

SOX Complaints: From OSHA to the ARB

Joseph W. Galera
King & Greisen, LLP
1670 York St.
Denver, CO 80206
(303) 298-9878
April 15, 2010

A. Sarbanes-Oxley (“SOX”)

Section 806 of the Corporate and Criminal Fraud Accountability Act of 2002, Title VIII of the Sarbanes-Oxley Act of 2002, protects employees of publicly traded companies who report fraud. Specifically, the Act protects employees from discrimination by companies, and representatives of companies, because the employee has engaged in protected activity pertaining to a violation of 18 U.S.C. §§ 1341, 1343, 1344, or 1348, or any rule or regulation of the Securities and Exchange Commission, or any provision of Federal law relating to fraud against shareholders. 29 C.F.R. §1980.100.

B. Administrative Process

A written complaint must be filed with the OSHA Area Director within ninety (90) days of the time the employee learns that he or she has been discriminated against. The act provides for the following relief: reinstatement or front pay in lieu of reinstatement, back pay with interest, restoration of seniority/sick leave/etc., emotional distress, attorney’s fees and costs, and any affirmative relief.

1. Investigation

Upon receipt of the complaint, the Assistant Secretary will notify the named person of the filing of the complaint, of the allegations, and of the substance of the evidence supporting the complaint.

The Complainant must make a *prima facie* showing “that protected behavior or conduct was a contributing factor in the unfavorable personnel action alleged in the complaint.” 29 C.F.R. §1980.104(b). The decision whether to continue to investigate can also be supplemented by an interview of the Complainant.

The named person has twenty (20) days from receipt of the notice of the filing of the complaint to submit a written statement, including supporting documentation substantiating its position, and may also request a meeting with the Assistant Secretary. If the named person fails to demonstrate by clear and convincing evidence that it would have taken the same unfavorable personnel action in the absence of the behavior protected by the Act, the Assistant Secretary will conduct an investigation.

2. Issuance Of Findings

The Assistant Secretary will issue written findings as to whether there is reasonable cause to believe that the named person has discriminated against the Complainant within sixty (60) days of the filing of the complaint.

C. Litigation And Appeal Of The Assistant Secretary's Findings

Any party can object and request judicial review of the Assistant Secretary's findings and preliminary order if such objection is filed within thirty (30) days of receipt of the findings. Objections can include allegations that the complaint was frivolous or brought in bad faith.

1. Hearings

Proceedings are generally conducted in accordance with the rules of practice and procedure for administrative hearings before the Office of the Administrative Law Judges ("ALJ"). The Rules of Evidence are generally relaxed during these proceedings.

2. Discovery Is Permitted

Discovery is permitted in SOX hearings before an ALJ. An opportunity to conduct discovery is important in order to uncover questionable employment practices. See *Laxmi v. Southern Cal. Edison*, 1998 WL 168938, *3 (1998); *Timmons v. Mattingly Testing Servs.*, Case No. 05-ERA-40, ARB Dec., June 21, 1996 (holding that an opportunity for extensive discovery is crucial . . . to protecting employees and the public interest). Discovery should not be denied when it is not "excessively dilatory or otherwise contumacious." *Secretary of Labor v. Genesee Brewing Comp.*, 1983 WL 23874, *1 (O.S.H.R.C. 1983 April 27). Furthermore, trial subpoenas can be obtained through a motion to the ALJ.

3. Burden of Proof

To prevail on a SOX Complaint, the Claimant must prove by a preponderance of the evidence that: (1) the Complainant engaged in protected activity or conduct; (2) the Respondent knew that the Complainant engaged in "protected activity"; (3) the Complainant suffered an unfavorable personnel action; and (4) the protected activity was a contributing factor in the unfavorable action. *Collins v. Beazer Homes USA, Inc.*, 334 F. Supp.2d 1365 (N.D. Ga. 2004); *Richards v. Lexmark International, Inc.*, 2004-SOX-00049 (ALJ June 20, 2006).

4. "Protected Activity" Defined

"Protected activity" as defined under the Act includes providing to an employer information regarding conduct which the employee reasonable believes constitutes a

violation of various criminal fraud provisions, any rule or regulation of the SEC, or any provisions of Federal law relating to fraud against shareholders. 18 U.S.C. § 1514A (a)(1).

