Bloomberg BNA

Daily Labor Report®

WHISTLEBLOWERS

The Labor Department's Administrative Review Board recently has been handing down decisions under the Sarbanes-Oxley Act's whistleblower provisions that are more pro-claimant than those in previous years, management attorney Edward T. Ellis of Littler Mendelson writes in this BNA Insights article.

In a detailed analysis of some recent ARB cases, Ellis looks at the board's reasoning and applicable precedent and offers suggestions for organizations entering ARB proceedings.

Reconstituted ARB Expanding Sarbanes-Oxley Whistleblower Protections

By Edward T. Ellis

"Since the [Sarbanes-Oxley Act] was passed in 2002, the government has ruled in favor of corporate whistleblowers in 21 out of 1,455 complaints. Another 996 cases have been dismissed. The rest of the cases were withdrawn, settled or are pending." **Source: *Wall Street Journal*, Dec. 1, 2009.**

The conventional wisdom is that the Department of Labor is a hospitable venue for corporate respondents in Sarbanes-Oxley Act (SOX) cases, one in which the defense success rate may exceed 95 percent.

The figures cited in the *Wall Street Journal*, which University of Nebraska law professor Richard Mobley generated through a study of Occupational Safety and Health Administration/Administrative Law Judge (ALJ) proceedings, are also the basis for the assumption that complaining employees will, in the future, use the Dodd-Frank Wall Street Reform and Consumer Protection Act to bypass the DOL and file their suits in the federal court system.

Those assumptions may be old news. The newly constituted Administrative Review Board of the DOL (ARB) is making the OSHA/ALJ process more hospitable to complainants. It is also deciding cases that encourage the federal courts to treat SOX whistleblowers more favorably than they have in the decade since SOX became law.

The ARB, with a full complement of Democratic appointees as of early 2011, is committed to expanding SOX coverage, broadening the concept of protected activity, restricting employer defenses, and generally making the DOL a friendlier place for whistleblowers. A review of the ARB's decisions over the past year demonstrates the dramatic change being wrought in the conventional wisdom.

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Key Elements of a Sarbanes-Oxley Claim in Early 2011

A year ago, an attorney seeking to bring—or defend—an action under the whistleblower protection provisions of the Sarbanes-Oxley Act, 18 U.S.C. § 1514A, could look to the decisions of the federal courts of appeal and the ARB and predict with some certainty whether a particular complainant satisfied the key elements of a SOX whistleblower claim. The jumping off point, the Department of Labor regulations on SOX, articulates the "prima facie case" as follows:

> "(i) the employee engaged in a protected activity or conduct; (ii) the [employer] knew or suspected, actually or constructively, that the employee engaged in the protected activity; (iii) the employee suffered an unfavorable personnel action; and (iv) the circumstances were sufficient to raise the inference that the protected activity was a contributing factor in the unfavorable action." 29 C.F.R. § 1980.104(b)(2).

 ISSN 0418-2693

The regulations then provide that, if the complainant could establish all the elements of the prima facie case by a preponderance of the evidence, the burden shifts to the employer to prove by ''clear and convincing evidence'' that it would have taken the adverse action against the complainant even absent the protected activity. Despite the fact that Congress and the DOL regulation-drafters clearly designed this scheme to tilt in favor of the whistleblower, very few SOX whistleblower claims succeeded at the agency level.

The key element in the prima facie case is ''protected activity,'' which the courts and the ARB defined as a specific and material allegation of securities fraud or a violation of a Securities and Exchange Commission (SEC) regulation that has occurred or is about to occur. Decisions from the federal courts of appeal have often cited legislative history to the effect that Section 806 of SOX, 18 U.S.C. § 1514A, was passed to ''encourage and protect [employees] who report fraudulent activity that can damage innocent investors in publicly traded companies.'' *Day v. Staples Inc.*, 555 F.3d 42, 52 (1st Cir. 2009); see also *Van Asdale v. International Game Technology*, 577 F.3d 989, 1002 (9th Cir. 2009). These cases and others hold that, for an employee communication involving fraud to be protected, it must be an allegation of securities fraud and the fraud must be ''material'' as that term has been applied in the federal securities laws. *Day*, 555 F.3d at 55; *Livingston v. Wyeth Inc.*, 520 F.3d 344, 351, n.1 (4th Cir. 2008).

