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Blowing your SOX off:

What is whistleblowing while you work?

Sarbanes-Oxley has become the new battleground for claims of whistleblower protections. Where the law is, and isn't.

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A decade ago, a federal district court examining New Jersey's Conscientious Employee Protection Act (CEPA) helped narrow the scope of one of the most far-reaching whistleblower statutes in the country. In *Blackburn v. United Parcel Service, Inc.,* 3 F. Supp. 2d 504 (D.N.J. 1998), the district court rejected a plaintiff's CEPA whistleblower claim finding, in part, plaintiff only did what he was obligated to do in his managerial capacity when he questioned his employer's pricing policies. The court reasoned plaintiff had not engaged in a protected activity by bringing to the company's attention a multitude of issues he was otherwise required to do as a manager, and CEPA did not protect those who, as the court put it, were simply "squeaky wheels" and "pains in the ass."

In the years since *Blackburn*, federal and state legislatures have enacted new whistleblower laws and amended existing ones providing employees with new avenues for claiming anti-retaliation protection. One statute frequently worrying employers is the Sarbanes-Oxley Act of 2002 (SOX). Since its passage, the law has become a favorite for plaintiffs attorneys who have attempted to wedge a wide range of employee complaints under its purview.

Sarbanes-Oxley suit

Section 806 provides employees of publicly traded companies with protection against adverse employment action due to the employee assisting in investigations related to certain categories of fraud or for reporting such behavior. Taking a cue from SOX, the New Jersey legislature amended CEPA in 2005 to specifically address SOX-like reports of fraud against shareholders. Specifically, the legislature amended N.J.S.A. 34:19-3 by inserting provisions protecting disclosure of information regarding "any violation involving deception of, or misrepresentation to, any shareholder, investor, [or] client."

Statutes like SOX have reopened the debate as to whether complaining employees are engaging in a protected activity or are simply being "squeaky wheels."

Civil whistleblower protection

To establish a *prima facie* case of discrimination under SOX, a complainant must show (1) he engaged in protected activity as defined by the law, (2) the employer knew of the protected activity, (3) he was the subject of an adverse employment action, and (4) the protected activity was a contributing factor to the adverse employment action. *Livingston v. Wyeth, Inc.,* 2006 U.S. LEXIS 52978, *24 (M.D.N.C. July 28, 2006.

Section 806 makes it unlawful for covered entities to discharge, demote, suspend, threaten, harass or in any other way discriminate against an employee in the terms and conditions of employment because the employee engaged in protected activity as defined by the law. Under §806, protected activity is defined as any lawful act by the employee to:

1. provide information;
2. cause information to be provided; or
3. otherwise assist in an investigation regarding conduct the employee reasonably believes constitutes a violation of:

a) federal criminal mail, wire, bank and securities fraud statutes;
b) SEC rules or regulations; or
c) any federal law related to fraud against shareholders

when the information is provided to or the investigation is conducted by a:
(i) federal regulatory or law enforcement agency;
(ii) a member or committee of Congress; or
(iii) a person with supervisory authority over the employee (or a person working for the employer who has the authority to investigate, discover or terminate misconduct).
18 U.S.C. § 1514 A.

Generally speaking, protected activity is defined under the law as reporting an employer's conduct that the employee reasonably believes constitutes a violation of the laws and regulations related to fraud against shareholders. In *Hughart v. Raymond James & Associates, Inc.,* 2004-SOX-9 (ALJ Dec. 17, 2004), the administrative law judge (ALJ) examined case law developed in environmental and nuclear safety whistleblower cases and determined a protected activity under SOX has three components:
(1) The report or action must involve 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 objectively reasonable; and
(3) The complainant must communicate his concern to either his or her employer, the federal government or a member of Congress.

As noted by the district court in *Bishop v. PCS Admin. (USA), Inc.,* 2006 U.S. Dist. LEXIS 37230*30-31 (N.D. Ill. May 23, 2006):

> "All the statutes and regulations referenced in §1514(a)(1) are ones setting forth fraud. The phrase 'relating to fraud against shareholders' in this provision must be read as modifying each item of the series, including 'rule or regulation of the Securities and Exchange Commission.' "

Like the court in *Bishop*, the administrative review board in *Platone v. FLYi, Inc.,* 04-154, 2003-SOX-27 (ARB Sept. 29, 2006), found that in order to be protected activity under SOX, "the alleged fraudulent conduct must at least be of the type that would be adverse to investors' interests." In reaching this decision, the board cited the law's preamble that states the purpose of SOX is to "protect investors." Therefore, in order to be considered protected activity under SOX, the complained-of activity must not only relate to federal criminal mail, wire, bank and securities fraud statutes; SEC rules or regulations; or any federal law, but to ones specifically relating to fraud against shareholders.

