A Timely Analysis of Legal Developments

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January 2012

DOL Confirms SOX Whistleblower Protections Do Not Apply Extraterritorially

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At a time when the extraterritorial reach of U.S. regulations seems to grow at a rate faster than the economy, U.S. employers breathed a sigh of relief when the U.S. Department of Labor's Administrative Review Board (ARB) confirmed by a 3-2 vote that the whistleblower provision of Title VIII of the Sarbanes-Oxley Act (SOX) has no extraterritorial application.

In *Villanueva v. Core Labs. NV, Saybolt de Colombia Limitada*, ARB Case No. 09-108 (ARB Dec. 22, 2011), the ARB affirmed a decision dismissing a whistleblower complaint, despite the fact that the alleged retaliatory decision occurred in the U.S., because the complaint involved a foreign citizen who alleged violations of foreign law by his foreign employer.

The difficulty in future cases will be determining the extent to which the essential claims at issue trigger extraterritorial application of SOX.

The Complaint

The complainant lived and worked in Colombia for over 20 years as the General Manager (CEO) for Saybolt de Colombia Limitada (Saybolt Colombia), a Colombian company. He was not a U.S. citizen and never worked in the U.S. during his employment. Importantly, Saybolt Colombia did not list securities in the U.S. under Section 12 or file reports under Section 15(d) of the Securities and Exchange Act of 1934.

The complainant believed Saybolt Colombia was violating Colombian tax laws as a result of a transfer pricing scheme between Saybolt Colombia and an affiliate in the Dutch Antilles. He allegedly raised concerns to his superiors in Colombia as well as to the Chief Accounting Officer of the company's indirect affiliate in Houston, Texas. The affiliate, Core Laboratories N.R. ("Core Labs"), is a Netherlands company publicly traded on the New York Stock Exchange. Two independent investigations in response to the claims failed to find any impropriety. Nevertheless, the complainant refused to sign the company's Colombian tax returns when they became due and claimed that after his report to the affiliate in Houston, he was denied a pay raise and eventually terminated. He further alleged that his termination was perpetrated by American executives of Core Labs in the U.S.

The complainant filed a whistleblower complaint under SOX, which was heard by an Administrative Law Judge (ALJ) at the Department of Labor. In dismissing the complaint, the ALJ relied primarily

on *Carnero v. Boston Scientific Corporation*, 433 F.3d 1 (1st Cir. 2006), the only federal appellate court decision to specifically address the extraterritoriality of SOX's whistleblower protections. The ALJ reasoned that the complaint was the "exact" scenario as in *Carnero*.

The ARB Affirmed that SOX's Whistleblower Protections Have No Extraterritorial Application

While rejecting the reasoning of the ALJ, the ARB affirmed the ALJ's ruling, based on the Supreme Court's recent decision in *Morrison v. National Australian Bank, Ltd*. In *Morrison*, 130 S. Ct. 2869 (2010), the U.S. Supreme Court engaged in a two-step process to resolve any extraterritoriality issue. In one step, the adjudicative body determines the extraterritorial reach of the relevant statute. The other step is deciding whether the essential events occurred extraterritorially and, thus, outside of the statute's domestic reach.

Applying *Morrison's* first step, the ARB confirmed that SOX's whistleblower provision, Section 806(a)(1), has no extraterritorial application. Indeed, that provision is silent as to any extraterritorial application and further analysis, including SOX's legislative history, failed to overcome that presumption. The ARB noted that Section 929P of the recently-passed Dodd-Frank Act provides federal district courts jurisdiction over proceedings brought or instituted by the Securities Exchange Commission or the U.S. government. Nevertheless, Section 929A of that Act, which addresses SOX's Section 806(a), failed to include similar language. Accordingly, the ARB reasoned that Congress's silence as to Section 806's extraterritorial application conclusively establishes Congress's intent to withhold its application outside the borders of the U.S.

As for *Morrison's* second step, the ARB considered whether the essential parts of the alleged fraud occurred domestically or whether they triggered extraterritorial application. Here, the ARB focused on the *locus of the fraudulent activity* being reported and stressed that the "onus of the alleged fraud involved actions affecting foreign companies doing business in a foreign country, and a failure to comply with foreign tax law."

The ARB further noted that even if the complainant's allegation that a publicly-traded American company controlled all aspects of Saybolt Colombia were true, it would "not change the fact that the disclosures involved violation of extraterritorial laws and not U.S. laws or financial documents filed with the SEC." Thus, despite the allegation that the retaliatory decision was made in the U.S., the ARB held that, pursuant to *Morrison*, "some domestic contact will not convert an extraterritorial application to a domestic one."

Impact on Employers

The ARB's confirmation that SOX's whistleblower provisions, at least in this case, have no extraterritorial application is a relief for multinational employers. Covered employers can find some assurance in the limited circumstance that non-U.S. citizens of indirect foreign subsidiaries have no claim under SOX for retaliation based on their complaints about violations of foreign laws in foreign countries. Indeed, where "the driving force of the case – the fraudulent activity being reported – [is] solely extraterritorial," there is no cause of action under Section 806.

Despite the ARB's conclusion in this case, the question of whether the alleged fraudulent activity is "solely extraterritorial" is an analysis that remains in an immense ocean of gray. Such an evaluation will, of necessity, require a case-by-case analysis, resulting in continued confusion about the exact scope of the whistleblower protections under SOX. Indeed, the dissent strenuously argued that there was no issue of extraterritoriality in this case because the complainant took his complaint to the chief accountant in Texas and the foreign subsidiaries' conduct was directed from Houston. While the ARB rejected the dissent's argument and found that the "driving force" of the case – the fraudulent activity – was an extraterritorial one, it conceded that courts should consider the "location of the protected activity, the location of the job and the company the complainant is fired from, the location of the retaliatory act, and the nationality of the laws allegedly violated that the complainant has been fired for reporting . . . ." The ARB further noted that, "where the complainant, for example, is working for a covered company in the United States, but may have worked in a foreign office of the company for part of the time, [these facts] may require a different outcome." In other words, to the extent a complainant can show that the alleged fraud affects a U.S. security or a financial disclosure law, the complainant may have a claim.

This decision did not address the extraterritorial application of the Dodd-Frank Act. As a result, it remains unclear how Dodd-Frank will be applied in these types of cases.

In sum, the ARB decision lends some clarity to the boundaries of the extraterritorial application of SOX's whistleblower provision. Nevertheless, there remain uncertainties. Companies covered by SOX must exercise caution and restraint when faced with a whistleblower complaint, regardless of whether that complaint comes from a domestic or international source.

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