

Schiff Hardin Case Alert — Recent Sarbanes-Oxley Decision

On January 28, 2004, in one of a handful of recent decisions interpreting the whistleblower provisions of the Sarbanes-Oxley Act of 2002 (the “Act”), an Administrative Law Judge (“ALJ”) ruled that a CFO who made reports of potential wrongdoing was terminated in retaliation for his protected activity under the statute, and ordered the CFO to be reinstated with back pay. See *Welch v. Cardinal Bankshares Corporation*, 2003-SOX-15 (Jan. 28, 2004). This decision and others like it have important implications for employers.

By way of background, Section 806 of the Act protects employee “whistleblowers” in publicly-traded companies who provide information to any number of designated authorities regarding conduct which the employee **reasonably believes** constitutes a violation of an SEC rule or other federal law designed to deter fraud against shareholders. 18 U.S.C. § 1514A.

In this case, the Company’s CFO reported certain questionable conduct that he believed he had a duty to report. The Company’s management called a subsequent meeting with its attorney and outside auditor to investigate the allegations, but the CFO refused to attend the meeting without his personal attorney. The Company suspended him that day and fired him the following week for refusing to attend the meeting. The CFO filed a complaint claiming that his termination was in retaliation for his protected activity under the Act. The Occupational Safety and Health Administration (“OSHA”), the federal agency designated to handle such complaints, denied the complaint. On appeal, the ALJ first determined that the employee had engaged in a number of activities that constitute “protected” activities under the Act, including: 1) informing an external auditor and the President/CEO and Chairman of the Board of Directors that he could not certify certain financial statements because the statements contained improper entries that could potentially mislead investors; 2) notifying an external auditor that he could not attest to the validity of the Company’s financial statements because the auditors had not given him sufficient access to the Company’s financial data; 3) reporting concerns that the Company’s internal controls were deficient because too many entries were made by individuals outside of the finance department; and (4) reporting to management his concerns that these problems could constitute fraudulent activity under the Act. After finding that the employee had engaged in protected activity, the ALJ went on to find that the protected activity was a **contributing factor** in the adverse employment action. In a lengthy decision, the ALJ ruled that the proximity in time between the employee’s protected activities and his termination (6-7 weeks) was sufficient to create an inference of unlawful discrimination. The ALJ rejected the Company’s stated reason for the firing — that the employee refused to attend the meeting-as a mere “pretext” for the retaliatory motive. In reaching his decision, the ALJ noted that whether the Company **actually violated** any federal fraud statute or regulation was not at issue; rather, the fact that the individual **reasonably believed** that his employer engaged in such conduct and reported this concern, and suffered an adverse employment action as a result, was sufficient to show that he was fired in retaliation for his protected activity under the statute.

The ALJ ordered reinstatement, back pay, and litigation costs and expenses, and gave the CFO 30 days in which to produce evidence upon which the back pay award and the litigation fees and expenses could be calculated. It is likely that the Company will appeal the adverse ruling to the Administrative Review Board.

If you have any questions regarding this ruling, please contact one of the members of Schiff Hardin’s Labor & Employment Group.

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