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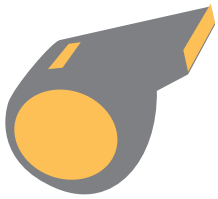
SOX Whistleblower Team Management Alert



Top 10 Whistleblower Decisions Of 2011

Whistleblower litigation implicating a wide range of critical compliance issues continued to proliferate in 2011, and we saw a range of game-changing decisions. Here are some of the tunes that courts, whistleblowers and employers were singing last year.

#10: Don't Look Back (Boston)

Henderson v. Masco Framing Corp., No. 11-cv-00088, 2011 U.S. Dist. LEXIS 80494 (D. Nev. July 22, 2011)

This case of second impression results in a split in the approach federal courts have taken in determining whether the provision in the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) precluding mandatory pre-dispute arbitration of whistleblower claims under Section 806 of the Sarbanes-Oxley Act of 2002 (SOX) is retroactive.

Before July 2010 (when Dodd-Frank was enacted), Plaintiff entered into a pre-dispute arbitration agreement with his employer, which governed all claims under federal law, including SOX whistleblower claims. Plaintiff filed suit under Section 806 of SOX, alleging he was discharged in retaliation for complaining that the company improperly withheld FICA Medicare taxes from his retention bonuses. He moved to compel arbitration, and the court focused on whether Dodd-Frank applies retroactively. In considering Plaintiff's motion, the court acknowledged that there were "two non-binding, diametrically-opposed cases supporting [the parties'] respective positions" – *Riddle v. DynCorp Int'l Inc.*, 733 F. Supp. 2d 743 (N.D. Tex. 2010) (denying retroactive application) and *Pezza v. Investors Capital Corp.*, No. 10-cv-10113, 767 F. Supp. 2d 225 (D. Mass. Mar. 1, 2011) (giving retroactive application). The court, however, rejected the *Pezza* court's approach and stressed that the presumption against retroactivity is particularly strong where, as in this case, a retroactive application would eliminate established contractual rights. Accordingly, the court granted the employee's motion to compel arbitration.

#9: Too Much Too Little Too Late (Johnny Mathis and Deniece Williams)

Schroeder v. Greater New Orleans Fed. Credit Union, No. 10-cv-31169, 2011 WL 6307889 (5th Cir. Dec. 19, 2011)

The Fifth Circuit reversed the dismissal of a whistleblower retaliation claim under the Federal Credit Union Act (12 U.S.C. § 1790b(a)(1)) (the Act), based on, among other reasons, a perceived lack of timely and complete documentation regarding a whistleblower's performance problems.

Plaintiff was a manger in the company's lending department and call center. Around December 2007, Plaintiff informed the CEO that she believed potentially fraudulent conduct was occurring in connection with lending practices. In March 2008, Plaintiff made the same reports to the Board of Directors (Board). On May 30, 2008, Plaintiff brought her claims of fraud to the chair of the company's Supervisory Committee (Committee). According to Plaintiff, on June 19 and 20, 2008, she made seven calls to the National Credit Union Administration (NCUA). The NCUA had no record of her calls, and she never told any

supervisors about the calls. However, two co-workers claimed that Plaintiff expressed her plans to contact the NCUA in June 2008. A week after her alleged calls to the NCUA, Plaintiff again complained to the Committee, and the company hired an auditor to investigate. The investigation confirmed that some loans violated internal policies, but there was no criminal fraud. In mid-July 2008, co-workers asserted that they informed the CEO that Plaintiff contacted the NCUA. On August 8, 2008, the CEO reduced Plaintiff's salary, and Plaintiff then complained to the Board and Committee that this was retaliatory. Over the next week, the company added complaints about Plaintiff's performance in her personnel file. On October 8, 2008, the Board discharged Plaintiff.

Plaintiff filed a whistleblower retaliation suit under the Act, which expressly bars a credit union from retaliating against an employee because that individual provided information to the NCUA or the U.S. Attorney General regarding any violation (by a credit union) of any law or regulation. The district court granted the company summary judgment. The Fifth Circuit affirmed the finding that Plaintiff's demotion, which was preceded only by internal complaints, was not actionable. But it found that there was a genuine issue of material fact as to whether the Company knew Plaintiff complained to the NCUA. It also ruled that a fact issue existed as to causation given its conclusion that there was little evidence of disciplinary problems in Plaintiff's personnel record, and that Plaintiff's performance issues were recorded in her personnel file after her complaints to the NCUA and just a week before her termination.

