

6th Circ. Hands A Landmark Victory To SOX Whistleblowers

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The Sixth Circuit's decision in *Rhinehimer v. U.S. Bancorp Investments Inc.* on May 28 broadly construing protected conduct under the Sarbanes-Oxley Act is a landmark win for SOX whistleblowers. It signals the demise of the onerous Platone standard of SOX-protected whistleblowing and indicates that the employee-favorable Sylvester standard is now the law of the land.

Judicially Created Loopholes Narrowing SOX Whistleblower Protection

Congress enacted SOX's whistleblower protection provision to combat a "corporate code of silence," a code that "discourage[d] employees from reporting fraudulent behavior not only to the proper authorities, such as the [FBI and U.S. Securities and Exchange Commission], but even internally." S. Rep. No. 107-146, at 4-5 (2002).



Jason Zuckerman

And to ensure that whistleblowers could serve as an effective early warning system for companies and prevent the next Enron Corp., Congress specifically provided that a whistleblower need only complain about conduct that he "reasonably believe[d]" violated one of the enumerated anti-fraud provisions in Section 806 (federal criminal prohibitions against bank fraud, mail fraud and wire fraud; any rule or regulation of the SEC; or any provision of federal law relating to fraud against shareholders). The plain meaning of the statute did not limit protected conduct to disclosures of actual shareholder fraud.

But, less than four years after the enactment of SOX, the U.S. Department of Labor's Administrative Review Board appointed by Secretary of Labor Elaine Chao significantly weakened Section 806 of SOX by imposing onerous burdens on whistleblowers that were contrary to the statute's plain meaning and intent.

In *Platone v. FLYi Inc.*, ARB Case No. 04-154 (Sept. 29, 2006), the ARB set forth the following requirements for SOX protected conduct:

- A SOX complainant's disclosure must "definitively and specifically" relate to one of the six enumerated categories found in 18 U.S.C. § 1514A.

- The disclosure must “approximate ... the basic elements” of the kind of fraud or violation alleged. For example, a disclosure about securities fraud must allege “a material misrepresentation (or omission), scienter, a connection with the purchase, or sale of a security, reliance, economic loss, and loss causation.”

Under Platone, SOX whistleblower protection was available only to employees who were familiar with the intricacies of federal securities law, and many cases were dismissed on summary judgment based on the failure to meet the onerous Platone standard.

And to compound Platone, some federal courts imposed an unduly high standard of objective reasonableness. For example, a Fifth Circuit decision concluded that an internal complaint about a company overstating gross profits in violation of SEC Staff Accounting Bulletin 101 did not qualify as protected conduct because the company’s financial reports had not yet been filed with the SEC. See *Allen v. Admin. Review Bd.*, 514 F.3d 468, 476 (5th Cir. 2008). The apparent logic of *Allen* is that the whistleblower should wait until shareholders have been defrauded before making an internal complaint. That reasoning, however, was contrary to the prophylactic purpose of Section 806.

ARB Rejects Platone and Adopts Broad Standard of SOX-Protected Conduct

In May 2011, an ARB appointed by Secretary of Labor Hilda Solis issued a monumental decision in *Sylvester v. Parexel International LLC*, ARB Case No. 07-123 (ARB May 25, 2011) expressly abrogating Platone and adopting the following broad construction of SOX-protected conduct:

- SOX complainants need only show that they reasonably believed the conduct complained about violated a relevant law. *Id.* at *14.
- An employee need not wait until misconduct occurs to make a protected disclosure, so long as the employee “reasonably believes that the violation is likely to happen.” *Id.* at *16.
- A complaint need not allege shareholder fraud to receive SOX’s protection. SOX was enacted to address “corporate fraud generally,” and so a reasonable belief that a violation of “any rule or regulation of the SEC” could lead to fraud is protected, even if the violation itself is not fraudulent. For example, SOX would protect a disclosure about deficient internal controls over financial reporting, even though there is no allegation of actual fraud. *Id.* at *19.
- The reasonable belief standard does not require complainants to have told management or the authorities why their beliefs are reasonable. *Id.* at *42.
- SOX complainants no longer need to show that their disclosures “definitively and specifically” relate to the relevant laws. *Id.* at *41.
- SOX complainants do not need to establish criminal fraud. Requiring a complainant to allege, prove or approximate the elements of fraud would be contrary to the whistleblower protection provision’s purpose. *Id.* at *47.

The ARB expressly found that the Platone standard was in conflict with “the plain language of the SOX whistleblower protection provision, which protects ‘all good faith and reasonable reporting of fraud.’” *Id.* at *14-15, 30 (quoting 148 Cong. Rec. S7418-01, S7420. When Sylvester was issued, the key battleground in SOX litigation in federal court became whether federal courts would continue deferring to the prior ARB’s Platone decision or would instead adopt the current ARB’s Sylvester decision.