When 'blowing the whistle' is part of the job

Many jobs, by their very nature, involve the reporting of suspected anomalies, irregularities and other such issues. But does that automatically convert these employees to whistleblowers subject to statutory protection? In *Robinson v. Morgan Stanley*, 2005-SOX-44 (ALJ March 26, 2007), the complainant was the respondent's internal auditor. When the complainant believed the company was not seriously treating concerns she raised about its fiscal health, she prepared a memorandum documenting what she believed to be failures in audit controls and management fraud. The ALJ rejected the complainant's claim finding the concerns she raised pursuant to her duties as an internal auditor were not protected activity under SOX.

However, three months later, an ALJ in *Deremer v. Gulfmark Offshore Inc.*, 2006-SOX-2 (ALJ June 29, 2007) muddied the issue. The court explained that excepting one's job duties from protected activity under SOX would violate the spirit of the law. In this case, which like *Robinson* involved an auditor who raised concerns about internal controls, the judge pointed out that "[t]he Act contains no language excluding one's job duties from protected activity." Based on these conflicting decisions, it remains unclear whether an employee would be considered a whistleblower if 'blowing the whistle' is part of his or her job.

When a whistleblower 'calls foul'

The confusion is not limited to SOX. The state Superior Court has found CEPA also protects employees who blow the whistle on themselves. In *Donofry v. Autotote Systems, Inc.*, 350 N.J. Super 276 (App. Div. 2001), the plaintiff, a general manager, was responsible for ensuring employees were licensed by the Casino Control Commission at the defendant's Atlantic City simulcasting facility. Under his watch, a number of employees worked without the requisite licenses and the plaintiff eventually disclosed these violations to the company's local counsel. Soon after, the company terminated the employee for "cost[ing] the company a lot of money and ... jeopardiz[ing] their license[.]"

The plaintiff filed suit under CEPA, claiming his reporting of his own transgression was protected activity. Despite the company's logical argument the plaintiff should not be protected under CEPA because he allowed the violations to happen, the court emphasized the company would not have known of the violations but for plaintiff's revelation. Accordingly, the court rejected the defendant's argument that the plaintiff's own role in allowing the reported violations precluded his recovery. In doing so, the court noted it was "not aware of any New Jersey case holding that [a] plaintiff's participation in the unlawful conduct he reports is a *per se* bar to a whistleblower claim."

How does an employer know the whistle has been blown?

While ALJs have typically found an employee's complaints must relate to fraud against shareholders, this has not stopped creative plaintiffs lawyers from arguing the most innocuous workplace complaints constitute protected activity under SOX.

For example, in *Espinoza v. Sysco Corp.*, 2005-SOX-25 (ALJ Dec. 27, 2006), the complainant, a lead diesel mechanic in one of the respondent's facilities, alleged his supervisor asked him to repair the supervisor's personal vehicle and that of another manager. When another employee reported this to Sysco human resources, the company began an investigation. As part of that investigation, the complainant confirmed he had repaired personal vehicles at his supervisor's direction. Two months later, the company demoted the complainant.

The complainant filed a SOX complaint with OSHA alleging his internal complaints about the repair of personal vehicles resulted in his demotion. OSHA found the complainant had not engaged in protected activity under the law.

On appeal, the ALJ granted summary decision to the employer, affirming OSHA's finding that the complainant had not engaged in protected activity. In response to the employer's motion, the complainant argued he "reasonably believed" his disclosures regarding his supervisor's actions constituted a fraud on shareholders. Specifically, the complainant alleged:

> " … [he] reasonably believed that: (1) "section 1341 (frauds and swindles) was violated" when [his supervisor] ordered him to "fluff" his "work time onto company vehicles;" (2) "section 1342 [*sic*] fraud by wire, radio, or television] was violated when [his supervisor] used the company phone to order the engine for the Company Presidents [*sic*] personal vehicle and to order parts on company accounts," and (3) the 'Securities and Exchange Act of 1934 was violated by the SYSCO Corporation statement that it has internal controls to prevent the unauthorized use of company assets which is stated in the annual report.' "

In support of its finding these reports did not constitute protected activity under the law, the ALJ found the complainant had merely provided information about a particular use of a company resource and may have raised a possible violation of some internal company policy. However, the complainant had not identified anything close to fraud against shareholders. The judge reasoned even though the servicing of personal vehicles cost the company the value of parts and labor, this did not involve "any sort of transaction involving fraud against shareholders or intentionally deceitful statements made to actual or potential investors about the value of the company, or anything else that could reasonably and objectively be deemed a fraud against shareholders." While the complainant had cast his complaints in terms of shareholder fraud in his motion papers, the court found no evidence he provided the company with information that "definitively and specifically" related to any of the listed categories of fraud or securities violations under §806.