Furthermore, the case law required that the whistleblower's statement concern a present violation of the securities laws—as opposed to a violation that might occur in the future depending on contingencies that may or may not occur. *Livingston*, 520 F.3d at 352-56. Finally, the statement must ''definitively and specifically'' relate to one or more of the six federal enactments enumerated in Section 1514A(a)(1): mail fraud, wire fraud, bank fraud, securities fraud, any rule or regulation of the SEC, or any other federal law relating to fraud against shareholders. *Van Asdale*, 577 F.3d at 997; *Welch v. Chao*, 536 F.3d 269, 275, 28 IER Cases 1792 (4th Cir. 2008); *Allen v. Administrative Review Board*, 514 F.3d 468, 476, 27 IER Cases 140 (5th Cir. 2008).

As of the beginning of 2011, the leading case from the ARB was the 2006 case, *Platone v. FLYi Inc.*, ARB Case No. 04-154, 25 IER Cases 278 (ARB Sept. 29, 2006), *aff'd*, 548 F.3d 322 (4th Cir. 2008), which involved an employee's communications to her management about ''billing discrepancies.'' In *Platone*, the ARB first articulated the ''definitively and specifically'' standard and held also that a SOX complainant alleging mail or wire fraud must allege unlawful conduct that is at least ''adverse to investors' interests,'' i.e., not all mail or wire fraud allegations are protected by SOX. Over the next few years, the courts of appeals generally accepted the ARB's statutory construction on these points. *Van Asdale*, 577 F.3d at 997; *Day*, 555 F.3d at 55; *Welch*, 536 F.3d at 275; *Allen*, 514 F.3d at 476.

A further requirement for the protected communication was that the complainant must have a subjective belief that the conduct being reported violated one of the six sources of law in Section 1514A, and the complainant's belief must be objectively reasonable. *Van Asdale*, 577 F.3d at 1000; *Harp v. Charter Communications, Inc.*, 558 F.3d 722, 723,28 IER Cases 1448 (7th Cir. 2009); *Allen* 514 F.3d at 477.

The second and third elements of the prima facie case are standard fare for employment lawyers and—prior to 2011—had received little commentary from the ARB or the courts. The employer must be aware of the protected communication, and the complainant must have suffered an unfavorable personnel action. As of one year ago, no decision had applied *Burlington Northern & Santa Fe Railway Co. v. White*, 548 U.S. 83, 98 FEP Cases 385 (2006), to expand the class of retaliatory acts beyond the ''terms and conditions of employment,'' the phrase that appears in 18 U.S.C. § 1514A.

The fourth element, circumstances that give rise to the inference that the protected activity was a contributing factor in the employer's decision to make the unfavorable personnel action, is the ''causal link,'' or nexus requirement, borrowed from statutory retaliation law. See, e.g., *Jalil v. Avdel Corp.*, 873 F.2d 701, 49 FEP Cases 1210 (3d Cir. 1989).

Analysis of causation usually begins with the temporal relationship between the protected communication and the unfavorable personnel action and proceeds to the analysis of legitimate nondiscriminatory reasons for the decision, comments showing the state of mind of the decisionmaker, comparative discipline and other evidence pointing to pretext. These being familiar concepts, neither the ARB nor the federal courts have broken new ground in this area.

2011: A Year of Change for the OSHA/ALJ System

A lawyer looking to ascertain the elements of a SOX whistleblower case in 2012 has a more difficult task, due primarily to an ARB that used a series of 2011 cases to expand the reach of SOX and the protections afforded to employees.

The ARB issued three decisions during 2011 that resulted in changes in application of SOX law. A fourth decision at the end of the year showed how dramatically the ARB's view of SOX had changed in just one year and how it had morphed into a view that likely diverges from that of the federal courts of appeals.