Protected Activity under SOX has three components: 1) The report or action must be related to a purported violation of a federal law or SEC rule or regulation relating to fraud against shareholders; 2) The Complainant's belief about the purported violation must be subjectively and objectively reasonable; 3) The Complainant must communicate the concern to either his/her employer, the federal government, or a member of Congress; and 4) The report or complaint must involve actions outside the Complainant's assigned duties. *Robinson v. Morgan Stanley*, 2005-SOX-44 (ALJ Mar. 26, 2007); *Hughart v. Raymond James & Associates, Inc.*, 2004-SOX-9 (ALJ Dec. 17, 2004).

a. The "Reasonable Belief" Standard

To come within the protection of the Act, the Complainant must have reasonably believed that the Respondent violated one of the enumerated statutes or regulations of SOX. *Platone v. Atlantic Coast Airlines*, 2003-SOX-27 (ALJ Apr. 30, 2004). A belief that an activity was illegal may be reasonable even when subsequent investigation proves a complaint was unfounded. *Halloum v. Intel Corporation*, 2003-SOX-0007 (ALJ March 4, 2004). "The statutory language makes it clear that the Complainant is not required to show that the reported conduct actually constituted a violation of the law, but only that she reasonable believed that the Respondent violated one of the enumerated statutes or regulations." *Id.* at 21.

A Complainant's belief must be both "a subjective belief and an objectively reasonable belief that the conduct complained of constituted a violation of relevant law." *Welch v. Chao*, 536 F.3d 269 n. 4 (4th Cir. 2008).

In *Mann v. United Space Alliance, LLC, et. al.*, 2004-SOX-15 (ALJ February 18, 2005), the Office of Administrative Law Judges denied a motion for summary judgment when it found that a perpetration of a fraud on the National Aeronautics and Space Administration ("NASA") could also perpetrate a fraud on shareholders. The Complainant alleged that he was subjected to adverse actions by his employer when he notified his supervisors of possible violations of the Federal Acquisitions Regulations, which could constitute fraud on NASA. The ALJ agreed that improperly favoring certain vendors in violation of federal acquisition regulations could also perpetrate a fraud on shareholders. The ALJ relied heavily on *Collins v. Beazer Homes USA, Inc.*, 334 F. Supp. 2d 1365 (N.D. Ga. 2004) which, in denying defendant's motion for summary judgment, stated:

If Congress had intended to limit the protection of Sarbanes-Oxley to accountants, or to have required Complainants to specifically identify the code section that they believe was being violated, it could have done so. It did not. Congress instead protected "employees" and adopted the "reasonable belief" standard for those who "blow the whistle" on fraud

and protect investors. ...Additionally, though Defendants contend that Plaintiff's complaints were too vague to constitute protected activity, the individuals to whom they were addressed understood the serious nature of Plaintiff's allegations. ...The Court agrees with Defendants that the connection of Plaintiff's complaints to the substantive law protected in Sarbanes-Oxley is less than direct. However, Plaintiff's allegations detailed violations of the company's internal accounting controls in favor of preferential treatment based on personal relationships. *Collins*, 334 F. Supp. at 1377-1378.

In *Hendrix*, the court held that although the Complainant never identified a particular code section he believed had been violated, such specificity is not required under SOX. "The Act merely requires that the Complainant have a reasonable belief he is blowing the whistle on fraud and protecting investors." *Hendrix*, citing *Collins v. Beazer Homes USA, Inc.*, 334 F. Supp.2d 1365, 1377 (N.D.Ga. 2004).

b. Complainant's SOX Complaint Must Include Conduct Relating To Fraud

A whistleblower need not cite the specific law or regulation that he believes is being violated in his report or other alleged protected activity. *Fraser v. Fiduciary Trust Co. Int'l*, 417 F. Supp.2d 310, 322 (S.D.N.Y. 2006). The "context" of the disclosure and "the circumstances giving rise to the communication," if closely related to potential fraud against shareholders, may be sufficient to satisfy the pleading requirements of a SOX whistleblower claim. *Id.* Where the communication is "barren of any allegations of conduct that would alert [a Respondent] that [the Complainant] believed the company was violating any federal rule or law related to fraud against shareholders," the reporting is not protected by SOX. *Id.* See also *Platone*, 2003-SOX-27 (ALJ Apr. 30, 2004), ("The relevant inquiry is not what [is alleged in the complaint filed with OSHA], but [what was] actually communicated to [the] employer prior to ... termination.").

"Fraud" is an integral element of a cause of action under § 806 and incorporates requisite accusation of intentional deceit that under SOX would pertain to a matter that is material to or that would impact shareholders or investors. *Grant v. Dominion East Ohio Gas*, 2004 SOX 63 at 40 n. 40 (Sec'y Mar. 10, 2005) (citing *Hopkins v. ATK Tactical Systems*, 2004 SOX 19 (Sec'y May 27, 2004) (discontented employee's request for explanations about projects, accounting, and software without reference to fraud or intentional deception of stockholders is not protected activity). The alleged fraudulent conduct must "at least be of a type that would be adverse to investors' interests" and meet the standards for materiality under the securities laws such that a reasonable shareholder would consider it important in deciding how to vote. *Platone*, 2003-SOX-27 (ALJ Apr. 30, 2004).

