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BY WALKER M. DUKE AND WADE L. MCCLURE

Whistle-Blower Claims Can Cause Collateral Damage to Businesses

IT IS NO SECRET THAT EMPLOYERS HAVE ENJOYED A track record of success in Sarbanes-Oxley (SOX) Act whistle-blower claims. Decisions from the U.S. Department of Labor's Occupational Safety and Health Administration (OSHA) and associated administrative law judges overwhelmingly have gone against the purported whistle-blowers. However, that does not mean companies should start pounding their chests when these claims arise. To the contrary, it is often the collateral damage caused by a SOX whistle-blower claim that creates the worst headaches for a business.

SOX, enacted in 2002, explicitly protects whistle-blowers against discrimination. It provides that publicly traded companies may not discharge, demote, suspend, threaten, harass or otherwise discriminate against an employee because of any lawful act done by that employee: 1. to provide information or assist in an investigation regarding conduct that the employee reasonably believes is a violation of Securities and Exchange Commission (SEC) rules and regulations or fraud against shareholders; or 2. to file, testify, participate in, or otherwise assist in a proceeding relating to alleged violations of the SEC's rules and regulations or federal securities laws.

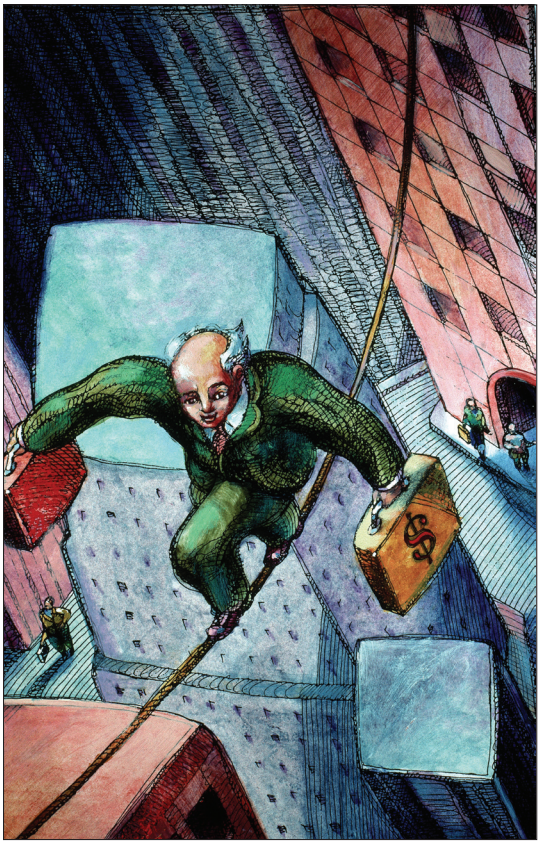
Employees who believe they have been subjected to adverse employment decisions because of their whistle-blowing first must file a complaint with OSHA, which then informs the company and the SEC of the allegations. OSHA will dismiss the complaint without an investigation unless the employee makes a basic showing of the elements of his or her claim, or the employer demonstrates by clear and convincing evidence that it would have taken the adverse employment action regardless of the protected activity.

If the employee meets this initial burden of proof, OSHA will conduct an investigation and issue its findings, including an order of relief if a violation of SOX occurred. Either party may then request further review from an administrative law judge (ALJ) and later appeal the ALJ's decision to the U.S. Department of Labor's Administrative Review Board. Finally, whistle-blowers can pursue litigation in federal court if the Department of Labor does not completely resolve a complaint within 180 days.

An empirical study of whistle-blower claims by Richard E. Moberly in the 2007 *William & Mary Law Review* shows that employers have won an overwhelming majority of decisions at the OSHA and ALJ levels. It also showed, in the first few years of SOX's existence, employees won 3.6 percent of the cases decided at the OSHA level and 6.5 percent of the cases at the ALJ level. Many claims fail simply for procedural reasons, such as the employee not filing a claim within the short statute of limitations period of 90 days from the date of the alleged retaliation. OSHA and ALJs also deny a large number of claims, because the claimants cannot show that the protected activity was a contributing factor in the adverse employment decision. In short, while every case is unique and stands or falls on its own merits,

BEFORE THE WHISTLE BLOWS

- Employers have a track record of success when facing whistle-blower claims under the Sarbanes-Oxley Act.
- However, a claim can be the beginning of much more serious problems such as a suit, a Securities and Exchange Commission investigation and a securities fraud class action.
- Employers' responses to whistle-blower claims should begin long before an employee files the first complaint.



employers have a track record of success at these administrative levels.

