ALERTS AND UPDATES

Sarbanes-Oxley Whistleblower Protections Apply to Non-Tangible Employment Action

November 2, 2011

The U.S. Department of Labor Administrative Review Board (ARB) has concluded in *Menendez v. Halliburton, Inc.*, that an employer's release of a whistleblower's identity to other employees violated the whistleblower's right to confidentiality, which by itself constituted an adverse action against the whistleblower and thus violated the anti-retaliation provisions of the Sarbanes-Oxley Act of 2002 (SOX).[1] The ARB determined that whistleblowers are protected against unfavorable employment action that is "more than trivial" and "non-tangible,"[2] even when the whistleblower's reasonable belief was ultimately mistaken.[3]

Background. On May 8, 2006, Anthony Menendez brought a claim against his employer, Halliburton, Inc., under Section 806[4] of SOX, alleging that he suffered retaliatory adverse action as a result of his report to the U.S. Securities and Exchange Commission (SEC) and his employer's Audit Committee of perceived defective accounting practices.[5]

In early 2005, Menendez filed a confidential complaint with the SEC regarding Halliburton's revenue recognition practices. The SEC subsequently notified Halliburton of the complaint. Menendez later notified Halliburton's Audit Committee of the concerns included in his complaint, believing his identity would be kept confidential in accordance with Halliburton's policy.[6] Subsequently, Halliburton's general counsel transmitted an email to relevant Halliburton employees mandating document retention to comply with the SEC investigation, stating that the investigation was based on Menendez's complaints and divulging his identity. As a result, Menendez was shunned by colleagues,[7] relieved of responsibilities and assigned a new immediate supervisor ranking lower than his previous supervisor. In September 2006, the SEC formally notified Halliburton that no enforcement action was being recommended.[8]

ARB's Analysis. According to the ARB, a successful claim under Section 806 must satisfy a three–part test: (i) the employee engaged in SOX–protected activity;[9] (ii) the employee suffered an adverse action;[10] and (iii) the employee's action was a contributing factor in the adverse action.[11] In this regard, the ARB determined that exercising his whistleblower rights under SOX was a "protected activity"; and as a result of Halliburton's divulging his name and thereby breaching his confidentiality, Halliburton caused Menendez to suffer an "adverse action." As to the third factor, the ARB requested the Administrative Law Judge (ALJ) to determine whether Menendez's protected activity was a contributing factor to his adverse action.[12]

In developing its standard, the ARB defined adverse actions as "unfavorable employment actions that are more than trivial, either as a single event or in combination with other deliberate employer actions. . . ."[13] The ARB determined that an adverse action is one that would discourage a reasonable employee from taking protected action and is "not necessarily retaliatory or illegal."[14]

The ARB concluded that under SOX Section 806, the employee needed to demonstrate only that such activity would deter a reasonable person from engaging in protected activity. The ARB continued by noting that the employee also asserted that this action breached his right to confidentiality, in violation of SOX Section 301, which requires audit committees of public companies to develop procedures to handle anonymous complaints from employees. Construing Section 301's requirement

that employers establish confidential channels of communication for their employees to afford consistency with Section 806's anti–retaliation provisions, the ARB determined that Section 806 provides whistleblower protection to employees who make use of such channels.[15] Accordingly, the ARB agreed with Menendez that the right to confidentiality that Section 301 affords effectively establishes a "term and condition" of employment within the meaning of Section 806's whistleblower protection provision, and that the exposure of his identity in connection with his complaint constituted a violation of that employment term and condition.[16]

The ARB concluded that "a reasonable employee in Menendez's position would be deterred from filing a confidential disclosure regarding misconduct if there existed the prospect that his identity would be revealed to the very people implicated in the alleged misconduct."[17]

For Further Information

If you would like assistance in reviewing your whistleblower policy and the manner in which you conduct investigations into whistleblower complaints or have any questions about the *Menendez v. Halliburton* decision, please contact Laurence Lese, Richard Silfen or Joel Ephross; one of the members of the Securities Law Practice Group; one of the members of the Employment, Labor, Benefits and Immigration Practice Group; or the lawyer in the firm with whom you are regularly in contact.

Notes

1. *Menendez v. Halliburton, Inc.*, ARB Nos. 09–002–003, ALJ No. 2007–SOX–005 (ARB Sept. 13, 2011).

2. The ARB concluded that, irrespective of the breach of his confidentiality, Menendez in this case did not suffer any tangible employment consequences. In this regard, the ARB stated: "SOX Section 806's plain language states that no company 'may discharge, demote, suspend, threaten, harass, or in any other manner discriminate against an employee in the terms and conditions of employment.' By explicitly proscribing non-tangible activity, this language bespeaks a clear congressional intent to prohibit a very broad spectrum of adverse action against SOX whistleblowers." *Halliburton* at 15.

3. A basic principle of *Halliburton* is that a whistleblower is protected in his report of suspect accounting practices regardless of whether his allegation is ultimately correct, as long as his belief is reasonable.

4. Section 806 of SOX provides in pertinent part: "No company with a class of securities registered under section 12 of the Securities Exchange Act of 1934 . . . or that is required to file reports under section 15 of the Securities Exchange Act of 1934. . . or any officer, employee, contractor, subcontractor, or agent of such company, *may discharge, demote, suspend, threaten, harass, or in any other manner discriminate against an employee in the terms and conditions of employment because of any lawful act done by the employee* –

   (1) 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 section 1341, 1343, 1344, or 1348, any rule or regulation of the Securities and Exchange Commission, or any provision of Federal law relating to fraud against shareholders, when the information or assistance is provided to or the investigation is conducted by –

(A) a Federal regulatory or law enforcement agency;

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(C) a person with supervisory authority over the employee (or such other person working for the employer who has the authority to investigate, discover, or terminate misconduct)." (emphasis added).