#8: Come Together (The Beatles)

DeGuelle v. Camilli, No. 10-cv-2172, 2011 U.S. App. LEXIS 24868 (7th Cir. Dec. 15, 2011)

The Seventh Circuit ruled that retaliation against an employee for reporting alleged criminal activity to law enforcement can constitute a racketeering "predicate act," resulting in liability under the Racketeer Influenced and Corrupt Organizations Act ("RICO"). RICO makes it unlawful for an employee of an enterprise engaged in interstate commerce to "conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity," which requires the commission of at least two "predicate acts" of racketeering. SOX added retaliation for "providing to a law enforcement officer any truthful information relating to the commission or possible commission of any Federal offense" to the list of predicate acts.

Plaintiff filed a lawsuit alleging that his employer terminated him in retaliation for reporting a tax fraud scheme to law enforcement, and argued that his termination was retaliatory and constituted a predicate act under RICO. A rare move in this context, the Seventh Circuit reversed the district court's dismissal of the complaint, finding that Plaintiff sufficiently alleged that the company's motivation in terminating Plaintiff was retaliation for the disclosure of the alleged tax scheme, and concluding that "[r]etaliatory acts are inherently connected to the underlying wrongdoing exposed by the whistleblower."

#7: The Song Remains The Same (Led Zeppelin)

Johnson v. Stein Mart, Inc., No. 10-cv-13434, 2011 U.S. App. LEXIS 18736 (11th Cir. Sept. 9, 2011) (unpublished)

The Eleventh Circuit incorporated defenses common to basic employment law doctrine into the SOX whistleblower context in the course of granting the company summary judgment.

Plaintiff alleged she was transferred, disciplined and discharged from her inventory planner position in retaliation for blowing the whistle on improper accounting and business practices. She began complaining in Spring 2003. On December 1, 2004, the company issued Plaintiff written discipline because she deviated from a purchase plan. On February 11, 2005, Plaintiff received a negative performance evaluation and was placed on a 90-day performance improvement plan. On March 15, 2005, Plaintiff told the CFO that she believed she was retaliated against for her prior internal complaints about what she believed to be unlawful business practices. The CFO conducted an investigation into Plaintiff's claim, and concluded on May 10, 2005 that there was no evidence to support her allegations. On May 19, 2005, the company terminated Plaintiff's employment.

The district court granted the company summary judgment on Plaintiff's Section 806 claim, and the Eleventh Circuit affirmed. The Eleventh Circuit concluded that there was clear and convincing evidence that the company would have discharged Plaintiff in the absence of her complaint. In so concluding, the Eleventh Circuit embraced the employment law doctrine that:

(i) an employer need not be "correct" in determining that a plaintiff's performance is unsatisfactory; (ii) courts "do not sit as a super-personnel department"; and (iii) an employee cannot avoid the consequences of unacceptable performance by blowing the whistle.

#6: With A Little Help From My Friends (The Beatles)

Egan v. TradingScreen, Inc., No. 10-cv-8208, 2011 U.S. Dist. LEXIS 47713 (S.D.N.Y. May 4, 2011)

2011 saw the first decision under Dodd-Frank's anti-retaliation provision. Plaintiff was the company's head of sales for the Americas. In early 2009, he allegedly learned that the CEO was diverting corporate assets to another company that he solely owned. In January 2010, believing that the CEO's behavior was jeopardizing the company's business, Plaintiff reported it to the President of the company, who then contacted the Board of Directors (Board). The Board hired an outside law firm to conduct an investigation, in which Plaintiff participated. The investigation confirmed Plaintiff's allegations. Shortly thereafter, the CEO terminated Plaintiff's employment.

