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Varsity Blues: Lessons for California Employers

By Dan M. Forman

All employers should be prepared and plan ahead for unexpected illicit behavior of their employees. The criminal detention of employees, whether related to their jobs or not, creates disturbances in the workplace that planning can minimize.

The sophisticated educational institutions at the heart of the Varsity Blues college admissions scandal set up some protocols to guard against improper influence from commercial college preparation companies by precluding contact between such organizations and their admissions' departments. However, the Varsity Blues scheme created a self-described "side door" to get around such restrictions. According to the United States attorney's office, current and former coaches from Georgetown, Stanford, UCLA, the University of San Diego, USC, University of Texas, Wake Forest and Yale were identified as weak links for bribery to gain admission of high-paying clients' children as athletic recruits.

Stanford University's former sailing coach, John Vandemoer, became the first person sentenced in the Varsity Blues' scandal. He was sentenced to one day of prison (which had been served), six months of home confinement, and two years of supervised release, along with a $10,000 fine. The court cited Vandemoer's decision to provide the bribe money to the sailing program, instead of lining his pockets, as one of the reasons for leniency. The U.S. attorney sought a 13-month prison term that was to be followed by one year of supervised release.

Stanford continues to struggle over what to do with over $700,000 of funds illicitly provided to its sailing program. Stanford's president announced the termination of Vandemoer's employment in March and assured the public that "we will ensure that Stanford will not benefit from the monies that were contributed to the Stanford sailing program as part of this fraudulent activity. We are working to determine the most appropriate way to redirect the funds to an entity unaffiliated with Stanford, consistent with the regulations governing such gifts and in cooperation with the government."

The university is undertaking additional caution, no doubt, as the funds were provided to its programs compared to an employee who has lined his or her own pockets. An employee who embezzles, skims, dips or fraudulently takes their employer's money (or opportunities) violates a common law duty of loyalty to their employer. That duty means that employees must turn over any benefit they gain due to their employment to their employer. In California, that common law duty is codified as Labor Code Section 2860: "Everything which an employee acquires by virtue of his employment, except the compensation which is due to him from his employer, belongs to the employer, whether acquired lawfully or unlawfully, or during or after the expiration of the term of his employment."

More examples employers should be aware of include employees making purchases at a discount price and pocketing the difference between a discount price and the retail price charged to their employer, or vendors giving "kickbacks" to decision-makers to select their products or services over those of competitors, typically at greater expense to the employer. Other situations may include trading on insider information, or using information learned from an employer for personal gain at the expense of the company. For example, an employee who learns of her employer's plan to purchase specific real estate or other commodities and who makes the purchase at a low price and forces the employer to pay an inflated price has breached her duty of loyalty. Another example is putting "ghost" employees onto payroll. In these circumstances, the employer may prosecute the employee for breach of the duty of loyalty to attempt to recuperate the misappropriated funds and can then use its judgment to return the funds to clients or to the company's bottom line as appropriate.

Employee arrests can bring additional complications that employers need to plan for as

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arrests may be accompanied by law enforcement's seizure of cellphones, laptops and other employer-owned devices. These devices may contain an employer's trade secret, proprietary and confidential information and the means to access additional important information or documents. The seizure of such items could impede an employer's business, deal flow or the completion of important projects.

In the wake of the Varsity Blues scandal, all employers should take the opportunity to examine their operations and make plans to (1) take preventative measures, including back up of information on portable devices, (2) investigate alleged fraud, kickback schemes and other suspect conduct of employees, (3) work with law enforcement, (4) respond to substantiated allegations of fraudulent conduct by employees, and (5) manage public relations should an arrest or scandal make the headlines.

While not all fraud can be deterred, employers should implement measures that monitor employees who have responsibility for acquisitions, handle funds or who are exposed to confidential and/or trade secret information. Employees should be encouraged to "see something, say something" without retaliation. The sooner an employer is aware of a potential problem, the sooner the employer can investigate and take action to minimize or reverse damages.

An employer that suspects that an employee has engaged in any type of financial impropriety should promptly commence an investigation. While this may not be required by law, alleged financial misconduct by employees should be investigated in a manner similar to legally mandated investigations, such as investigations of sexual harassment or discrimination claims. A thorough investigation is critical to determining how the financial misconduct was carried out, the extent of the misconduct, identifying other participants, and creating protocols to prevent, deter and detect such fraudulent activities in the future. Engaging the appropriate, neutral experts and outside counsel — which brings the protection of attorney- client privilege — is essential to this process. Employers should resist the urge to resort to "self-help" simply by docking wages or withholding paychecks from employees it believes were complicit in these schemes.

Many of the institutions implicated in the Varsity Blues scandal had already detected concerns relating to the accused coaches and recruitment practices, started their own investigations, and taken action before the scandal hit the front pages. Georgetown and Yale have publicly disclosed that they terminated the employment of the accused coaches before being alerted to the FBI's investigation. Other institutions, including UCLA, UT and Wake Forest announced the immediate suspension of their coaches while they conducted internal investigations.

In light of the charges, the publicity involved, and information about the complicity of their employees, these schools took swift action in a very public manner. But they continue to struggle with internal investigations into applicants, current students and graduates, and their image in a very public arena. Thus, the public relations aspect is important. Communications with public relations departments or outside providers about potential fraud should be coordinated with counsel to ensure that privilege is retained.

Several of the universities are facing civil suits filed by graduates claiming a loss in the value of their diplomas. Last month, a class action was filed in federal court on behalf of "all individuals who, between 2012 and 2018, applied to UCLA, USC, USD, Stanford University, U-Texas at Austin, Wake Forest University, Georgetown University, or Yale University, paid an undergraduate admission application fee to one or more of these universities, with respect to an undergraduate admission application that was rejected by the university." *Tamboura et al. v. Singer et al.*, 5:19-cv-03411-SVK (N.D. Cal., filed June 14, 2019). These plaintiffs bring a civil RICO conspiracy action against the perpetrators of the Varsity Blues scheme and are attempting to hold the universities to liability under California's and other states' version of California's Consumer Legal Remedies Act, essentially for false advertising. They also assert a variety of claims of negligence and negligent supervision, alleging that the schools failed to monitor their employees and the admissions process. And they raise respondeat superior claims of liability against the universities for the employees' participation in the bribery scheme. They do not articulate how any damages might be calculated under this theory, other than the refund of application fees, but they essentially are seeking a refund of the application fee on behalf of tens of thousands of college applicants based on allegations that the college admissions process was tainted by the Varsity Blues scheme.

The universities in the Varsity Blues scandal took swift action against fraud to create an overall positive impact against future litigation that might arise from potential employment and other claims down the road as well as to put their best foot forward to minimize any adverse impact on their reputations. Planning ahead for the unexpected requires maintaining a high level of alert to the potential for internal fraud and cheating as well as having a team of professionals identified in advance of the crisis. When the potential fraud or other misbehavior is raised to the attention of employers, prompt consultation with counsel to weigh the delicate balance of privacy laws, internal investigations, law enforcement, potential employment related liability, publicity and other consequences.

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