

In This Issue:

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In a matter of first impression, the Fourth Circuit Court of Appeals held that Sarbanes-Oxley whistleblower claims initially filed with the Department of Labor can be subject to *de novo* review in federal district court if the Department of Labor does not issue a final decision within 180 days of the filing of the complaint. The practical impact of this ruling is the possibility that employers will be faced with defending SOX claims on two fronts.

Fourth Circuit Rules that SOX Whistleblowers May Have Two Bites at the Apple

By Gregory C. Keating and Jennifer L. Mora

In a significant case of first impression decided December 31, 2009, the United States Court of Appeals for the Fourth Circuit held that an individual has the right to *de novo* review in federal district court after losing in a hearing before an administrative law judge from the federal Occupational Safety and Health Administration (OSHA). In *Stone v. Instrumentation Laboratory Co.*, (No. 08-2196, Dec.), the Fourth Circuit, relying solely on the plain language of the Sarbanes-Oxley Act, rejected any claim that allowing an individual with a whistleblower complaint to start anew in federal district court would lead to the “absurd” result of duplicative litigation. Rather, the Fourth Circuit noted that by allowing whistleblowers to request *de novo* review in federal district court if their complaint languished at OSHA, “Congress unquestionably chose an aggressive time-table for resolving whistleblower claims and reasonably created a cause of action in an alternative forum should the Department of Labor (DOL) fail to comply with such a schedule.” The result for employers is the possibility of fighting an employee’s whistleblower claim under the Sarbanes-Oxley Act on two fronts, before the DOL and in federal courts.

Background

David Stone was employed by Instrumentation Laboratory Company (ILC) as the Director of National Accounts. ILC is in the business of developing, manufacturing, and distributing critical care and diagnostic instruments, as well as other related products and services, for use primarily in hospital laboratories. Upon assuming his role as Director of National Accounts, Stone learned that one of his superiors at ILC was not accurately tracking, reporting, and paying certain administrative fees to Group Purchasing Organizations (GPOs), which were strategic affiliations of hospitals that concentrate buying power in order to negotiate lower prices. ILC was required to pay the GPOs administrative fees of 3% of sales revenue generated from purchases. Stone discovered that his superior’s omissions resulted in a multi-year cumulative liability of at least half a million dollars and threatened ILC’s ability to sell products to most

of its customers. According to Stone, this failure to maintain adequate internal controls and track administrative fees resulted in ILC “misrepresenting its financial condition to shareholders.”

For approximately seven months, Stone repeatedly voiced his concerns about deficient internal controls and unpaid GPO fees directly to his superior and two other ILC managers. However, Stone’s efforts were met with resistance and outright refusals to correct the problems. Stone contended that ILC and the managers to whom he reported his concerns retaliated against him and ultimately terminated his employment.

The Administrative Proceedings Before OSHA and Their Dismissal

In accordance with the Sarbanes-Oxley Act, Stone filed a retaliation claim with OSHA on June 19, 2006. On January 3, 2007, more than 180 days after Stone’s claim was filed, OSHA issued its preliminary findings. Consistent with the governing regulations, Stone filed a timely objection to OSHA’s findings and requested a hearing before an administrative law judge (ALJ). On March 1, 2007, ILC filed a motion for summary decision before the ALJ. In response, Stone moved to delay consideration of the motion for the purpose of conducting discovery. The ALJ denied Stone’s motion and granted ILC’s motion for summary decision on September 6, 2007. Next, Stone successfully petitioned the Administrative Review Board (ARB) for review of the ALJ’s order. On October 1, 2007, the ARB established a briefing schedule, which was modified after Stone requested that the schedule be changed.

On November 8, 2007, more than one month before Stone’s opening brief was due to the ARB under the modified briefing schedule, Stone filed a notice with the ARB stating his intention to file a *de novo* action in federal district court. The ARB issued an order to show cause why Stone’s administrative appeal of the ALJ’s order should not be dismissed. After ILC failed to respond, and after receiving Stone’s notice that he had filed a *de novo* action in federal court, the ARB dismissed Stone’s administrative appeal. The ARB based its dismissal on its belief that it no longer had jurisdiction over Stone’s complaint because he filed a lawsuit in federal court.

District Court Dismisses Stone’s Lawsuit on Preclusion Principles and Remands Complaint to the ARB

Stone filed his lawsuit requesting *de novo* review with the federal district court on November 26, 2007. Several months later, the district court granted ILC’s motion to dismiss, finding that the ALJ’s ruling dismissing Stone’s administrative complaint was a “final judgment on the merits” for purposes of collateral estoppel. The district court rejected Stone’s argument that he did not have a “full and fair opportunity to litigate his claims before the ALJ” and further concluded that allowing Stone to pursue relief in federal court would be “wasteful.” Accordingly, the district court ordered the Secretary of Labor to “re-institute proceedings” and further ordered the ARB to “rule on the merits of Stone’s appeal within 90 days.” Stone, however, declined to proceed further given his belief that the filing of his complaint in federal district court divested the ARB of jurisdiction. As a result, the ARB entered a final order of dismissal. After receiving a final judgment from the district court dismissing his whistleblower claim, Stone appealed.

Sarbanes-Oxley and the DOL’s Regulations

The Sarbanes-Oxley Act provides employees of publicly traded companies with whistleblower protection, and prohibits employers from terminating or otherwise retaliating against employees who report “potentially unlawful conduct” that has occurred or is in progress. In order for an employee or former employee to seek relief as a whistleblower, they must adhere to the procedure set forth in section 1514A(b), which states that an aggrieved individual may seek relief by: (1) filing a complaint with the Secretary of Labor; or (2) filing a *de novo* action in federal district court if the Secretary of Labor has not issued a final decision within 180 days of the filing of the complaint and there is no showing that the delay was due to the bad faith of the complainant.

