, loyalty, and performance. Instead, EY represented to Plaintiffs that it would be able to favorably settle their individual audits and did not disclose the extent or seriousness of the investigations into its conduct. Plaintiffs reasonably relied on EY’s representations and advice and trusted that it was telling them the truth. Likewise, Plaintiffs relayed these representations to their employer, Sprint.

6. The IRS knew of EY's fiduciary duties to Plaintiffs, and of EY's conflict of interest, but nonetheless helped EY to hide information from Plaintiffs knowing that such information would have been critical to Plaintiffs' evaluation of whether to trust EY and whether to continue to tell Sprint that EY was trustworthy and devoted to helping Plaintiffs resolve their tax audits with the IRS. The IRS also permitted EY to continue to represent Plaintiffs before the IRS, notwithstanding that this continued representation violated Treasury Department Circular No. 230, 31 C.F.R. §§ 10.0-10.93 (2003).

7. As a result of EY's breach of fiduciary duty and of the IRS's active concealment of the criminal investigation and the truth about the tax shelter promoter audit, Esrey and LeMay could not defend themselves against allegations by Sprint and Sprint shareholders regarding their participation in the EY-promoted transactions. For instance, Plaintiffs were unable to tell Sprint that EY's tax shelter promotion activities were being criminally investigated. Instead, the blame for the tax shelters fell on Plaintiffs and they were ultimately forced to resign from Sprint in 2003.

JURISDICTION AND VENUE

8. This action arises under the Federal Tort Claims Act, 28 U.S.C. §§ 2671-80. This Court has jurisdiction over this case pursuant to 28 U.S.C. §§ 1346(b)(1) and 2674.

9. Venue is proper in this district pursuant to 28 U.S.C. §§ 1391(e) and 1402(b).

THE PARTIES

10. Plaintiff William T. Esrey is an individual with his residence at 1314 Spraddle Creek Road, Vail, CO 81657. Plaintiff Ronald T. LeMay is an individual with his residence at 1214 West 55th Street, Kansas City, MO 64112.

11. Defendant is the United States of America.

BACKGROUND

A. EY's Fiduciary Relationship with the Plaintiffs.

12. Esrey was employed by Sprint from 1980 through 2003. Esrey was Sprint's CEO from 1985 through 2003 and Sprint's Chairman from 1990 to 2003.

13. LeMay was employed by Sprint from 1985 through 2003. LeMay was Sprint's President and Chief Operating Officer from 1996 to 2003, except for a period of approximately one hundred days during which Mr. LeMay left Sprint to serve as Chairman and Chief Executive Officer of Waste Management, Inc.

14. EY is a global accounting firm and one of the largest accounting firms operating in the United States.

15. EY had been Esrey's tax advisor and financial planner for over two decades as of 2002. EY had been LeMay's tax advisor and financial planner for over one decade as of 2002.

16. EY was in a fiduciary relationship with Esrey and LeMay. That fiduciary relationship included the duty of candor, the duty of loyalty, the duty of performance, and the duty to act in the best interests of Esrey and LeMay.

17. During the time that Esrey and LeMay were employed by Sprint, EY was Sprint's certified public accountant.

18. On the advice of EY, Esrey and LeMay engaged in two transactions promoted by EY, the Contingent Deferred Swap ("CDS") transaction in 1999 and 2000 and the CDS Add-On ("Add-On") transaction in 2000 and 2001.

B. The IRS Investigations of EY.

19. The IRS initiated an audit of EY's promotion of certain tax shelters (the "Promoter Audit") in March 2002.

20. IRS employees conducting the Promoter Audit worked at an IRS office located in New York, New York.

21. During 2002, the IRS also began to audit taxpayers who had participated in tax shelters promoted by EY, including entities owned by Esrey and LeMay (the "Investor Audits"). IRS employees located in New York, NY worked on the Investor Audits.

22. EY represented Esrey and LeMay before the IRS in connection with the Investor Audits.

23. The IRS dealt directly with EY as representatives of Esrey and LeMay during the Investor Audits.

24. On June 21, 2002, the United States Attorney's Office for the SDNY informed EY that it was initiating an investigation into EY's conduct in promoting tax shelters.