Four years later, we now know the answer, and it is decisively positive for whistleblowers. In particular, the Second and Third Circuits and several district courts have adopted the ARB’s Sylvester standard of SOX-protected conduct, and no federal court has rejected the reasoning in Sylvester. See *Nielsen v. AECOM Tech. Corp.*, 762 F.3d 214, 220-21 (2d Cir. 2014) (granting Skidmore deference to Sylvester); *Wiest v. Lynch*, 710 F.3d 121 (3d Cir. 2013) (according Chevron deference to Sylvester); *Stewart v. Doral Fin. Corp.*, 997 F. Supp. 2d 129, 135-36 (D.P.R. 2014) (adopting the Sylvester standard).

Rhinehimer adopts the Sylvester standard and agrees with the ARB’s observation in Sylvester “that an interpretation demanding a rigidly segmented factual showing justifying the employee’s suspicion [referring to Platone] undermines this purpose and conflicts with the statutory design, which turns on employees’ reasonable belief rather than requiring them to ultimately substantiate their allegations.” In addition, Rhinehimer suggests that the issue of objective reasonableness is rarely amenable to summary disposition:

The issue of objective reasonableness should be decided as a matter of law only when no reasonable person could have believed that the facts [known to the employee] amounted to a violation” or otherwise justified the employee’s belief that illegal conduct was occurring. *Livingston v. Wyeth Inc.*, 520 F.3d 344, 361 (4th Cir. 2008) (Michael, J., dissenting) quoted in Sylvester. If, on the other hand, “reasonable minds could disagree about whether the employee’s belief was objectively reasonable, the issue cannot be decided as a matter of law.” *Id.*

Rhinehimer v. U.S. Bancorp Investments Inc., No. 13-6641 (6th Cir. May 28, 2015). Post-Rhinehimer, the focus of summary judgment motions in SOX cases will likely shift from protected conduct to causation.

Rhinehimer’s Protected Disclosure and Trial Win

At trial, Michael Rhinehimer prevailed on his claim that he was disciplined and fired in retaliation for alerting one of his superiors to unsuitable trades made by a co-worker to the detriment of an elderly client of U.S. Bancorp Investments (“USBII”).

Rhinehimer’s manager expressly admitted that he gave Rhinehimer a written warning for opposing the unsuitable trades because Rhinehimer’s complaint “prompted a [Financial Industry Regulatory Authority] investigation ... and anybody associated with this was really feeling the heat.” In addition, the manager warned Rhinehimer that if he were to sue the bank, his career in the city would be over. The bank placed Rhinehimer on a performance improvement plan requiring him to increase his revenue to \$40,000 per month, and shortly after placing him on the plan, the bank terminated his employment.

Rhinehimer prevailed at trial. On appeal, USBII argued that under Platone, Rhinehimer was required to establish facts from which a reasonable person could infer each of the elements of an unsuitability fraud claim, including the misrepresentation or omission of material facts, and that the broker acted with intent or reckless disregard for the client’s needs.

The Sixth Circuit held that the evidence was more than sufficient to sustain the jury's finding that Rhinehimer reasonably believed that certain trades constituted unsuitability fraud. And the court noted the "employee's reasonable belief is a simple factual question requiring no subset of findings that the employee had a justifiable belief as to each of the legally defined elements of the suspected fraud."

Rhinehimer is an important development for corporate whistleblower rights and protections in that it restores the original intent of SOX whistleblower protection. A whistleblower's reasonable belief is now assessed in a manner consistent with similar anti-retaliation statutes (i.e., the employee must subjectively believe that there is a violation, and the belief must be objectively reasonable).

SOX whistleblowers no longer need to jump through the additional hurdles imposed by Platone, and a wide range of disclosures about conduct that could lead to fraud (not just actual fraud) are protected. In conjunction with other favorable elements of Section 806, including: (1) the broad scope of actionable adverse actions recognized in the Fifth Circuit's recent ruling in *Halliburton Inc. v. ARB*, No. 13-60323 (5th Cir., Nov. 12, 2014); (2) the favorable "contributing factor" causation standard articulated by the ARB in *Powers v. Union Pacific Railroad Co.*, ARB No. 13-034, ALJ No. 2010-FRS-30 (ARB April 21, 2015); (3) the onerous same-decision defense for employers elucidated by the ARB in *Speegle v. Stone & Webster Construction*, ARB 13-074, 2005-ERA-006 (ARB Apr. 25, 2014); and (4) the wide range of remedies, including preliminary reinstatement and uncapped compensatory damages, the broad scope of protected conduct renders SOX a potent remedy to combat whistleblower retaliation.

—By Jason Zuckerman, Zuckerman Law

Jason Zuckerman is principal at Zuckerman Law. Zuckerman serves as co-chairman of the Whistleblower Subcommittee of the American Bar Association's Labor and Employment Section's Employee Rights and Responsibilities Committee.

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