A Complainant must at least implicate fraud in order to be protected activity. In *Skidmore v. ACI Worldwide, Inc.*, No. 08:08CV1 (D. Neb. June 18, 2008) (case below ALJ No. 2007-SOX-77), the court held that "[i]n order for a SOX claim to survive a Rule

12(b)(6) motion to dismiss, a complaint must state a cause of action where an employee reasonably believed that the reported conduct was violating the provisions of § 1514A relating to shareholder fraud.”

However, in *Hendrix v. American Airlines, Inc.*, 204-AIR-10, 2004-SOX-23 (ALJ Dec. 9, 2003), the court held that although a Complainant never identified a particular code section he believed had been violated, the Act merely required that a Complainant have a reasonable belief that he was blowing the whistle on fraud and protecting investors. In fact, “[a] belief that an activity was illegal may be reasonable even when subsequent investigation proves a Complainant was entirely wrong. The accuracy or falsity of the allegations is immaterial; the plain language of the regulations only requires an objectively reasonable belief that shareholders were being defrauded to trigger the Act’s protections.” *Halloum v. Intel Corp.*, 2003-SOX-7 (ALJ Mar. 4, 2004).

In *Allen v. Administrative Review Bd., USDOL*, No. 06-60849, _ F.3d _, 2008 WL 171588 (5th Cir. Jan. 22, 2008) (case below ARB No. 06-081, ALJ Nos. 2004-SOX-60 to 62), the court held that an employee’s complaint must “definitively and specifically relate” to one of the six enumerated categories found in § 1514A. It is sufficient that “the individuals to whom [the complaints] were addressed understood the serious nature of [the employee’s] allegations.” *Collins*, 334 F. Supp. 2d at 1377-78.

In *Giurovici v. Equinix, Inc.*, ARB No. 07-027, ALJ No. 2006-SOX-107 (ARB Sept. 30, 2008), the court held that Complainant was not engaged in protected activity because he never conveyed that his disagreements with the report in question meant that the Respondent was engaged in securities fraud or had violated a SEC rule or regulation or any federal law relating to fraud against shareholders. As such, the Complainant did not directly or specifically implicate the listed categories of fraud or securities violations under SOX.

In *Platone v. USDOL*, No. 07-1635 (4th Cir. Dec. 2008), the court held that “a Complainant must alert management to more than the fact that the company’s near-term profits were affected by billing discrepancies in order to meet the standard of definitively and specifically alleging mail or wire fraud [under the whistleblower provision of SOX].” In *Bozeman v. Per-Se Technologies, Inc.*, 1:03-CV-3970 (N.D. Ga. Sept. 12, 2006), the court held that “While a plaintiff need not show an actual violation of law by his employer, or cite a code section he believes was violated, ‘general inquiries ... do not constitute protected activity’ ” *Collins*, 334 F. Supp. 2d at 1376. “[I]n order for the whistleblower to be protected by [SOX], the reported information must have a certain degree of specificity [and] must state particular concerns, which, at the very least, reasonably identify a Respondent’s conduct that the Complainant believes to be illegal. “[g]eneral inquiries ... do not constitute protected activity.” *Bechtel Constr. Co. v. Sec’y of Labor*, 50 F.3d 926, 931 (11th Cir. 1995).

Additionally, in *Walton v. NOVA Information Systems*, 2005-SOX-107 (ALJ Mar. 28, 2006), the ALJ rejected the Respondent’s argument that, to be protected activity under the SOX, the Complainant’s allegation of a violation of a SEC rule or regulation

must be related to fraud against shareholders. The ALJ found that to rule otherwise would be to in effect remove the phrase “any rule or regulations of the Security and Exchange Commission” from the SOX. In *O’Mahony v. Accenture Ltd.*, No. 1:07-CV-07916 (S.D.N.Y. Feb. 5, 2008), the court disagreed with authority holding that § 1514A limits the activity to be protected only to reporting conduct that involves “fraud against shareholders.” The court held that by listing certain specific fraud statutes to which § 1514A applies and then extending the reach of the whistleblower protection to violations of any provision of federal law relating to fraud against securities shareholders, § 1514A clearly protects an employee against retaliation based upon the whistleblower’s reporting of fraud under any of the enumerated statutes regardless of whether the misconduct relates to “shareholder fraud.”