The Department of Labor’s regulations set forth the procedure governing the administrative review process for whistleblower claims brought under Sarbanes-Oxley and the procedure for notifying the Secretary of Labor that a complainant intends to seek *de novo* review

in federal court. First, OSHA issues preliminary findings, which can be challenged before an ALJ. The ALJ's decision must contain findings, conclusions, and an order. The complainant can further challenge an adverse ALJ ruling by filing a petition for review with the ARB. If the ARB does not accept the petition for review, the ALJ's decision becomes the final decision of the Secretary of Labor. If, however, the ARB accepts a claimant's petition for review, the ALJ's decision is inoperative unless and until the ARB issues an order adopting the ALJ's decision. After the Secretary of Labor issues a final decision, the complainant can appeal directly to the circuit court of appeals. However, as occurred in Stone's case, if a "final" administrative decision has not been timely issued within 180 days of the filing of the complaint and the complainant desires *de novo* review in federal district court, the complainant must file a written notice of intent to file a lawsuit in federal court.

Court of Appeals Concludes DOL's Failure to Issue Final Decision Within 180 Days of a Complaint Opens Door for a Lawsuit in Federal Court

It is against this procedural and factual backdrop that the Fourth Circuit had little difficulty in concluding that the plain language of the Sarbanes-Oxley Act permitted Stone to seek *de novo* review in federal district court and that the district court not only incorrectly deferred to the ARB's decision but also incorrectly remanded Stone's case back to the ARB for a final determination on the merits. Indeed, the plain language of the Sarbanes-Oxley Act, which the Fourth Circuit found to be plain and unambiguous, expressly states that a complainant may bring "an action at law or equity for *de novo* review in the appropriate district court" if the Secretary of Labor has not issued a final decision within 180 days after the filing of the administrative complaint. According to the Fourth Circuit: "[t]he text of the statute is clear – if the DOL has not reached a final decision within the time period established by Congress, a complainant has the *statutory right* not merely to undefined relief in another forum, but to '*de novo* review' in federal district court." The court further added that the individual's "right to pursue such relief is not circumscribed in any manner by the statute."

In Stone's case, the Secretary of Labor did not issue a final decision within 180 days after the filing of his complaint with OSHA. Moreover, Stone correctly followed the procedures for notifying the Secretary of Labor of his intent to seek *de novo* review in federal court. As a result, Stone was statutorily entitled to *de novo* review, or a "fresh look," in federal court. The Fourth Circuit rejected the district court's attempt at deferring to the ARB's decision by claiming that Stone had "a full and fair opportunity to litigate his claims before an ALJ" and that it would be "wasteful" to relitigate his claims in federal court. In so doing, the Fourth Circuit noted that the plain language of the Sarbanes-Oxley Act does not allow a federal court to give deference to any prior administrative rulings. Rather, the federal court is *required* to review the matter *de novo*. Although the Fourth Circuit stated that deferring to the ARB's decision may be more efficient, it was compelled to reject such a conclusion as being "in direct conflict with the unambiguous language" of the Sarbanes-Oxley Act.

The Fourth Circuit then considered ILC's argument that the court's literal interpretation of the statute would lead to an "absurd" result. At the outset, the court acknowledged that allowing *de novo* review if an ALJ has already issued a ruling may result in "duplication of efforts." Moreover, the Secretary of Labor opined in its comments to the regulations implementing the complaint mechanism set forth in the Sarbanes-Oxley Act that "it would be a waste of the resources of the parties, the Department, and the courts for complainants to pursue duplicative litigation" and that the Secretary of Labor anticipated "that Federal courts will apply [preclusion] principles if a complainant brings a new action in Federal court following extensive litigation before the [DOL] that has resulted in a decision by an [ALJ] or the Secretary." The Fourth Circuit found the Secretary of Labor's predictions unpersuasive given Congress's choice "of an aggressive time-table for resolving whistleblower claims" and its decision to allow a complainant to file a lawsuit in a different forum if the Department of Labor failed to meet the 180-day schedule. According to the court, "[a] natural result of the aggressive timeframe is that efforts will be duplicated when the DOL engages in a thorough, yet administratively non-'final,' process that fails to resolve the administrative case within the prescribed timeframe." Because of the clear and unambiguous language in the Sarbanes-Oxley Act allowing Stone to seek *de novo* review in federal court after the inability to obtain finality within 180 days, the court concluded that the Secretary of Labor and the courts could not "engage in creative interpretation of the statute to avoid duplication of efforts, *even if the goal for doing so is laudable.*"

Implications for Employers

The legal implications for employers are clear. If an employee or former employee files a complaint with OSHA alleging a whistleblower claim under Sarbanes-Oxley, the employer will be forced to defend the allegation by submitting evidence to OSHA for a preliminary finding, proceeding to a hearing with an ALJ, and possibly being subject to a third level of administrative review at the ARB. If this process is not completed within 180 days, or if the process is completed but a final decision is not issued within 180 days of the filing of the complaint, the employee or former employee has an absolute right to file a lawsuit in federal district court for a “fresh look” at the claim. This will necessarily result in the type of duplicative litigation that courts have sought to prevent for decades. Unfortunately, it is unclear whether OSHA will speed up its enforcement and investigative efforts upon receipt of a Sarbanes-Oxley claim or will delay in the investigation armed with the knowledge that after 180 days, the case will end up in federal court. Either way, employers must be aware of the possibility of fighting the Sarbanes-Oxley battle on two fronts both before a federal agency and in the federal courts.

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