5. On several occasions, Menendez raised the issue of accounting difficulties with his immediate supervisor, the chief accounting officer of Halliburton. Thereafter, Menendez submitted his claim to the SEC.

6. Halliburton's policy of confidentiality regarding whistleblower submissions to the Audit Committee provided, in relevant part: "Your confidentiality shall be maintained unless disclosure is: Required or advisable in connection with any governmental investigation or report; In the interests of the Company, consistent with the goals of the Company's Code of Business Conduct; Required or advisable in the Company's legal defense of the matter." *Halliburton* at n.27.

7. Indeed, the auditors at KPMG (Halliburton's auditors), with whom Menendez usually worked closely, also refused to interact with him. KPMG's legal counsel had instructed its employees not to interact with Menendez on accounting issues until the complaints were resolved.

8. The Audit Committee's investigation likewise concluded with no changes in the company's accounting practices. By letter dated October 17, 2006, Menendez submitted his resignation.

9. Halliburton did not dispute whether Menendez's actions were protected, but whether its action was adverse and whether Menendez's action caused its action. The ARB focused on "(1) [w]hether the ALJ erred in concluding Menendez engaged in activity protected under Section 806 of SOX; (2) [w]hether the ALJ erred in concluding that Menendez did not sustain adverse employment action within SOX Section 806 as a result of a breach of whistleblower confidentiality, isolation, investigation, removal of duties, demotion, and/or constructive discharge." *Halliburton* at 10. The ARB noted that "Furthermore, the reasonableness of Menendez's position is not necessarily undermined by the fact that the SEC ultimately approved Halliburton's accounting methods. An employee's non-frivolous complaint does not have to ultimately withstand internal or external review to merit Section 806 protection; such a standard would clearly undermine employee initiatives in bringing to light perceived misconduct. The Board has ruled that an employee's reasonable but mistaken belief in employer misconduct may constitute protected activity. Courts have also concluded, '[t]o encourage disclosure, Congress chose statutory language which ensures that "an employee's reasonable but mistaken belief that an employer engaged in conduct that constitutes a violation of one of the six enumerated categories is protected."'" *Halliburton* at 13–14.

10. The ALJ ruled that the confidentiality breach did not constitute an adverse action, finding that Halliburton did no more than identify the employee as having made allegations against the company "to a group of people who would have known it was him anyway," and thus, this action had "no practical impact" and, therefore, failed to constitute an adverse action under SOX. *Halliburton* at 21. The ARB disagreed and stated that once the employee's confidentiality was breached, evidence that he may have been identified in some other way was not only purely speculative, but also was immaterial to an analysis of adverse action. *Halliburton* at 25.

11. The ARB stated that "The statute is designed to address (and remedy) the effect of retaliation against whistleblowers, not the motivation of the employer. Proof of 'retaliatory motive' is not necessary to a determination of causation." *Halliburton* at 31.

12. The ARB noted that "If Menendez carries his burden of proving causation Halliburton can avoid liability by demonstrating by clear and convincing evidence that it would have taken the same adverse action in the absence of the protected activity." *Halliburton* at 11.

13. The ARB cited *Williams v. American Airlines*, ARB No. 09-018, ALJ No. 2007-AIR-004 (ARB Dec. 29, 2010), as the controlling standard, though it relied on *Burlington Northern & Santa Fe Railway Co. v. White*, 548 U.S. 53 (2006), as a persuasive reference. *Burlington* requires the employer's action be one measured by both severity and scope of the action. "Briefly, the Supreme Court's holding in *Burlington* addressed both the degree and scope of protection Title VII's anti-retaliation provision (Section 704) affords. With respect to the *degree* of actionable harm, the Court held that a Title VII plaintiff bringing a retaliation claim need only show the employer's challenged actions are 'materially adverse' or 'harmful to the point that they could well dissuade a reasonable worker from making or supporting a charge of discrimination.'" *Halliburton* at 16. The ARB continued: "The Supreme Court in *Burlington* also held that the *scope* of actionable harm under Title VII's anti-retaliation provision was broader than that of Title VII's anti–discrimination provision (Section 703). By contrasting the language of the anti-discrimination provision (Section 703) with the anti-retaliation provision (Section 704), the Court explained why the correct standard for claims under Title VII's anti-retaliation provision should not be limited to 'ultimate employment decisions' or 'tangible employment actions.'" *Halliburton* at 17.

14. According to the ARB, "An adverse action however is simply something unfavorable to an employee, not necessarily retaliatory or illegal." *Halliburton* at 29. The ARB found that "Nothing in Section 806 requires a showing of retaliatory intent." *Halliburton* at 31.

15. The ARB noted that "Rather than a limitation on what is to be considered an adverse action under Section 806, we are of the opinion that 'terms and conditions of employment' are not significant limiting words and should be construed broadly within the remedial context of Section 806. . . .Under Section 806, the language 'in the terms and conditions of employment' does not limit Section 806's intended protection to economic or employment-related actions." *Halliburton* at 18.

16. *Halliburton* at 24.

17. "Since the purpose of confidentiality is to encourage employees to come forward with the information about SOX violations, permitting an employer to indiscriminately expose the identity of an employee who presents information concerning questionable accounting or auditing matters would most assuredly chill whistleblower-protected activity, thereby defeating the very purpose the confidentiality provided by Section 301 was meant to achieve and, as a result, undermining the SOX's overall purpose and objectives. Employees who exercise their right under Section 301 to engage in confidential disclosures should be protected from employer retaliation under the Section 806's whistleblower provisions if the employer fails to provide the requisite confidentiality." *Halliburton* at 24.