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ARB Ruling Takes Broad View of Scope of Protected Activity Under SOX

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In the latest sign that the Department of Labor (DOL) is taking a harder line against employers defending whistleblower claims under the Sarbanes-Oxley Act (SOX), the DOL's Administrative Review Board (ARB) recently ruled in *Sylvester et al. v. Parexel International LLC*, ARB No. 07-123 (May 25, 2011), that (1) SOX complaints filed with the Occupational Safety and Health Administration (OSHA) are not subject to the pleading standards under *Twombly* and *Iqbal*; (2) SOX-protected conduct is not limited to complaints relating to fraud against shareholders; (3) the reported misconduct need not "definitely and specifically" relate to one of the laws enumerated under SOX Section 806—a reasonable belief of a violation is sufficient; and (4) a complainant can engage in protected activity under SOX Section 806 even if he or she fails to allege, prove, or approximate the specific elements of fraud, such as materiality, scienter, reliance, economic loss, or loss causation.

ARB Announces Standards Applicable to SOX-Protected Activity

Parexel is a publicly traded company that tests drugs for pharmaceutical companies and other clients. Complainant Sylvester was a Case Report Forms Department Manager who was responsible for the accurate reporting of clinical study data pursuant to the FDA's Good Clinical Practice standards. Complainant Neuschafer was a Clinical Research Nurse responsible for reporting accurate clinical data. The complainants alleged that one or both of them had reported two instances of the false reporting of clinical data to a manager and a supervisor, but that nothing was done about their complaints. They also alleged that Parexel declined to investigate the alleged conduct because doing so would have adversely affected its profits from the clinical studies, thus adversely impacting the value of its stock. Finally, they alleged that to the best of their knowledge, the false data had never been corrected and was reported as accurate by Parexel in communication through the U.S. mail and by wire communications such as the Internet. The complainants alleged that they were subject to adverse employment decisions after these reports, including but not limited to termination of employment.

The complainants filed SOX whistleblower claims with OSHA. OSHA dismissed both complaints. On appeal, the Administrative Law Judge (ALJ) granted Parexel's motion to dismiss the SOX complaints on the grounds that the complainants failed to adequately plead activity protected under SOX Section 806.

Hearing the appeal en banc, the ARB ruled that the ALJ had committed reversible error on several grounds. *See Sylvester*, ARB No. 07-123.

Pleading Standard for SOX Complaints Before OSHA

First, the ARB held that the pleading standards set forth by the U.S. Supreme Court in *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007), and *Ashcroft v. Iqbal*, 129 S. Ct. 1937 (2009), do not apply to SOX claims initiated with OSHA. SOX complaints are governed by regulations that do not require any "particular form of complaint," but require that the complaint be in writing and contain "a full statement of the acts and omissions, with pertinent dates, which are believed to constitute the violations." 29 C.F.R. § 1980.103(b). OSHA then has a duty, if appropriate, to interview the complainant and supplement a complaint that lacks a prima facie claim. 29 C.F.R. § 1980.104(b)(1). If the complaint, as supplemented, alleges a prima facie SOX claim, OSHA initiates an investigation.

The ARB ruled that the pleading standards in *Twombly* and *Iqbal* are inappropriate for SOX complaints and the procedures noted above for supplementing those complaints even if they are deficient as originally filed. Further, the ARB stated that "SOX claims are rarely suited for Rule 12 dismissals," and that ALJs should freely grant parties the opportunity to amend their initial filings to provide more information about their complaint before the complaint is dismissed.

SOX-Protected Conduct: Reasonable Belief Standard

The ARB ruled that a SOX complainant need only express a "reasonable belief" of a violation to establish that he or she engaged in protected activity. The reasonable belief standard requires an examination of the subjective and objective reasonableness of a complainant's beliefs. The objective standard "is evaluated based on the knowledge available to a reasonable person in the same factual circumstances with the same training and experience as the aggrieved employee." *Sylvester*, ARB No. 07-123 at 14 (quoting *Harp v. Charter Commc'ns*, 558 F.3d 722, 723 (7th Cir. 2009)).

The ARB ruled that the complainant need not actually convey the reasonableness of his or her beliefs to the employer, and that the issue of reasonable belief often involves factual issues that "cannot be decided in the absence of an adjudicatory hearing." *Sylvester*, ARB No. 07-123 at 15. The ARB ruled that the ALJ erred by dismissing the complaints without examining the facts relating to the reasonableness of the complainants' beliefs.