An issue of first impression, the court considered whether Dodd-Frank's anti-retaliation provisions require a plaintiff *personally* to report information to the SEC. Though Plaintiff never personally and directly reported any information to the SEC, he claimed he was protected since he initiated the inquiry and disclosed information in interviews with the law firm conducting the investigation. Plaintiff claimed he was "acting jointly" with the law firm because he expected the law firm to report the information to the SEC. The court agreed with Plaintiff, noting that "[t]he plain text of the statute merely requires that the person seeking to invoke the private right of action have acted with others in such reporting, not that he or she led the effort to do so." It thus found Plaintiff's cooperation with the law firm's investigation sufficient to allow him to invoke Dodd-Frank's protections — provided he demonstrate that the law firm did in fact provide the information to the SEC. Notably, in a subsequent decision in this case, the court dismissed Plaintiff's claim with prejudice because Plaintiff could not show that the law firm relayed his statements to the SEC.

#5: This Is How We Do It (Montell Jordan)

Hemphill v. Celanese Corp., 430 Fed. Appx. 341, 2011 U.S. App. LEXIS 13019, No. 10-cv-10746 (5th Cir. July 23, 2011) (unpublished)

This Fifth Circuit confirmed that conducting an independent investigation into a whistleblower's performance issues substantially heightens an employer's chances of prevailing on summary judgment.

Plaintiff, an internal audit manager, reported concerns that employees were not complying with legal requirements and internal policies. The company investigated and concluded that there were no violations of any laws. But Plaintiff alleged that his supervisor then told him not to "develop issues," and rebuffed his request to report alleged violations of SEC rules to the audit committee. Soon thereafter, Plaintiff allegedly yelled at his secretary. A human resources ("HR") employee who was unaware of Plaintiff's complaints conducted an investigation into this conduct. The employees who were interviewed worked in a different department than Plaintiff and "had no material interest in [Plaintiff's] auditing activities." The HR investigator recommended that Plaintiff be terminated due to his "lying during a formal investigation, harassment of an employee, and creating a negative work environment for the team and those around him."

Plaintiff filed a complaint under Section 806, and the district court granted the company summary judgment. The Fifth Circuit affirmed, finding that Plaintiff's protected activity did not contribute to the discharge decision, noting that the company presented "substantial evidence" that it conducted an investigation into Plaintiff's inappropriate behavior and decided to discharge him on this basis alone. It also found that the company presented clear and convincing evidence that it would have discharged Plaintiff regardless of whether he engaged in protected activity. In so finding, the court emphasized that: (i) the company conducted a thorough investigation; (ii) the HR professionals who supported the recommendation to terminate had no knowledge of the alleged protected activity; (iii) HR interviewed employees who did not work in Plaintiff's department and "had no material interest in plaintiff's auditing activities"; and (iv) the supervisor who allegedly told Plaintiff to not "develop issues" was not involved in the investigation and "simply accepted the unanimous termination recommendation."

#4: Anything Goes (Cole Porter)

Menendez v. Halliburton, Inc., No. 09-002, 2011 DOL Ad. Rev. Bd. LEXIS 83 (ARB Sept. 13, 2011)

In 2011, the U.S. Department of Labor's Administrative Review Board (ARB) adopted a new standard governing "adverse employment actions" under Section 806. Now, according to the ARB, an employee need not experience a "tangible" consequence as a result of protected activity.

Claimant filed suit under Section 806, alleging that the company retaliated against him because he had complained to the SEC and the company's audit committee regarding accounting practices. In particular, he claimed that the company violated his expectations of confidentiality by "outing" him / exposing his identity as a whistleblower. The Administrative Law Judge (ALJ) dismissed his complaint, finding that he had failed to demonstrate that the company had taken adverse action against him. The ARB, however, found that the ALJ erred in finding that Complainant did not suffer an adverse action, concluding that Section 806's reference to the "terms and conditions of employment" does not limit SOX's protections to "economic or employment-related actions." The ARB then analyzed Complainant's claim that the e-mails referencing his whistleblower complaints breached his right to confidentiality under Section 301 of SOX, which requires publicly-traded companies to establish procedures for confidential, anonymous submissions of employee complaints. The ARB found that Section 301 "effectively establishes a 'term and condition' of employment within the meaning of Section 806's whistleblower protection provision," and concluded that purportedly outing Complainant was an adverse action.

