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“PROTECTED ACTIVITY” CONTINUES TO BROADEN UNDER SOX

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Whistleblower claims under the Sarbanes-Oxley Act of 2002, 18 U.S.C. § 1514A (“SOX”) are on the rise. Plaintiffs’ attorneys are catching on quickly, especially given the trend towards broadening the scope of whistleblower protections under SOX. In light of the recent case law below, corporate employers should tread carefully when it comes to employee complaints about corporate fraud and wrongdoing.

Whistleblower Protections Under SOX

SOX contains protections for employees who “blow the whistle” by reporting suspected violations of corporate fraud and wrongdoing.

Section 806 of SOX, codified in § 1514A(a), prohibits publicly-traded companies from retaliating against employees for “any lawful act done by the employee . . . to provide information, cause information to be provided, or otherwise assist in an investigation regarding any conduct which the employee reasonably believes constitutes” a violation of 18 U.S.C. § 1341 (mail fraud), 18 U.S.C. § 1343 (mail, radio or television fraud), 18 U.S.C. § 1344 (bank fraud), 18 U.S.C. § 1348 (securities fraud), “or any rule of regulation of the Securities and Exchange Commission [“SEC”] or any provision of Federal law relating to fraud against shareholders.” 18 U.S.C. § 1514A(a).

Whistleblower claims under Section 806 are subject to a burden-shifting framework. In order to establish a claim of retaliation, an employee must establish by a preponderance of the evidence that:

- (1) the employee engaged in protected activity (i.e., blew the whistle);
- (2) the employer was aware of the employee’s protected activity;
- (3) the employee suffered an adverse employment action; and
- (4) the employee’s protected activity was a contributing factor in the unfavorable action.

Bechtel v. Admin. Review Bd., 710 F.3d 443, 447 (2d Cir. 2013). Section 806 also requires that the employee show that he “reasonably believed” his employer’s conduct constituted a SOX violation, and that belief must be objectively and subjectively reasonable. 18 U.S.C. § 1514A(a); Rhinehimer, 787 F.3d at 805.

If the employee meets his burden, the employer faces the uphill battle of establishing, “by clear and convincing evidence,” that it would have taken the same adverse action absent the protected activity. Rhinehimer, 787 F.3d at 806.

Employee Engaging in “Protected Activity” Must Have Subjective and Objective Reasonable Belief of a SOX Violation

Courts and the Department of Labor consider an employee’s knowledge and expertise when determining whether an employee’s belief that his employer was violating SOX was reasonable. For example, in Becker v. Community Health Systems, Inc., 2014-SOX-00044 (ALJ Nov. 9, 2016), the complainant (a Chief Financial Officer) alleged that

he was constructively discharged after he refused to adjust the corporation's earnings figure from negative \$12.8 million to negative \$4 million without explanation. The Administrative Review Board ("ARB") held in the complainant's favor, finding that his extensive experience supported the reasonableness of his skepticism regarding the reduction.

However, an employee's knowledge level can also be held against him or her. In Beacom v. Oracle America, Inc., the Vice President of one of Oracle's Sales Divisions alleged that the company falsely projected inflated sales revenue numbers. 825 F.3d 376, 381 (8th Cir. 2016). The Eighth Circuit held that plaintiff's alleged belief that the company was defrauding its investors was objectively unreasonable. Id. The Court reasoned that an individual in plaintiff's position would have understood the "predictive nature" of sales projections and that the alleged discrepancy in the figures (although \$10 million dollars) was only "minor" given that Oracle annually generated billions of dollars. Id.

"Protected Activity" Must Relate to Fraud Under SOX, Although Mail and Wire Fraud Are Broadly Construed

Another recent ARB decision, Dietz v. Cypress Semiconductor Corp., ARB No. 15-017, 2016 WL 1389927, at *5 (ARB March 30, 2016), broadened the scope of "protected activity" even further. In Dietz, the complainant worked as a program manager and sent an email to his supervisor invoking the corporation's whistleblower policy and complaining that the bonus plan violated state wage law. Id. at *2. In a later teleconference, the complainant complained that the corporation purposefully did not inform employees that the bonus plan provided for compulsory deductions from their base salary when it gave these prospective employees their offer letters. Id. The complainant alleged a series of retaliatory reprimands and resigned shortly thereafter. Id. at *3-4.

The ARB held that the complainant's email was not "protected activity" because he only reported that he thought the bonus plan violated state wage laws, and this allegation is not enough "without some allegation of a knowing misrepresentation or concealment of material facts." Id. at *5. However, the ARB held that the complainant blew the whistle on the teleconference when he complained that he believed the corporation had acted "knowingly." Id. at *6. The ARB further held that the complainant had a reasonable belief that the bonus plan constituted mail or wire fraud because the corporation used mails or wires in the course of executing and administering the bonus plan. Id. In so holding, the ARB noted that "mail and wire fraud statutes can be triggered even when the connection between the alleged fraud and the use of mails or wires might seem tenuous." Id. While Dietz has been viewed as a victory for whistleblowers, the decision also reinforces the requirement that whistleblower complaints must relate to one of the six categories of fraud under SOX.

Verfuert v. Orion Energy Sys., Inc., No. 14-C-352, 2016 WL 4507317, at *1 (E.D. Wis. Aug. 25, 2016), demonstrates that courts will draw a line between protected and unprotected activity. In Verfuert, the plaintiff, CEO of a publicly-traded company, expressed concern about numerous corporate issues, including alleged stock manipulation and his belief that the company's law firm might have a conflict of interest, to the Board of Directors. Id. On the morning the Board scheduled a meeting to terminate his employment, the CEO sent what he described as a "whistleblower e-mail" to several Board members detailing his concerns. Id. at *3.

The district court granted summary judgment for the company, rejecting the CEO's attempt to elevate complaints about "waste," violations of codes of conduct and breaches of fiduciary duty to fraud under SOX. Id. at *5. The court noted that the CEO's concerns about alleged stock manipulation could have amounted to protected activity, however, the Board was aware of the allegations at least four years before the CEO supposedly "blew the whistle." Id. at *7. The court further held that the CEO's own certification (as accurate) of the company's quarterly and annual reports during the same time period he alleged the company failed to make "required disclosures" rendered it impossible for him to establish that he "subjectively believed" fraud was occurring during the same time frame. Id. at *9.

Lessons for Employers and Their Counsel

- Given the broad scope of “protected activity,” it is critical that employers obtain all of the details about a complaint when it is made. Any fraud-related complaints may likely fall within the broad scope of SOX.
- Employers should create detailed documentation of the employee’s complaint. This will help guard against an employee attempting later to expand the scope of the complaint.
- Employers should tread carefully with potential whistleblower claims as they can be costly.



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