The ARB further ruled that the complainant need not complain about an actual violation of the law. A reasonable, but mistaken, belief that a violation of one of the laws in Section 806 has occurred will suffice.

SOX-Protected Conduct: "Definite and Specific" Standard

The ARB also held that the ALJ erred by applying the "definite and specific" evidentiary standard to the complainants' reports. In *Platone v. FLYi, Inc.*, ARB No. 04-154 (September 29, 2006), the ARB imposed a requirement, drawn from case law under the Energy Reorganization Act, that a SOX complainant must establish that the activity or conduct for which protection is claimed "definitely and specifically" relates to one or more of the laws enumerated under Section 806. As noted by the ARB in *Sylvester*, this standard has been followed in a number of other ARB decisions, and several circuit court decisions. The ARB in *Sylvester*, however, ruled that the standard is whether the complainant provided information that he or she reasonably believed related to a violation of one of the laws listed under Section 806, and that it was "error for the ALJ to dismiss the complaints in this case for failure to meet a heightened evidentiary standard espoused in case law but absent from SOX itself." *Sylvester*, ARB No. 07-123 at 18–19.

In light of the prior circuit court decisions referencing the "definite and specific" standard, it is unclear whether circuit courts in the future will defer to the change in position of the ARB with respect to this standard.

In addition, as recognized by the concurring and dissenting opinion of Deputy Chief Administrative Appeals Judge Brown, the majority opinion in *Sylvester* does not abrogate the requirement, previously recognized by the ARB and the Fourth Circuit, that in reporting misconduct, an employee "must identify the specific conduct that the employee believes to be illegal." *Id.* at 41 (Brown, J., concurring and dissenting) (quoting *Welch v. Chao*, 536 F.3d 269, 276 (4th Cir. 2008)).

SOX-Protected Conduct: Alleging Fraud

The ARB ruled that SOX-protected conduct extends to reporting a reasonable belief of a violation of any of the laws enumerated under Section 806—not only fraud against shareholders. The laws listed in Section 806 are mail fraud (18 U.S.C. § 1341); wire, TV, and radio fraud (§ 1343); bank fraud (§ 1344); securities fraud (§ 1348); any rule or regulation of the Securities and Exchange Commission (SEC); or any violation of federal law relating to fraud against shareholders. The ARB noted that only the last category of unlawful conduct refers to fraud against shareholders, and that "[o]n their face, mail fraud, fraud by wire, radio, or television, and bank fraud are not limited to frauds against shareholders." *Sylvester*, ARB No. 07-123 at 20. In fact, the ARB noted that a violation of "any rule or regulation" of the SEC may be "completely devoid of any type of fraud." *Id.*

Finally, the ARB ruled that:

> [A] complainant can have an objectively reasonable belief of a violation of the laws in Section 806, i.e., engage in protected activity under Section 806, even if the complainant fails to allege, prove, or approximate specific elements of fraud, which would be required under a fraud claim against a defrauder directly. In other words, a complainant can engage in protected activity under Section 806 even if he or she fails to allege or prove materiality, scienter, reliance, economic loss, or loss causation.

Id. at 22. The ARB reasoned that SOX was designed to prevent potential fraud at its earliest stages. The ARB noted, however, that a complainant's concerns could involve "such a trivial matter that he or she did not engage in protected activity under Section 806." *Id.*

Conclusion

Applying these standards to the allegations by the complainants in *Sylvester*, the ARB ruled that the complainants had satisfied the pleading standard for alleging SOX-protected conduct. According to the ARB, the complainants alleged that they reported fraudulent activities to a manager or supervisor, described how the allegedly fraudulent activities related to the financial status of the company, stated that those activities related to one or more of the laws listed in SOX Section 806 (with a focus on mail and wire fraud), alleged that their employer had knowledge of their protected activity, and alleged that they were subjected to adverse employment actions in retaliation for such protected activity. The ARB, therefore, reversed the ALJ's dismissal and reinstated the complaints.

Impact of *Sylvester* on SOX-Covered Companies

In light of this ruling, a broader array of conduct may be considered protected activity under SOX than might have been considered protected before *Sylvester*. The result of this decision likely will be that more employees will be able to claim that they engaged in SOX-protected conduct, more SOX whistleblower claims will be filed, and fewer claims will be dismissed on a prehearing motion.

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