



Issue Date: 11 December 2017

CASE NO.: 2017-SOX-00049

IN THE MATTER OF

**NICK GRYGA,
Complainant**

v.

**HENKELS & MCCOY, INC.,
Respondent**

ORDER DISMISSING COMPLAINT AND CANCELLING HEARING

This case arises out of Section 806 of the Sarbanes-Oxley Act of 2002 (“SOX” or “the Act”), technically known as the Corporate and Criminal Fraud Accountability Act, P.L. 107-204, codified at 18 U.S.C. § 1514A, *et seq.*, and the employee protective provisions promulgated thereunder at 29 C.F.R. Part 1980. Under SOX, the Secretary of Labor is empowered to investigate and determine “whistleblower” complaints filed by employees of publicly-traded companies who are allegedly discharged, retaliated against, or otherwise discriminated against, with regard to their terms and conditions of employment, for providing information about fraud against company shareholders to supervisors, federal agencies, or members of Congress.

I. BACKGROUND

A. Procedural History

On June 20, 2017, Nick Gryga (Complainant) filed his original complaint with the Occupational Safety and Health Administration (OSHA) where he alleged retaliation by his former employer, Henkels & McCoy, Inc. (H&M or Respondent), after he expressed concerns of “construction fraud as well as collusion on work performed by Respondent for a publically traded company.” (Compl., p. 2).

On June 23, 2017, the Secretary of Labor found that because neither Complainant nor Respondent is covered under SOX, OSHA lacked jurisdiction to conduct any further investigation in this matter. On July 26, 2017, Complainant filed an objection to OSHA’s findings and a request for a hearing.

On October 18, 2017, Respondent filed a Motion to Dismiss for Failure to State a Claim because Respondent is not a covered employer and Complainant is not a covered employee

under the provision of SOX. Complainant filed a Response on November 2, 2017. Respondent filed a Reply on November 14, 2017.

B. The Parties Positions

Complainant does not dispute that Respondent is a private corporation and standing alone is not a covered employer under SOX. However, Complainant contends that as an employee of a “contractor” of a publicly-traded company or a company required to file reports under Section 15(d), he is therefore a covered employee under SOX. He cites 18 U.S.C. § 1514A and *Lawson v. FRM LLC*, 134 S.Ct. 1158 (2014) for support.

In his Reply Complainant summarizes his Complaint:

Respondent does not have to be a publically traded corporation in order for the whistleblower provisions of SOX to apply to its employees. Complainant reported and discovered construction fraud as well collusion on work performed by Respondent for a publically traded company. Essentially, Complainant discovered Respondent falsified payment applications, billed for unperformed work, engaged in subcontractor and client collusion, manipulated change orders, manipulated the schedule of values and contingency accounts, diverted lump-sum cost to time and material cost, diverted purchases, and overbilled for labor, equipment, tools and materials while fulfilling its role as a contractor for a publically traded company.

Respondent contends that based on the legal standards for determining coverage under SOX, Complainant’s claim does not encompass SOX’s employee whistleblower protections. Respondent argues that Complainant has failed to plead coverage sufficiently to avoid dismissal, as he complains about perceived construction fraud by Respondent against its publicly traded client, Spectra Energy. Respondent asserts SOX coverage does not apply where the alleged fraud was committed against the publicly traded company. SOX coverage does not apply without any alleged violation by or on behalf of a publicly traded company.

II. DISCUSSION

A. Standard for Motion to Dismiss

1. Rule 12(b)(1)

Respondent asserts a jurisdictional challenge and claims it not subject to the whistleblower provisions of SOX.

Although 29 C.F.R. Part 18, Rules of Practice and Procedure for Administrative Hearings, does not contain a section pertaining to such a motion to dismiss, 29 C.F.R. § 18.10(a) indicates that in situations not addressed in Part 18, the Federal Rules of Civil Procedure are applicable. In turn, Fed. R. Civ. P. 12(b)(1) addresses a motion to dismiss for lack of subject matter jurisdiction.

The ARB has discussed subject matter jurisdiction in SOX cases, notably in *Sylvester v. Parexel Int'l, LLC*, ARB Case No. 07-123, ALJ Case Nos. 2007-SOX-39 AND 2007-SOX-42, slip op. at 10-11 (ARB May 25, 2011):

Subject matter jurisdiction “refers to a tribunal’s power to hear a case.” *Morrison v. Nat’l Australian Bank*, 130 S. Ct. 2869, 2877 (2010) (citing *Union Pacific v. Bhd. Of Locomotive Eng’rs*, 130 S. Ct. 584, 596-97 (2009)). Subject matter jurisdiction “presents an issue quite separate from the question whether the allegations the plaintiff makes entitles him to relief,” *Morrison*, 130 S. Ct. at 2877, and thus under the whistleblower laws over which the Department of Labor has jurisdiction, should not be confused “with the wholly separate question whether [a complainant’s] actions might be covered as ‘protected activities.’” *Sasse v U.S. Dept. of Justice*, ARB No. 99-053, ALJ No. 1998- CAA-007, slip op. at 3 (ARB Aug. 31, 2000).