***Sylvester v. Parexel International LLC*, No. 07-123, 32 IER Cases 497 (ARB May 25, 2011).** In *Sylvester*, the most dramatic of the four cases and the only en banc decision, the ARB decided that the whistleblowing communication need not be related to shareholder fraud. In *Sylvester*, the allegations related to the employer's drug testing research facilities and the alleged failure of management to adhere to the Good Clinical Practices (GCP) standards established by the federal Food and Drug Administration (FDA).

The complainants advanced the theory that management ignored their complaints of GCP violations because the results of an investigation would have affected the profit flowing from the studies, which would have affected the stock price, which would have caused corporate credit problems and contradicted the company's statements to its shareholders that it adhered to the GCP. Whether this was a claim of shareholder fraud is a good question, but the ARB avoided the question by holding that a complainant need not allege shareholder fraud to obtain SOX whistleblower protection. 32 IER Cases at 510 -11. In so holding, the ARB explicitly recognized that it was contradicting its own holding in *Platone*, and the holdings of the Fourth Circuit in *Welch*,

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the Fifth Circuit in *Allen*, the First Circuit in *Day* and the Ninth Circuit in *Van Asdale*. *Id*. at 511.

The ARB then held that regardless of the statutory or legal basis for the complaint, a complainant would no longer be held to the ''definitively and specifically'' evidentiary standard first announced in *Platone* in 2006, reiterated by the ARB 12 times since and approved by four courts of appeals. A whistleblower's allegations, even if vague and nonspecific , may now be sufficient to establish a claim—at least as a matter of administrative pleading.

Sylvester also dispensed with the ''materiality'' element that had been adopted by the courts of appeals, and held that the whistleblower need not even allege fraud. The ARB stated:

> ''We feel the purposes of the whistleblower protection provision will be thwarted if a complainant must, to engage in protected activity, allege, prove, or approximate that the reported irregularity or misstatement satisfies securities law ''materiality'' standards, was done intentionally, was relied upon by shareholders, and that shareholders suffered a loss because of the irregularity.''

Sylvester, 32 IER Cases at 512.

In the procedural section of the decision, the ARB noted that the ''complaint'' before the ALJ is usually a letter written to OSHA, often without the benefit of counsel. The ARB expressly rejected, as inappropriate in the administration setting, the Federal Rule of Civil Procedure, Rule 12(b)(6) pleadings standard established by the Supreme Court in *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 75 USLW 4337 (2007), and *Ashcroft v. Iqbal*, 556 U.S. 662 (2009).

The ARB sought to discourage the ALJs under its jurisdiction from entertaining motions challenging the sufficiency of SOX pleadings. One of the judges dissented on the ground that motions akin to Rule 12 (b)(6) motions should be banned altogether. The ARB majority merely discouraged the practice. 32 IER Cases at 505-06.

***Menendez v. Halliburton Inc.,* Nos. 09-002, 09-003, 32 IER Cases 1435 (ARB Sept. 13, 2011).** In *Menendez*, the ARB waded into the murky area of what employer actions are sufficiently adverse to trigger the protection of SOX, and drew the Supreme Court's decision in *Burlington Northern & Santa Fe Railway Co. v. White*, 548 U.S. 53, 98 FEP Cases 385 (2006), into the discussion.

In *Burlington Northern*, a unanimous Supreme Court had interpreted the anti-retaliation provisions of Title VII to prohibit retaliatory acts of an employer that have no impact on terms and conditions of employment. The court held that an employee need only show that the employer's actions were ''harmful to the point that they could well dissuade a reasonable worker from making or supporting a charge of discrimination.'' 548 U.S. at 68. *Burlington Northern* created both a low threshold and a broad scope of activity protected under the retaliation provision in Title VII, thus making it easier for complainants to establish a claim.

The ARB in *Menendez* went beyond *Burlington Northern* to hold that any ''non-trivial'' employer act can be retaliation under SOX, regardless of whether it was employment related. The act need not even be sufficient to dissuade the employee from complaining – it just cannot be trivial.