25. At that time, EY retained Gerald Feffer ("Feffer"), an esteemed criminal tax lawyer with the law firm of Williams & Connolly.

26. On June 24, 2002, EY's General Counsel, Kathryn Oberly ("Oberly"), informed certain EY employees of the investigation and placed a litigation hold on all materials related to EY's promotion of tax shelter transactions (the "Litigation Hold").

27. On June 28, 2002, Shirah Neiman ("Neiman"), a senior Assistant U.S. Attorney at SDNY, contacted Oberly about the investigation. Neiman requested, among other things, a letter confirming that EY had placed a litigation hold on relevant documents and information about the criminal statute of limitations.

28. On July 2, 2002, Feffer faxed to Neiman a copy of the Litigation Hold pursuant to Neiman's June 28 request.

29. Prior to this litigation hold being put into place, EY personnel had already destroyed documents relating to EY's tax shelter activities.

30. On July 9, 2002, Neiman informed EY's criminal counsel that the IRS had declined to authorize the opening of a grand jury proceeding at

that time, but that her office would continue to monitor the matter. The Litigation Hold was never lifted.

31. Throughout 2003, the IRS CID pursued a criminal investigation of EY's conduct in promoting tax shelters.

32. In June 2003, IRS agents involved in the EY Promoter Audit told EY that CID was investigating the conduct of certain EY employees and that the Promoter Audit team was sharing documents with CID.

33. EY agreed in concept to settle the Promoter Audit with the IRS for approximately \$13 million.

34. During June 2003, EY and the IRS negotiated over use of the term "penalty" in the IRS press release announcing the settlement of the Promoter Audit. The IRS initially insisted that the word "penalty" be used to accurately describe the settlement payment in the IRS press release. EY told the IRS it was concerned that the fact it paid a penalty would be "discovered by clients" and used in litigation against EY. At least one in-person settlement meeting between EY and the IRS took place in New York.

35. Although the IRS's initial position was that use of the term "penalty" was not negotiable, the IRS changed its position and agreed to remove the term "penalty" from the press release if EY would "sweeten the deal."

36. On July 2, 2003, EY and the IRS settled the Promoter Audit. EY paid the IRS a \$15 million

penalty, which included a \$1.4 million increase in the payment in exchange for the IRS's agreement not to call that payment a "penalty" in the press release announcing the settlement. The IRS knowingly induced or participated in EY's breach of fiduciary duty when it helped EY conceal the true nature of its settlement payment.

37. By May 2004, SDNY had initiated a federal grand jury investigation of EY's sale of tax shelters. On May 19, 2004, Justin Weddle, Assistant United States Attorney at SDNY, called EY's criminal counsel and informed him that SDNY was formally investigating EY's tax shelter activities.

38. On May 24, 2004, newspapers reported that EY was under grand jury investigation for its tax shelter activities.

39. In May 2007, the grand jury indicted four EY employees for participating in a scheme to defraud the IRS by designing, marketing, implementing, and defending fraudulent tax shelters.

40. On May 8, 2009, the four EY employees were convicted of multiple charges, including tax evasion in connection with the tax shelters.¹ The Second Circuit affirmed two of the convictions and reversed the other two convictions.²

41. On February 28, 2013, EY entered into a non-prosecution agreement with SDNY, pursuant to which EY agreed to pay \$123 million.

¹ *United States v. Coplan*, Dkt. No. 1:07-cr-00453-SHS (S.D.N.Y. May 7, 2009).

² *United States v. Coplan*, 703 F.3d 46 (2d Cir. 2012).

42. On March 1, 2013, SDNY issued a press release relating to the non-prosecution agreement touting EY's cooperation with the government investigation into the tax shelters since approximately 2003, during the time the IRS was helping EY conceal its conflict of interest from Plaintiffs.

C. EY's Breach of Fiduciary Duty.

43. EY was on notice from June 2002 that its conduct in promoting tax shelters had attracted the attention of federal prosecutors.