Finally, a Complainant need not expressly identify the complained of actions as illegal depending on to whom the Complainant reports the actions. In *Deremer v. Gulfmark Offshore Inc.*, 2006-SOX-2 (ALJ June 29, 2007), in regard to whether a Complainant must expressly state that he considers the conduct to be illegal, the ALJ found that an examination must be made of the context in which and to whom the statements were made. In this case, the statements were made to the controller, auditors and an investigating law firm, all of whom should logically have recognized fraudulent behavior if the Complainant described it to them. Thus, the ALJ found that the Complainant was not required to specifically state to the Respondent that the activity of which he complained was illegal.

c. Reports Of Mail & Wire Fraud Need Not Relate To Fraud Against Shareholders

The relevant language of the mail-fraud (18 U.S.C. §1341) and wire-fraud (18 U.S.C. §1343) statutes is the same: “Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises . . . [uses the mails of wires, or causes their use] for the purpose of executing such a scheme or artifice . . . shall be punished.” “It is well settled that cases construing the mail fraud and wire fraud statutes are applicable to either.” *United States v. Shipsey*, 363 F.3d 962, 972 n. 10 (9th Cir. 2004). Both statutes are enumerated in SOX and provide the basis for a protected activity.

When a SOX whistleblower complaint is grounded in federal mail and wire fraud statutes, “the alleged fraudulent conduct must at least be of the type that would be adverse to investor’s interests.” *Platone v. FLYi, Inc.*, ARB No. 04-154, ALJ No. 2003-SOX-27 (ARB Sept. 29, 2006).

In *Reyna v. ConAgra Foods, Inc.*, No. 3:04-CV-00039 (M.D. Ga. June 11, 2007), Plaintiffs contended that they were terminated for reporting two incidents of fraud and that the fraudulent activities involved the use of mail or the internet and thus, the reporting of the activities were protected under SOX. Defendant argued that the reporting was not protected activity because the reports of mail fraud and wire fraud did not relate to “fraud against shareholders.” The court denied summary judgment holding,

“The statute clearly protects an employee against retaliation based upon that employee’s reporting of mail fraud or wire fraud regardless of whether that fraud involves a shareholder of the company.”

d. What Was Actually Communicated To The Respondent, Rather Than What Was Alleged In The Complaint, Determines Whether There Was A Protected Activity

In determining whether the Complainant engaged in protected activity, “the relevant inquiry is not what she alleged in her [OSHA complaint], but what she actually communicated to her employer prior to [her] termination.” *Platone v. FLYi, Inc.*, ARB No. 04-154, ALJ No. 2003-SOX-27 (ARB Sept. 29, 2006).

Although the law does require that a whistleblower do more than imply that a SOX violation occurred. In *Van Asdale v. International Game Technology*, No. 3:04-CV-00703-RAM (D. Nev. Aug. 10, 2007), Plaintiffs argued that Defendant’s General Counsel was an extremely sophisticated recipient of the information and must have understood that they were alleging shareholder fraud. The court held that although an inference could be drawn that he so understood, the law requires that a whistleblower do more than imply that a SOX violation occurred.

5. SOX Does Not Have A Materiality Standard

The Act “places no minimum dollar value on the protected activity it covers” and “[t]he mere existence of alleged manipulation, if contrary to a regulatory standard, might not be criminal in nature, but it very well might reveal flaws in the internal controls that could implicate whistleblower coverage for seemingly paltry sums.” *Morefield v. Excelon Services, Inc.*, 2004-SOX-2 (ALJ Levin, Jan. 28, 2004). However, under Supreme Court authority, for information to be material, there must be “a substantial likelihood that a reasonable shareholder would consider [the matter] important to his decision to invest.” *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976).

6. “Unfavorable Personnel Decision” Defined

Sarbanes-Oxley provides that an employer may not “discharge, . . . suspend, threaten, harass, or in any other manner discriminate against an employee in the terms and conditions of employment.” 18 U.S.C. § 1514A (a)(1). In *Allen v. Administrative Review Bd.*, 514 F.3d 468 (5th Cir. 2008) (case below ARB No. ARB No. 06-081, ALJ Nos. 2004-SOX-60 to 62), the court held that the *Burlington Northern & Santa Fe Railway Co. v. White*, 126 S. Ct. 2405 (2006), definition of “unfavorable personnel action” applies to SOX whistleblower claims -- *i.e.*, a plaintiff must show that a reasonable employee would have found the challenged action materially adverse, which in this context means it well might have dissuaded a reasonable worker from engaging in the protected activity.

D. Post Hearing Appeals

There is no time requirement in which the ALJ must issue a decision and order. However, an ALJ decision must contain appropriate findings, conclusions, and an order pertaining to remedies if appropriate.

Any party seeking review must file a written petition with the Administrative Review Board (“ARB”) within ten (10) business days of the date of the ALJ decision. The ALJ decision will become final unless the ARB issues an order within thirty (30) days of the filing of the petition notifying the parties that the case has been accepted for review.

After the ARB issues a final order, the adversely affected party may, within sixty (60) days after the issuance of that order, file a petition for review with the United States Court of Appeals for the circuit in which the violation allegedly occurred or the circuit in which the Complainant resided on the date of the violation.