But caution is required. Unsuccessful SOX whistle-blower claims can still cause a lot of collateral damage. The fact that SOX whistle-blower claimants typically lose does not mean that employers should treat whistle-blower claims lightly. To the contrary, even if successful at the OSHA and ALJ level, whistle-blowers may represent just the tip of the iceberg of claims, and headaches.

Regardless of the ultimate result of the OSHA investigation, employers will have to defend against whistle-blowers' allegations. That immediately translates into attorneys' fees, plus the time and effort required in responding to claimants' contentions. Because time represents many executives' most valued asset, they will feel the impact in more than just dollars and cents.

One significant feature of the enforcement of SOX whistle-blower protections is that the SEC receives the complaint. The underlying facts behind the complaint may well have an impact on the SEC's response, with the more questionable whistle-blower claims receiving less interest. However, this represents another layer of damage control and increased expense, not to mention potentially damaging publicity.

Most Department of Labor investigations of whistle-blowers' claims do not conclude within 180 days, which opens the real possibility of litigation in federal court. Litigation not only continues the time and expense of defending against the allegations, but it also brings with it discovery. Discovery, in addition to being costly, could reveal some previously unknown details of corporate dealings that may be damaging. If there is some evidence of questionable conduct underlying the whistle-blower's claim, a wrongful-termination claim could quickly snowball into a class action securities suit. If the SEC had not previously taken a second look at the company, a securities suit may prompt it to act.

All of a sudden, instead of easily prevailing before OSHA on a SOX retaliation claim, a company could find itself defending a whistle-blower suit, SEC investigation and securities fraud class action.

What to Do?

For all these reasons, even if an employer prevails before OSHA in the battle of a SOX whistle-blower claim, it may end up losing the war. With the potential of an SEC investigation, suits or, at a minimum, significant attorneys' fees, what should a business do?

A company's response to a whistle-blower complaint should have begun long before the whistle-blower even knows he or she has information to share. First, SOX and securities regulations require companies to establish procedures to receive, retain and handle complaints regarding accounting, internal accounting controls or auditing matters. Regulations also require procedures that allow employees confidentially and anonymously to submit concerns regarding questionable accounting or auditing matters.

These policies should contain provisions explicitly stating that whistle-blowers will not be the subject of retaliation and provide avenues of redress if they think they are being subjected to negative employment decisions. Employers should not simply pay lip service to these requirements; they should embrace them.

With respect to the actual whistle-blowers themselves, SOX requires an audit committee's investigation. The audit committee should take each whistle-blower complaint seriously. The procedures for handling these claims should have teeth and not just be window dressing for auditors. The key is to never get to the OSHA level. If there are serious and accurate allegations of securities fraud, the whistle-blower will give the company a head start to investigate the claims ahead of any SEC inquiry or securities suit.

While the record shows that not all SOX whistle-blower retaliation claims are meritorious, most possess the potential to be a costly, time-consuming exercise that could lead to more than just an opinion from OSHA or an ALJ. Prevention and a proactive approach to managing SOX claims are the keys. While it is impossible to insulate against all claims, by having the right procedures in place ahead of time and treating each SOX claim with care, companies should be able to limit their exposure. ELA

Walker M. Duke is an associate with Gibson, McClure, Wallace & Daniels in Dallas, where he focuses his practice on commercial litigation. His e-mail address is wduke@gmwd.com. Wade L. McClure is a partner in Gibson, McClure, Wallace & Daniels in Dallas. His focus is business litigation and corporate governance. His e-mail address is wmcclure@gmwd.com.