44. In June 2003, the IRS explicitly informed EY that a criminal investigation of EY's conduct, including the conduct of its employees and partners, was ongoing.

45. Larry D. Thompson, Deputy Attorney General, released a memo titled "Principles of Federal Prosecution of Business Organizations" (the "Thompson Memo") on January 20, 2003. One factor identified in the Thompson Memo to be considered in Department of Justice charging decisions is the organization's "willingness to cooperate." The Thompson memo states that organizational immunity or amnesty may be granted in exchange for cooperation.

46. As a result of the IRS criminal investigation of EY's conduct in promoting tax shelters, EY's interests conflicted with those of Esrey and LeMay.

47. EY did not tell Esrey or LeMay about the criminal investigation or its conflict of interest.

48. EY represented Esrey and LeMay before the IRS during the time it had an undisclosed conflict of interest associated with the criminal and promoter investigations.

49. Esrey and LeMay did not know about the IRS criminal investigation until the May 25, 2004 public disclosure of that investigation.

50. Prior to May 25, 2004, when the Wall Street Journal published an article about the criminal investigation of EY, Esrey and LeMay believed that EY continued to act in their best interests. Esrey and LeMay believed that their interests were aligned with EY's interests, in that Esrey, LeMay, and EY all had the same objectives to prevail against the IRS in the Investor Audits.

51. The IRS knew that EY was aware of the criminal investigation and that EY's interests conflicted with its tax shelter clients that it was representing before the IRS, including Esrey and LeMay.

52. It was IRS policy during 2002 to seek assurances from taxpayer representatives who were tax shelter promoters that their clients were informed of potential conflicts of interest. Internal Revenue Manual part 35.3.12.10 (rev. 5-9-06); NSAR 020331 (Sept. 10, 2002) ("The Manual requires the Service to seek assurances from the POA that the investors have been informed of the potential conflict of interest situation to protect the integrity of the settlement and litigation process.").

53. The IRS permitted EY to continue to represent Esrey and LeMay before the IRS, including before IRS employees working in New York, NY.

54. Plaintiffs filed petitions in the Tax Court in 2008 challenging Final Partnership Administrative Adjustments that were issued by the IRS on January 31, 2008 (the “Tax Court Case”).

55. Throughout the Tax Court Case, the IRS failed to disclose information relevant to the case, contrary to its discovery obligations and court order. Instead, the IRS repeatedly represented that documents were destroyed or did not exist, only to locate portions (but not all) of those documents at a later time when faced with sanctions or when additional information was revealed.

56. Pursuant to discovery in the Tax Court Case, on August 21, 2013, five days before trial, the IRS produced to Plaintiffs documents showing that EY told the IRS it was concerned that the fact it paid a penalty would be “discovered by clients” and that the IRS enabled EY to hide this information in exchange for a “sweetener” of \$1.4 million. This was the first time Plaintiffs learned of the IRS’s active enabling of EY’s breaches of its fiduciary duties to Esrey and LeMay.

57. Plaintiffs initiated an arbitration action against EY on September 15, 2011 (the “Arbitration”). On November 11, 2013, the Arbitration panel issued an interim award in favor of Esrey and LeMay; a final award was made on February 17, 2014. Plaintiffs incurred attorneys and expert fees and expenses relating to the Arbitration

action. The delay in Plaintiffs learning of the extent of EY's breaches of its fiduciary duties increased their Arbitration costs.

INJURY TO PLAINTIFFS

58. On February 26, 2001, Sprint entered into new employment agreements with both Esrey and LeMay. The Sprint Board authorized the contracts with full knowledge that Plaintiffs had entered into the transactions that EY had promoted.

59. LeMay was Esrey's likely successor as CEO of Sprint. The Board informed LeMay of that fact in writing on October 2, 2002.

60. The Sprint Board and the Sprint Audit Committee became concerned that there could be a conflict of interest between Esrey and EY and LeMay and EY because of the IRS audits of Esrey and LeMay. Beginning in 2002, Sprint required Esrey and LeMay to certify every quarter that they had no present intention to sue EY.