In justifying this decision, the ARB had to reconcile one significant difference between the text of Title VII's retaliation provision and the text in Section 1514A. The Title VII retaliation statute makes it unlawful for an employer ''to discriminate against any of its employees or applicants for employment'' because of a retaliatory motive. 42 U.S.C. § 2000e-3.

As the Supreme Court held, the protection in the statute is not limited to events affecting the employment relationship. SOX, on the other hand, expressly limits prohibited actionable adverse action to ''terms and conditions of employment.'' 18 U.S.C. § 1415A(a)(1). The ARB recognized that difference, but disposed of it with the following sentence:

> ''Rather than a limitation on what is to be considered adverse action under Section 806, we are of the opinion that 'terms and conditions of employment' are not significant limiting words and should be construed broadly within the remedial context of Section 806.

Menendez v Halliburton, Inc., ARB Case Nos. 09-002, 09-003, 32 IER Cases 1435, 1445 (ARB Sept. 13, 2011). According to the ARB, Congress might as well have left the key words out of the statute.

Menendez arose out of a dispute between a high-level accountant and the finance organization of an oil field services company—including its external auditors—over revenue recognition issues. The complainant seems to have been determined to make controversy at the company. The ARB decision notes that within three months of his hire, Menendez was arguing accounting policy with his manager and surreptitiously taping one of their conversations.

Menendez disagreed so vehemently with the other accountants at the company that he lodged a complaint with the SEC less than a year after he started work, and he followed up shortly with a complaint to the audit committee of the board of directors. He made both complaints anonymously, although the latter was at the express suggestion of the vice president of financial controls. The substance of both complaints was, of course, the same revenue recognition problem. When the SEC came to investigate, the company was not surprised. It was during the company's document retention efforts connected to the SEC investigation that one of Menendez's superiors identified him as the source of the complaint, which all the relevant accounting personnel apparently already knew—or at least strongly suspected.

The ARB held that the disclosure of the name of the complainant to the staff was a per se SOX violation. The ARB reasoned that because SOX Section 301 assures confidentiality for employees who go to the audit committee, confidentiality was a term and condition of employment by operation of the statute, and breach of that confidentiality was a violation of SOX. *Menendez*, 32 IER Cases at 1449-50. Since SOX retaliation could be any ''non-trivial'' action, disclosure of the complainant's identity qualified as a violation. In a footnote, the ARB also offered the dictum that a paid administrative leave pending an SEC investigation was likely a retaliatory act, even if it comes at the request of the complainant's attorney. *Id*. at 1451, n.155.

It is worth mentioning that the 2006 SEC investigation into revenue recognition issue completely exonerated the company, and when the complainant learned of the SEC's decision in late 2006, he obtained another job. The SOX case lives on.

***Vannoy v. Celanese Corp.*, No. 09-1118, 32 IER Cases 1454 (ARB Sept. 28, 2011).** In *Vannoy*, the complainant's job was to reconcile employee expense reimbursement submissions. He used his company laptop to download company proprietary and confidential information and he provided it through his attorney to the Internal Revenue Service as part of its Whistleblower Rewards Program. He also provided the IRS with the Social Security numbers of 1,600 company employees who had submitted expense reimbursement requests. Before extracting this data and providing it to the IRS, Vannoy signed a confidentiality agreement. He also worked subject to company policies on trade secrets, proprietary and confidential information, and personal data. In his deposition in the administrative action, he admitted taking confidential and proprietary information, including personal identifying information of his co-workers, without permission and without notice. Not surprisingly, the DOL ALJ dismissed his claim that the company terminated him in violation of SOX.

The ARB reversed, making the following principal holdings:

- The misconduct reported by the whistleblower need not be shareholder fraud;
- SOX protects disclosures by the employee to the IRS; and
- Theft of confidential and proprietary data from a company might be protected activity.

