

## Whistleblower Protection Pitfalls

Innocent companies are drained in defending adverse-action claims.

BY MARY E. PIVEC

In adopting the whistleblower protections contained in the Sarbanes-Oxley Act, Congress undoubtedly intended to deter fraud against shareholders by empowering employees, agents, and contractors of public companies to police and report corporate accounting practices that could have a material impact upon corporate solvency and net worth—without fear of unlawful retaliation.

Congress concluded that but for the whistleblowing of Sherron Watkins, Enron's massive accounting fraud would have gone undetected for far longer and injured far more innocent investors.

But Congress, unfortunately, legislated in haste and has produced a system that fails to serve the investing public. It also results in serious injustices to accused employers. As a result, SOX frequently drains innocent public companies of thousands of dollars in legal fees defending whistleblower claims relating to nonmaterial accounting decisions and the legitimate exercise of management prerogatives.

The SOX whistleblower provision prohibits companies from discriminating against anyone who lawfully assists in an investigation or proceeding relating to a violation of the federal securities laws or Securities and Exchange Commission rules, or who internally reports activity that he or she reasonably believes constitutes a violation of the securities laws relating to fraud.

An employee, consultant, or agent who believes he has been retaliated against for whistleblowing may file a complaint within 90 days following the discovery of the discriminatory conduct with the U.S. Department of Labor's Occupational Safety and Health Administration. The law entitles successful complainants to obtain equitable relief, including reinstatement, back pay with interest, compensatory and punitive damages, and attorney fees.

The plaintiffs bar has quickly seized upon the whistleblower provision as an easy opportunity for challenging adverse employment actions. In the 30 months since enactment, more than 400 whistleblower complaints have been filed with OSHA. The agency's goal is to attempt to complete SOX investigations within 60 days of receiving the complaint. As a result, corporate employers are given only 21 days to respond. In some cases,

OSHA investigations have languished for more than 12 months before a decision is issued.

### PRELIMINARY REINSTATEMENT

If OSHA determines there is reasonable cause to believe that the complainant engaged in protected whistleblower activity, that the activity was known to the company, and that adverse employment action was subsequently taken against the complainant, then OSHA must order the employee reinstated to his former position with full back pay pending any appeal of the liability determination by the employer. Should the employer ultimately prevail after an evidentiary hearing, the law precludes the employer from recovering the wages paid to the losing complainant.

The unfortunate employer seeking to challenge an OSHA reinstatement order has limited options. Regulations permit the employer to move to stay a reinstatement order before the Department of Labor's Office of Administrative Law Judges (OALJ). Yet to prevail, the employer must show not only a substantial likelihood that it will ultimately prevail (even though it has not yet had the opportunity to conduct any discovery), but also that reinstatement would cause irreparable harm to the employer, either as a safety or a security risk. In *Bechtel v. Competitive Tech. Inc.*, on March 29, 2005, the ALJ held that an OSHA finding of reasonable cause "strongly militates in favor of finding that the public policy supports reinstatement of Complainants, even given the uncomfortable circumstances that would reasonably accompany their return to the workplace."

### BAD PUBLIC POLICY

In my opinion, this is not good public policy. At a minimum, an accused employer should have the opportunity to review the OSHA investigative file and to depose the complainant prior to making its case for a motion to stay. Until the employer has had a fair chance to explore the basis for the complainant's protected activity claim, and to discover information supporting the existence of a safety or security risk, it is unfair to task the employer with proving that it has a substantial likelihood of success.

Although the Supreme Court approved the preliminary reinstatement remedy in the late 1980s in the whistleblower provisions of the

Surface Transportation Act, some of the language of the plurality decision suggests that the protracted nature of the review procedures provided by the Department of Labor in SOX cases is a serious violation of a corporate respondent's property interest in determining the composition of its work force—particularly in the executive suite. It is well-established that a corporate defendant is protected by the Fifth Amendment due process clause, and that it cannot be deprived of a property interest without a prompt post-deprivation hearing. Despite this, it may take two years or more for the employer to exhaust the SOX hearing process.

Although SOX cases are supposed to be handled on an expedited basis, particularly where preliminary reinstatement is involved, ALJs must also adjudicate a broad range of other claims as well. Assuming a corporate employer is lucky enough to get a decision within nine months of docketing its request for a hearing with the OALJ, the losing party has a right to request review by the Department's Administrative Review Board—which can tack six months or more onto the agency process.