61. In December 2002, Esrey and LeMay made a presentation to the Sprint Board recommending that Sprint dismiss EY as its auditor because of the Sprint Board's and Sprint Audit Committee's concern that there could be a conflict of interest between Esrey and LeMay and EY. At the same time, EY met with the Sprint Board and represented that its advice to Esrey and LeMay was sound and its actions proper. This was at a time when EY knew that same advice and those same actions were under criminal investigation.

62. In December 2002, neither Esrey nor LeMay knew of the criminal investigation of EY.

63. The Sprint Board determined that the potential conflict of interest was too great, and concluded that firing its auditor would result in negative publicity and would negatively impact Sprint.

64. The Sprint Board asked both Esrey and LeMay to resign from their positions at Sprint.

65. LeMay and Esrey left Sprint in April and May 2003, respectively.

66. EY remained Sprint's auditor until October 2003.

THE IRS'S DENIAL OF PLAINTIFFS' ADMINISTRATIVE CLAIMS

67. Pursuant to 28 U.S.C. § 2675(a), Esrey presented the IRS with the claim set forth herein on April 29, 2015.

68. On October 22, 2015, the IRS denied the Esrey FTCA Claim.

69. Pursuant to 28 U.S.C. § 2675(a), LeMay presented the IRS with the claim set forth herein on April 29, 2015.

70. On October 22, 2015, the IRS denied LeMay's claim.

**CAUSE OF ACTION
(AIDING AND ABETTING A BREACH OF
FIDUCIARY DUTY)**

71. All preceding allegations are incorporated here as if set forth in full.

72. EY breached its fiduciary duties of loyalty and performance to Plaintiffs.

73. The Defendant knowingly participated in EY's breaches of its fiduciary duties to Plaintiffs in violation of the laws of New York.

74. Plaintiffs exhausted their administrative remedies with regard to their claims against the Defendant.

PRAYER FOR RELIEF

WHEREFORE, Esrey and LeMay demand judgment against Defendant in the sums of \$42,550,000 and \$116,800,000, respectively, fees and costs, and such other relief as the Court deems appropriate.

Dated: April 22, 2016

Respectfully submitted,

s/ _____

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APPENDIX D

28 U.S.C. § 1346 United States as Defendant

(a) The district courts shall have original jurisdiction, concurrent with the United States Claims Court, of:

(1) Any civil action against the United States for the recovery of any internal-revenue tax alleged to have been erroneously or illegally assessed or collected, or any penalty claimed to have been collected without authority or any sum alleged to have been excessive or in any manner wrongfully collected under the internal-revenue laws;

(2) Any other civil action or claim against the United States, not exceeding \$ 10,000 in amount, founded either upon the Constitution, or any Act of Congress, or any regulation of an executive department, or upon any express or implied contract with the United States, or for liquidated or unliquidated damages in cases not sounding in tort, except that the district courts shall not have jurisdiction of any civil action or claim against the United States founded upon any express or implied contract with the United States or for liquidated or unliquidated damages in cases not sounding in tort which are subject to sections 7104(b)(1) and 7107(a)(1) of title 41. For the purpose of this paragraph, an express or implied contract with the

Army and Air Force Exchange Service, Navy Exchanges, Marine Corps Exchanges, Coast Guard Exchanges, or Exchange Councils of the National Aeronautics and Space Administration shall be considered an express or implied contract with the United States.

(b)

(1) Subject to the provisions of chapter 171 of this title, the district courts, together with the United States District Court for the District of the Canal Zone and the District Court of the Virgin Islands, shall have exclusive jurisdiction of civil actions on claims against the United States, for money damages, accruing on and after January 1, 1945, for injury or loss of property, or personal injury or death caused by the negligent or wrongful act or omission of any employee of the Government while acting within the scope of his office or employment, under circumstances where the United States, if a private person, would be liable to the claimant in accordance with the law of the place where the act or omission occurred.