On the last—and most significant—point, the ARB recognized a ''clear tension between a company's legitimate business policies protecting confidential information and the whistleblower bounty programs created by Congress to encourage whistleblowers . . . .'' *Vannoy v. Celanese Corp*., No. 09-1118, 32 IER Cases 1454, 1464 (ARB Sept. 28, 2011). The ARB cited the Dodd-Frank Act policy of rewarding employees who ''independently garnered, insider information that would be valuable to the SEC in its investigation'' as a justification for removing company documents in violation of an employment agreement and company policies. The only restriction the ARB seemed to acknowledge was that the employee's evidence gathering must not be ''unlawful.'' On this point, the judges seemed impressed that the local police department had investigated Vannoy's conduct but elected not to prosecute him. The ARB seemingly ignored the possibility that Vannoy violated the Computer Fraud and Abuse Act when he accessed the company system, thereby violating his confidentiality agreement and the terms of his company authorization.

***Prioleau v. Sikorsky Aircraft Corp.*, No. 10-060, 33 IER Cases 263 (ARB Nov. 9, 2011).** Perhaps nowhere is the current ARB majority's view of SOX whistleblower law better displayed than in *Prioleau*, in which the ARB again reversed an ALJ's grant of summary judgment. In that case, Prioleau was a systems engineer in the company's military helicopter program. One of his areas of responsibility was computer system security, and he had previously worked for the consultant that designed the computer infrastructure for the company's parent. Prioleau received two emails, four days apart, in June 2009.

The first, from the company's legal department, was an announcement that if, at some point in the future, the legal department issued a legal hold notice, then certain categories of electronically stored information (ESI) must be retained. This announcement was neither surprising nor controversial. The second email was from his former employer, the IT consultant, stating that the computer system of the company's parent had an application that, if not disabled, would automatically delete emails of a certain age.

Prioleau's protected activity, according to the ARB, was to write a memorandum to his superiors that explained that the requirements of the legal hold notice might be compromised by the automatic destruction policy. The company terminated Prioleau shortly after he sent the memorandum.

At the time of termination, no legal hold notices had been issued, no duty to preserve evidence had attached, and no one at the company had placed it in peril by destroying documents. Nevertheless, Prioleau filed a complaint alleging that he had been fired for ''reporting shareholder fraud and § 404 [SOX] assessment of internal controls of the Act.'' OSHA found against Prioleau and he appealed to the Office of Administrative Law Judges. The ALJ granted the company's motion for summary judgment, finding that Prioleau had not engaged in protected activity. The ARB reversed.

Prioleau's contention was that he had exposed a weakness in internal controls and that the combination of the legal hold and the deletion application ''made it clear that the company and its employees *may commit fraud*.'' *Prioleau v. Sikorsky Aircraft Corp*., ARB Case No. 10-060, 33 IER Cases 263, 266 (ARB Nov. 9, 2011) (emphasis added).

It should be evident that, giving Prioleau every benefit of the doubt, a theoretical concern that an email deletion application in a corporate computer system might delete emails that might be of legal interest at some point in the future is not an allegation of fraud, a violation of SEC rules and regulations, or even a weakness in internal financial controls. It was, however, sufficient for the ARB to remand the case for an evidentiary hearing.

This result was the first to provoke a dissent from one of the ARB members. The dissent asserted that Prioleau's case was critically defective because it required ''too many assumptions and giant leaps in logic.'' 33 IER Cases at 272.

It appears, then, that the 2012 ARB will include within the scope of ''protected activity'' speculation that other employees might commit fraud when placed in circumstances not yet presented.

Federal Court Decisions in 2011

The ARB is not the final word on 18 U.S.C. § 1514A. Nothing the ARB did in 2011 overturned the appellate decisions in *Platone*, *Welch*, *Day*, *Van Asdale*, *Allen*, or *Livingston*, which are controlling law in their respective circuits.

In one of the few federal court SOX cases decided in 2011, *Wiest v. Lynch*, No. 10-3288, 33 IER Cases 9 (E.D. Pa. July 21, 2011), a judge in the Eastern District of Pennsylvania ignored *Sylvester v. Parexel* and found the complaint defective because it did not satisfy the pleading standards set forth in the federal rules of civil procedure. The court held that ''the employee's communication must convey that his concern with any alleged misconduct is linked to an objectively reasonable belief that the company intentionally misrepresented or omit-

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ted certain facts to investors, which were material and which risked loss.'' 33 IER Cases at 10.

