

Employment

COMMENTARY

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Whistle-Blower Actions Under Sarbanes-Oxley

What Lessons Can Employers Learn From a Recent Federal Court Decision in Favor of Fired Employees?

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The Sarbanes-Oxley Act has created a multitude of questions for employers. Attorneys Allegra J. Lawrence-Hardy and Abigail J. Politzer of Sutherland, Asbill & Brennan explore recent developments in the law's expanding role in the workplace.

Federal courts and administrative law judges continue to wrestle with a variety of open questions concerning whistle-blower claims under the Sarbanes-Oxley Act, or SOX. A recent decision by a New York district court adds to several ongoing debates, including which actions by an employer may be considered retaliatory, when an employer may successfully defend on the ground that it would have taken the same personnel action even in the absence of any protected activity and whether reputational damages are available under SOX. *Mahony v. KeySpan Corp.*, 2007 WL 805813 (E.D.N.Y. Mar. 12, 2007). More generally, the *Mahony* decision serves as a stark reminder of the importance of maintaining proper documentation of personnel matters.

SOX's whistle-blower provisions cover employees of publicly traded companies. Specifically, these employees are protected from retaliation for providing information or otherwise assisting in an investigation concerning conduct the employee reasonably believes constitutes a violation of federal laws relating to fraud against shareholders. 18 U.S.C. § 1514(A)(a)(1). The employee bears the burden of demonstrating that the "protected" activity was a contributing factor to an unfavorable personnel action. 29 C.F.R. § 1980.104.

The employer can defeat a SOX claim by showing that it would have taken the same unfavorable personnel action in the absence of the protected behavior. 49 U.S.C. § 42121(b)(2)(B)(iv). Using this basic framework, federal courts are just beginning to parse out the reach of SOX's coverage and the scope of employers' defenses.

The Mahony Decision

Plaintiff Robert. J. Mahony worked as the director of strategic planning of the corporate affairs department at KeySpan Corp. until his termination in May 2003. In July 2001 KeySpan's director of accounting research, Frank Fanning, told Mahony he was concerned about several accounting and financial reporting errors.

In April 2002 Mahony told KeySpan's CEO, with whom he had a close relationship, that Fanning had scheduled a meeting with two KeySpan officers to discuss the accounting fraud allegations. At Mahony's recommendation, the CEO also attended the meeting. Two days after the meeting, David Manning, KeySpan's executive vice president of corporate affairs, received a document listing Fanning's allegations and indicated that the document be put in Mahony's personnel file. Manning ultimately ordered Mahony's subsequent termination.

Mahony said he began experiencing retaliation immediately after the April 2002 meeting. He said he was "isolated" within the company and his previously close relationship with KeySpan's CEO became "nonexistent." Mahony also claimed that he received dramatically different performance evaluations after the meeting.

According to Mahony, the unfavorable behavior continued until he was terminated 13 months later as part of a company-wide reduction in force.

Mahony filed a complaint under Sarbanes-Oxley with the U.S. Department of Labor. After 180 days had passed without a final decision, he withdrew his claim and filed suit in federal court. The court denied KeySpan's subsequent motion for summary judgment after finding material issues of fact and law as to whether Mahony had engaged in a protected activity under SOX and whether that alleged protected activity was a contributing factor in his termination. Further, the court found that KeySpan failed to prove as a matter of law that it would have terminated Mahony regardless of whether he had engaged in protected activity.

An Expansive View of SOX Retaliation

Thirteen months passed between Mahony's alleged protected activity and his termination — a period that enabled Fanning to communicate his accounting fraud concerns to KeySpan's CEO.

Federal courts have often granted summary judgment in cases brought under other employment discrimination statutes when a significant amount of time has passed between the alleged protected activity and the adverse employment action. See, e.g., *Haynes v. Level 3 Commc'ns LLC*, 456 F.3d 1215 (10th Cir. 2006) (seven-month period between protected activity and termination was too long to support inference of causation under Title VII, ADEA or ADA); *Lewis v. St. Cloud State Univ.*, 467 F.3d 1133 (8th Cir. 2006) (11-month period between protected activity and termination was too long to support inference of causation under Age Discrimination in Employment Act).

Of course, the passage of time alone is not determinative on the causation issue where there is other evidence to support an inference of a connection between the protected activity and the adverse employment action.

The *Mahony* court recognized this principle by holding as a matter of law that a 13-month gap between Mahony's protected activity and his termination did not preclude the court from finding a causal relationship between the two events in that case. Instead, the court was persuaded that Mahony's evidence of ongoing retaliation, *i.e.*, his isolation within the company, diminished relationship with the CEO and tainted performance reviews, could bridge the gap between his protected activity and termination more than one year later.

Even though Mahony's termination was enough to satisfy the requirement of showing that some adverse employment action was taken against him, the court nonetheless cited broad language from an early SOX decision in

discussing the parties' strained relationship: "An employment action is unfavorable if it is reasonably likely to deter employees from making protected disclosures. A complainant need not prove termination or suspension from the job or a reduction in salary or responsibilities." *Mahoney*, 2007 WL 805813, at * 6 (citing *Halloum v. Intel Corp.*, 2003-SOX-7, at *10 [A.L.J. Mar. 4, 2004]).

In *Halloum* the plaintiff had not been terminated but received a corrective-action plan that included "unattainable goals." *Halloum*, 2003-SOX-7, at *12. In light of the U.S. Supreme Court's decision in *Burlington Northern & Santa Fe Railway Co. v. White*, 126 S. Ct. 2405 (2006), which held that unlawful retaliation under Title VII does not require an economic injury such as a pay reduction, demotion or termination, some might argue that workplace snubs and isolation could become a new source of liability for employers.