(2) No person convicted of a felony who is incarcerated while awaiting sentencing or while serving a sentence may bring a civil action against the United States or an agency, officer, or employee of the Government, for mental or emotional injury suffered while in custody without a prior showing of physical

injury or the commission of a sexual act (as defined in section 2246 of title 18).

(c) The jurisdiction conferred by this section includes jurisdiction of any set-off, counterclaim, or other claim or demand whatever on the part of the United States against any plaintiff commencing an action under this section.

(d) The district courts shall not have jurisdiction under this section of any civil action or claim for a pension.

(e) The district courts shall have original jurisdiction of any civil action against the United States provided in section 6226, 6228(a), 7426, or 7428 (in the case of the United States district court for the District of Columbia) or section 7429 of the Internal Revenue Code of 1954.

(f) The district courts shall have exclusive original jurisdiction of civil actions under section 2409a to quiet title to an estate or interest in real property in which an interest is claimed by the United States.

(g) Subject to the provisions of chapter 179, the district courts of the United States shall have exclusive jurisdiction over any civil action commenced under section 453(2) of title 3, by a covered employee under chapter 5 of such title.

APPENDIX E

28 U.S.C. § 2680 Exceptions

The provisions of this chapter and section 1346(b) of this title shall not apply to—

(a) Any claim based upon an act or omission of an employee of the Government, exercising due care, in the execution of a statute or regulation, whether or not such statute or regulation be valid, or based upon the exercise or performance or the failure to exercise or perform a discretionary function or duty on the part of a federal agency or an employee of the Government, whether or not the discretion involved be abused.

(b) Any claim arising out of the loss, miscarriage, or negligent transmission of letters or postal matter.

(c) Any claim arising in respect of the assessment or collection of any tax or customs duty, or the detention of any goods, merchandise, or other property by any officer of customs or excise or any other law enforcement officer, except that the provisions of this chapter and section 1346(b) of this title apply to any claim based on injury or loss of goods, merchandise, or other property, while in the possession of any officer of customs or excise or any other law enforcement officer, if—

(1) the property was seized for the purpose of forfeiture under any provision of Federal law providing for the forfeiture of property other than as a sentence imposed upon conviction of a criminal offense;

(2) the interest of the claimant was not forfeited;

(3) the interest of the claimant was not remitted or mitigated (if the property was subject to forfeiture); and

(4) the claimant was not convicted of a crime for which the interest of the claimant in the property was subject to forfeiture under a Federal criminal forfeiture law.. [sic]

(d) Any claim for which a remedy is provided by chapter 309 or 311 of title 46 relating to claims or suits in admiralty against the United States.

(e) Any claim arising out of an act or omission of any employee of the Government in administering the provisions of sections 1–31 of Title 50, Appendix.

(f) Any claim for damages caused by the imposition or establishment of a quarantine by the United States.

[(g) Repealed. Sept. 26, 1950, ch. 1049, § 13 (5), 64 Stat. 1043.]

(h) Any claim arising out of assault, battery, false imprisonment, false arrest, malicious prosecution, abuse of process, libel, slander, misrepresentation, deceit, or interference with contract rights: *Provided*, That, with regard to acts or omissions of investigative or law enforcement officers of the United States Government, the provisions of this chapter and section 1346(b) of this title shall apply to any claim arising, on or after the date of the enactment of this proviso, out of assault, battery, false imprisonment, false arrest, abuse of process, or malicious prosecution. For the purpose of this subsection, “investigative or law enforcement officer” means any officer of the United States who is empowered by law to execute searches, to seize evidence, or to make arrests for violations of Federal law.

(i) Any claim for damages caused by the fiscal operations of the Treasury or by the regulation of the monetary system.

(j) Any claim arising out of the combatant activities of the military or naval forces, or the Coast Guard, during time of war.

(k) Any claim arising in a foreign country.

(l) Any claim arising from the activities of the Tennessee Valley Authority.

(m) Any claim arising from the activities of the Panama Canal Company.

(n) Any claim arising from the activities of a Federal land bank, a Federal intermediate credit bank, or a bank for cooperatives.