Courts, like in *Espinoza*, have looked to a decision of the Department of Labor's Administrative Review Board to support the finding that it is the employee's complaint to the employer — not the spin placed on the complaint in the submission to OSHA — that determines whether the employee engaged in protected activity. In *Platone v. FLYi, Inc.* the complainant, a manager of labor relations for a regional airline, uncovered irregularities in the pilot-union representatives' requests for removal from flight service. Pursuant to a collective bargaining agreement between the airline and the pilot's union, a pilot who needed to perform union-related business could request he or she be removed from scheduled flight service. The airline paid the pilot for the hours worked and also incurred the cost of paying a substitute pilot for performing the flight services. The complainant, the labor relations manager, became aware a number of pilots had picked up trips on their scheduled days off and later dropped those same trips to attend to previously scheduled union-related business. The union's policy did not cover reimbursement for dropped trips picked up on days originally scheduled off. The complainant brought this issue to the attention of her supervisor seeking advice on how to handle the situation.

Shortly after discovering the reimbursement issue, the company learned the complainant had been involved in a romantic relationship with a pilot, in violation of the company's conflict-of-interest policy. The company suspended and then terminated the complainant due to this conflict of interest.

The complainant filed a SOX whistleblower complaint with OSHA alleging the company terminated her employment after she discovered and reported a scheme to defraud shareholders and members of the pilots' union. She alleged that she "reasonably believed" the flight pay loss scheme violated federal mail and wire fraud statutes and SEC regulations regarding shareholder fraud. OSHA initially denied the complaint. On appeal, the ALJ found the complainant's report involved possible fraud by the pilot's union that could affect the airline's financial performance. The ALJ therefore concluded the company terminated the complainant in violation of SOX.

On appeal, the administrative review board declined to adopt the ALJ's recommended decision. In examining alleged protected activity under the law, the board found the relevant inquiry is not what the complainant alleged in her complaint to OSHA, but what she had actually communicated to her employer before her termination. The board found the issues complainant had identified regarding the flight loss pay did not involve shareholder fraud as she alleged in her complaint to OSHA. Rather, it found the complainant had simply raised a possible violation of an internal union policy, and expressed concern over how it might affect the employer's ability to collect a debt. The board found these concerns did not involve fraud against shareholders.

Debate rages on

While many courts have adopted the reasoning from decisions like *Bishop*, *Espinoza* and *Platone*, the non-precedential nature of these administrative decisions means the door still may be open for creative plaintiffs to bring SOX claims based on complaints with little relation to shareholder fraud. Last year, a federal district court in Georgia went a step further and found SOX protected employees whose complaint had nothing to do with shareholder fraud. In *Reyna v. Conagra Foods, Inc.*, 506 F. Supp.2d 1363 (M.D. Ga. 2007), the district judge found an employee engages in protected activity when he or she reports behavior the employee reasonably believes to constitute fraud, regardless of whether or not the suspected fraud is against shareholders. This reasoning was recently adopted by a judge in the Southern District of New York in *O'Mahony v. Accenture Ltd*, 07-CIV-7916 (S.D.N.Y. Feb. 5, 2008).

While the court's decisions in *Reyna* and *O'Mahony* are contrary to the Department of Labor's own interpretation of protected activity under SOX as set forth in the decisions of OSHA, ALJs and the ARB, they demonstrate the expansive view federal courts have taken regarding protected activity under the Act. As such, it may serve to bolster plaintiffs' claims they were terminated for engaging in whistleblowing under the law.

Given that case law examining the whistleblower protections afforded by SOX is still developing, prudent employers should investigate all employee complaints and carefully document the findings. While the level of investigation necessarily is dependent on the issues raised in the complaint, a proper investigation supported by documentation will go a long way to help defend whistleblower complaints, regardless of the statute they are brought under.

Likewise, employers should document all instances of employee misconduct or performance deficiencies. Such documentation also will help support any adverse actions taken against the employees, demonstrating the action was unrelated to the employee's alleged protected activity. Absent controlling case law, prudence, common sense and effectively implemented human resources policies and procedures continue to be an employer's best defense to whistleblower claims.

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