#3: Don't Stop Believin' (Journey)

Wiest v. Lynch, No. 10-cv-3288, 2011 U.S. Dist. LEXIS 132114 (E.D. Pa. Nov. 16, 2011)

Just as employers thought the sky was falling, this federal court held that the ARB's landmark decision in *Sylvester v. Parexel Int'l LLC* (discussed below) is not binding on federal courts, and continued to embrace a heightened standard for protected activity.

Plaintiffs filed a complaint alleging retaliation under Section 806 after having reported concerns about certain corporate expenditures. The court held that Plaintiffs failed to adequately allege that they engaged in protected activity, and stressed that Section 806 only protects employees who provide information regarding conduct they "reasonably believe" violates one of the laws enumerated in Section 806, and that the complaint must "definitively and specifically" relate to such laws. Following the dismissal of the complaint, Plaintiffs moved for reconsideration, relying on the ARB's decision in *Sylvester* rejecting the "definitively and specifically" standard. The court denied the motion, holding that "[a]n ARB decision is not binding authority on a United States district court." The court followed the lead of the First, Fourth, Fifth and Ninth Circuits in strictly applying the "definitively and specifically" standard. It also reiterated that the complaint was properly dismissed because Plaintiffs failed to establish that they had conveyed an objectively reasonable belief that fraud occurred.

#2: Upside Down (Diana Ross)

Sylvester v. Parexel Int'l LLC, No. 07-123, 2011 WL 2165854 (ARB No. 07-123) (*en banc*)

This decision is nearly the pinnacle of the liberal approach the ARB took last year in interpreting Section 806. Complainants reported to company managers that their co-workers failed to properly record test times for clinical drug trials that the company performed on behalf of drug manufacturers; that management responded that it "was no big deal"; and that they then were subjected to various forms of retaliation. The ALJ dismissed the complaint, finding that Complainants failed to establish they engaged in SOX-protected whistleblower activity. However, the ARB reversed, making the following significant pronouncements:

- The federal pleading standards do not apply to SOX whistleblower claims initiated with OSHA.
- An employee's complaint need not "definitively and specifically" relate to the categories listed in Section 806, and need not relate to fraud on shareholders.

- The "reasonable belief" standard does not require that the complainant actually communicate the reasonableness of his or her belief to management or other authorities.
- Section 806 protects complaints about a violation of law that has not yet occurred, provided that the employee reasonably believes, based on facts known to him or her, that the violation is about to be committed.
- A complainant need not establish the elements of criminal fraud.

The question now is whether federal courts will defer to this decision.

#1: Breaking The Law (Judas Priest)

Vannoy v. Celanese Corp., No. 09-1118, 2011 DOLSOX LEXIS 68 (ARB Sept. 28, 2011)

The ARB ruled that a whistleblower's misappropriation of confidential information in violation of a confidentiality agreement – which could irreparably harm the company and damage many other employees – might still qualify as protected activity.

Complainant was the former administrator of the company's expense reimbursement program. He filed an internal complaint asserting that the company's system of administering its electronic expense reimbursement and corporate credit card system, and alleged misuse of employee credit cards, posed financial risk to the company. Unbeknownst to the company, Complainant submitted a complaint under the IRS Whistleblower Reward Program, with which he disclosed the information he had misappropriated.

Following his discharge, Complainant filed a complaint with the OSHA under Section 806. OSHA dismissed the complaint, as did an ALJ, but the ARB ruled in Complainant's favor. The ARB recognized the tension between employer confidentiality policies and employee whistleblower bounty programs, which preclude companies from enforcing or threatening to enforce confidentiality agreements to prevent whistleblowers from cooperating with the SEC. The ARB directed the ALJ to conduct an evidentiary hearing to determine whether the information the complainant misappropriated was the kind of "original information" Congress intended to protect and whether the method of transfer of information was protected lawful conduct within the scope of SOX. In this regard, the ARB indicated that while Complainant's conduct may have violated company policy, no charges were brought in connection with his conduct. However, the ARB did not otherwise define "lawful conduct" in this context.

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