Although *Mahony* does not actually establish this proposition, given that he was in fact terminated, employers would do well to assume that *any* unfavorable behavior toward a whistle-blower will face intense scrutiny.

Establishing That the Employer Would Have Taken the Same Action Absent the Protected Activity

The *Mahony* court's rejection of KeySpan's defense, namely that it would have taken the same personnel action in the absence of protected behavior, illustrates the extremely high evidentiary hurdle faced by employers defending SOX whistle-blower claims. If a SOX employee can prove a whistle-blower violation, the employer can still seek to defeat the claim by demonstrating with "clear and convincing evidence" that it would have taken the same unfavorable personnel action in the absence of protected behavior. 49 U.S.C. § 42121(b)(2)(B)(iv).

As the *Mahony* court noted, this standard is even more stringent than the "'already tough' standard that employers face in other employment discrimination cases." 2007 WL 805813, at * 7 (quoting *Collins v. Beazer Homes USA Inc.*, 334 F. Supp. 2d 1365 [N.D. Ga. 2004]).

Employers should take note of the high level of scrutiny the court applied to KeySpan's insistence that Mahony's termination was part of a company-wide reduction in force and would have occurred regardless of whether he had engaged in protected activity.

Because KeySpan failed to provide any information about the salaries, titles and seniority of the other employees terminated as part of the reduction in force, the court found that the company failed to show that "any employees that were similar to [Mahony] were also fired."

Due to the absence of such evidence, KeySpan was not entitled to summary judgment.

A Troublesome Piece of Evidence

The *Mahony* court's ultimate decision to deny summary judgment apparently was influenced by a document that inexplicably ended up in Mahony's personnel file. KeySpan had argued that Manning, KeySpan's executive vice president of corporate affairs and the decision-maker behind Mahony's termination, had no knowledge of Fanning's allegations concerning accounting fraud or Mahony's efforts to help Fanning gain access to the CEO.

This position was undermined by a document that Manning himself directed to Mahony's personnel file — a document containing a list of Fanning's allegations. The existence of this document undermined KeySpan's "no knowledge" defense and was a key factor in the denial of summary judgment. *Mahony* should serve as a stark reminder to employers of the importance of documentation.

Reputational Damages Under SOX

The *Mahony* court held that reputational damages are available under SOX.

Although there is a split of authority regarding the availability of non-pecuniary damages, such as injury to reputation and emotional distress, under SOX, the possibility that courts and administrative law judges may allow employees in SOX whistle-blower cases to recover monetary damages for non-pecuniary injuries, such as harm to one's reputation, could significantly raise the stakes in these cases.

In a recent case an administrative law judge tied monetary and reputational injuries together by awarding \$643,000 to a SOX plaintiff to compensate for "the diminution in expected earnings in all of her future jobs for as long as the reputational injury is expected to affect her prospects." *Hagman v. Wash. Mut. Bank*, 2005-SOX-73, at *40 (A.L.J. Dec. 19, 2006).

SOX provides that a prevailing employee "is entitled to all relief necessary to make the employee whole." 18 U.S.C. § 1514A(c).

The act further states that compensatory damages will include reinstatement, back pay and "compensation for any special damages sustained as a result of the discrimination, including litigation costs, expert-witness fees and reasonable attorney fees." *Id.* Historically, "special damages" have included only monetary damages, *i.e.*, damages

capable of being estimated in money and resulting from specific events such as loss of a contract or loss of specific customers. Special damages typically do not include non-pecuniary damages such as injury to reputation.

There is currently no consensus as to the availability of reputational damages under SOX. For example, *Hanna v. WCI Communities Inc.*, 348 F. Supp. 2d 1332 (S.D. Fla. 2004), held that reputational damages are available under SOX based on language that allows a prevailing employee to recover "all relief necessary to make the employee whole." In contrast, *Murray v. TXU Corp.*, 2005 WL 1356444, **2-3 (N.D. Tex. June 7, 2005), held that SOX does not provide for any type of non-pecuniary damages, including reputational damages. The *Mahony* court sided with *Hanna* on this issue.

Both *Hanna* and *Murray* noted that SOX's remedy provision is analogous to Title VII of the Civil Rights Act of 1964 as it read prior to the 1991 amendments.

Before Title VII was amended, a Title VII plaintiff could not be compensated for any of the "traditional harms associated with personal injury, such as pain and suffering, emotional distress, harm to reputation or other consequential damages." See *United States v. Burke*, 504 U.S. 229 (1992). After the 1991 amendments, however, Title VII specifically provided for compensatory damages for non-pecuniary losses. 42 U.S.C. § 1981a(b)(3).

Based on the traditional meaning of "special damages" and the analogy to the pre-amendment reading of Title VII, employers have a strong basis for arguing *against* damages for harm to reputation and other non-pecuniary damages. Nevertheless, most of the courts and administrative law judges that have addressed the issue have allowed successful SOX whistle-blower plaintiffs to recover both pecuniary and non-pecuniary damages, including reputational damages.

Employer Response

Although federal courts are just beginning to examine the breadth of whistle-blower claims under SOX, decisions like *Mahony* suggest that employers should arm themselves against potential SOX claims.

In addition to establishing procedures for reporting and investigating alleged corporate misconduct and implementing policies that prohibit retaliation against whistle-blowers, employers should review relevant policies and practices to ensure proper documentation of personnel matters.