Wiest's internal complaints that certain corporate expenses ran afoul of corporate policies as well as SEC and IRS rules and regulations did not, in the district court's view, relate—definitively and specifically or otherwise—to shareholder fraud or one of the sources of law set forth in Section 1514A(a)(1).

On motion for reconsideration, the plaintiff raised *Sylvester v. Parexel* expressly, only to see it dismissed in a sentence. The court noted that *Sylvester v. Parexel* is not precedential in the Third Circuit and pointed out that, as a matter of pleading, a case filed directly in federal court is subject to the federal rules—and the interpretation put on the pleading rules by *Iqbal* and *Twombly*—and that the district court need not evaluate the complaint as if it were a letter submitted to OSHA. *Id.* at 13. *Wiest* is presently on appeal to the Third Circuit.

Will the Federal Courts Defer to the ARB's Reinterpretation of 18 U.S.C § 1514A?

Two of the Fourth Circuit's early and influential SOX opinions—*Welch* and *Platone*—came to the court from the ARB. In both cases, the Fourth Circuit deferred to the ARB's interpretation of § 1514A on the theory that the interpretation fell within the category of agency decisions covered by *Chevron v. Natural Resources Defense Council Inc.*, 476 U.S. 837 (1984), as interpreted in *United States v. Mead Corp.*, 533 U.S. 218, 229 (2001).

In *Welch*, the court deferred to the agency's now-disavowed ''definitively and specifically'' standard, referring to the burden on the whistleblower in making the initial complaint to management. While agreeing to *Chevron* deference, the Fourth Circuit made no determination that the statute had either (a) expressly delegated to the Department of Labor the responsibility for interpreting the statute, or (b) implicitly delegated such authority by leaving parts of Section 1514A ambiguous. These have typically been the grounds for according *Chevron* deference.

The other courts of appeal have decided cases that came through the federal court system after the plaintiffs withdrew them from the OSHA/ALJ process and filed in court at the expiration of the 180-day waiting period. *Chevron* deference has not been mentioned in those cases. None of the courts of appeal has faced the question of whether to allow the ARB to flip-flop its statutory interpretation (seemingly due to its change in composition from Republican to Democratic).

Wiest will pose exactly that question to the Third Circuit. In rejecting the employee's motion for reconsideration, the district court sidestepped the question of *Chevron* deference by finding that it ''need not examine whether *Chevron* deference is appropriate here because the Plaintiff's complaint is insufficient without regard to the ARB's interpretation of SOX 806 in *Sylvester*.'' 33 IER Cases at 12, n.7. Much will depend on how the Third Circuit construes the *Wiest* complaint.

Given the ARB decisions from 2011, it is difficult to imagine the current ARB deciding that a plaintiff who pleaded an internal complaint alleging violations of SEC and IRS rules in expense accounting should be thrown out of court as a matter of law.

Where Do Litigants Go in 2012 for the Answer?

Interpretations of critical aspects of SOX will likely be in flux for a time, especially if the solidly Democratic ARB continues to make decisions that broaden both the scope of SOX and the remedies available to a complainant.

The ARB may meet some resistance from the largely Republican federal judiciary that may view SOX primarily as a remedy for shareholder fraud. Resolution of the differences in approach may depend on whether the courts defer to the ARB's expertise, as appellants have suggested in *Wiest*.

If courts defer to the ARB's re-interpretation of the law, the key coverage and remedy provisions of an obstruction of justice statute (SOX § 806 is codified in U.S.C. Title 18, Chapter 73 ''Obstruction of Justice'') may become like *Weingarten* rights and apply to different groups of employees depending on which political party is appointing members of the National Labor Relations Board.

In the meantime, the OSHA/ALJ route to justice may be more hospitable to aggrieved whistleblowers than the federal courts, and plaintiffs' lawyers may think twice before exercising their option to proceed directly into federal court under the Dodd-Frank Act instead of allowing the administrative process to run its course.