Only after exhausting the Department of Labor's administrative review procedure is a corporate litigant entitled to review by a federal court. But even that review is limited to the record of the evidence and arguments developed before the Department of Labor. By contrast, Congress has given whistleblowers the option of short-circuiting the Labor Department process and litigating their claims before a federal jury once a complaint has been pending for 180 days.

### WHAT'S PROTECTED

Another deficiency in the whistleblower scheme is uncertainty as to what constitutes protected activity.

Congress clearly did not intend that chronic complainers would obtain protection under the SOX whistleblower provisions based on rank speculation that some aspect of an employer's management or accounting practices could arguably impact stock performance and shareholder value. Emerging case reports suggest that a number of SOX complaints have just these characteristics.

Additionally, in several decided cases, the gravity or materiality of the alleged financial impropriety was ruled to have no bearing on the complainant's right to reinstatement, back pay, compensatory damages, and attorney fees. For example, in *Morefield v. Excelon Services Inc.*, 2004-SOX-2 (ALJ Jan. 28, 2004), the judge held that the alleged improper manipulation of financial data impacting a mere .0001 percent of the respondent's annual revenues was sufficient to support a SOX whistleblower claim.

Despite the cases, corporate defendants should be prepared to strike hard at the reasonableness of the complainant's claims that particular financial transactions constituted fraud against the shareholders. A complainant must prove that at the time of the disclosure he or she harbored a subjective belief that a fraud had been perpetrated, and that the belief was objectively reasonable in light of his training and experience.

In *John C. Grant v. Dominion East Ohio Gas*, 2004-SOX-00063 (March 10, 2005), the respondent was successful, in part, because the employee, an engineering technician, couldn't prove that in questioning the alleged "accounting irregularities" he had sufficient information to form a belief that the irregularities constituted fraud. Although the administrative law judge also determined that the employer was not a covered party under SOX, the judge made the following observation that I hope will be adopted by her colleagues and the Administrative Review Board:

"The fact that [the complainant's] questions and concerns

happened to involve accounting and finances in some way does not automatically mean or imply that fraud or any other illegal conduct took place . . . Simply raising questions and lodging complaints [about accounting errors or procedures] without reference to or suspicion about fraud against shareholders is not protected activity."

Complainants have also been found wanting in proving their claims of corporate fraud to be objectively reasonable. In general, the more sophisticated and well-educated the complainant is in terms of financial and accounting procedures, the more stringent the test of objective reasonableness. For example, in *Lerbs v. Buca di Beppo*, 2004-SOX-8 (ALJ June 15, 2004), the court rejected claims of accounting fraud made by a corporate controller who should have realized that the employer's accounting standards and practices met accepted norms.

The fact is that once a complainant makes it past the "reasonableness" test, he is practically assured of victory in a whistleblower case. Although the federal courts have become more and more demanding of Title VII plaintiffs in retaliation cases in terms of demonstrating causation, the same cannot be said of OALJ judges and the Administrative Review Board in whistleblower cases. As a general rule, the closer in time the protected conduct is to an adverse action, the more likely causation will be inferred. However, even gaps of six months or more have not deterred findings of causation.

Compounding the difficulties of defending SOX cases is the rule that once a complainant has established a prima facie case, the burden shifts to the respondent to establish by "clear and convincing evidence" that it would have taken the action against the complainant whether or not he engaged in SOX-protected activity.

This is an extremely difficult burden, at a minimum requiring proof of documented poor performance and disciplinary intent that predates the protected activity. By comparison, in employment discrimination cases based on race, sex, national origin, religion, and disability, an employer need only articulate a legitimate, nondiscriminatory reason for taking the employment action. And although Congress has recognized "mixed motive" as a separate type of discrimination claim in Title VII and disability cases, such plaintiffs cannot obtain reinstatement, back pay, and compensatory damages. (In a mixed-motive case, the plaintiff acknowledges that unlawful discrimination was one of only several reasons for the adverse employment action.)

In SOX cases, by contrast, even a legitimate business reason will not save a corporate defendant from major liability and injunction penalties if the judge concludes that retaliation against the whistleblower played any role in the decision to take the challenged employment action. It is difficult to justify such heavy-handed treatment of employers, particularly in the absence of a carefully drawn definition of protected activity.

Thus far, corporate America has not raised a significant challenge to the SOX complaint adjudication system. Perhaps that is because the law is still new, and only a small percentage of public companies have been affected so far. Nevertheless, something should be done to correct abuses in the system.

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