Similar to federal complaints based on federal question jurisdiction, the burden of establishing subject matter jurisdiction under Section 806 is not particularly onerous. *See, e.g., Turner/Ozanne v. Hyman/Power*, 111 F.3d 1312, 1317 (7th Cir. 1997); *Musson Theatrical*, 89 F.3d 1244, 1248 (6th Cir. 1996). As the Board explained in *Sasse*, the Department of Labor’s subject matter jurisdiction is invoked “when the parties are properly before it, the proceeding is of a kind or class which the court is authorized to adjudicate, and the claim set forth in the paper writing invoking the court’s action is not obviously frivolous.” *Sasse*, slip op. at 3 (quoting *West Coast Exploration Co. v. McKay*, 213 F.2d 582, 591 (D.C. Cir.), *cert. denied*, 347 U.S. 989 (1954)).

2. Rule 12(b)(6)

Under Rule 12(b)(6), a pleading may be subject to dismissal for either of two reasons: “First, the law simply may not afford relief on the basis of the facts alleged in the complaint. . . . Second, regardless of whether the plaintiff is entitled to relief, the pleadings may be so badly framed that the plaintiff is not entitled to a trial on the merits.” *Walker v. S. Cent. Bell Tel. Co.*, 904 F.2d 275, 277 (5th Cir. 1990). A complaint is deemed inadequate if it fails to “set forth sufficient information to outline the claim or permit inferences to be drawn that these elements exist.” *Gen. Star Indem. Co. v. Vesta Fire Ins. Corp.*, 173 F.3d 946, 950 (5th Cir. 1999). “[C]onclusory allegations of legal conclusions masquerading as factual conclusions will not suffice to prevent a motion to dismiss.” *Jones v. Alcoa, Inc.*, 339 F.3d 359, 362 (5th Cir. 2003) (quoting *Fernandez-Montez v. Allied Pilots Ass’n.*, 987 F.2d 278, 284 (5th Cir. 1993); *see also Jones v. Greninger*, 188 F.3d 322, 325 (5th Cir. 1999) (“Mere conclusory allegations of retaliation will not be enough to withstand a proper motion for dismissal of the claim.”)).

Unlike a motion for summary decision filed after discovery, a facial challenge offered to a complaint through Rule 12(b)(6) points to a missing essential element (no protected activity or adverse action) or a legal bar to the claim (e.g., sovereign immunity, lack of coverage over the respondent, the statute of limitations). *Evans v. U.S. Environmental Protection Agency*, ARB Case No. 08-059, ALJ Case No. 2008-CAA-3, slip op. at p. 10 (ARB July 31, 2012). A motion

to dismiss under Fed. R. Civ. P. 12(b)(6) tests the sufficiency of the complaint, not the merits of the case. *Id.*

Also, “Rule 12 motions challenging the sufficiency of the pleadings are highly disfavored by the SOX regulations and highly impractical under the Office of Administrative Law Judge (OALJ) rules.” *Sylvester*, ARB Case No. 07-123, slip op. at p. 13.

The court must address whether it has jurisdiction under Rule 12(b)(1) to hear Complainant’s SOX whistleblower action, as well as whether Complainant has stated a claim upon which relief can be granted under Rule 12(b)(6).

B. Jurisdiction under SOX

Section 806 of SOX, codified at 18 U.S.C. § 1514A, creates a private cause of action for employees of publicly-traded companies who are retaliated against for engaging in certain protected activity. Section 1514A(a) states, in relevant part:

(a) No company with a class of securities registered under section 12 of the Securities Exchange Act of 1934 (15 U.S.C. 78l), or that is required to file reports under section 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(d)), including any subsidiary or affiliate whose financial information is included in the consolidated financial statements of such company, or nationally recognized statistical rating organization (as defined in section 3(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78c), 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;

(B) any Member of Congress or any committee of Congress; or

(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); or

(2) to file, cause to be filed, testify, participate in, or otherwise assist in a proceeding filed or about to be filed (with any knowledge of the employer)

relating to an alleged 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.

18 U.S.C. § 1514A(a).

A **company** means “any company with a class of securities registered under section 12 of the Securities Exchange Act of 1934 (15 U.S.C. 78l) or any company required to file reports under section 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(d)) including any subsidiary or affiliate whose financial information is included in the consolidated financial statements of such company.” 29 C.F.R. § 1980.101(d).

A **covered person** means “any company, including any subsidiary or affiliate whose financial information is included in the consolidated financial statements of such company, ... or any officer, employee, contractor, subcontractor, or agent of such company...” 29 C.F.R. § 1980.101(f).

An **employee** is means “an individual presently or formerly working for a covered person, an individual applying to work for a covered person, or an individual whose employment could be affected by a covered person.” 29 C.F.R. § 1980.101(g).

Thus, the aggrieved employee’s first responsibility is to show that SOX covered his employer.

C. “Contractor” under SOX

1. Supreme Court finds that employees of a “contractor” for a publicly-traded mutual fund company may be covered by SOX’s whistleblower protections in Lawson v. FMR LLC

The Supreme Court recently ruled on whether 18 U.S.C. § 1514A protected employees of certain privately held companies who act as a “contractor” to publicly-traded companies. *Lawson v. FMR LLC*, 134 S.Ct. 1158, 188 L.Ed. 2d 158; 2014 U.S. LEXIS 1783 (Mar. 4, 2014).

In *Lawson*, two former employees (Lawson and Zang) of private companies that contracted to advise or manage Fidelity mutual funds brought separate actions against their former employers, alleging the employers unlawfully retaliated against them in violation of §1514A. *Lawson*, at 1161; *Gibney v. Evolution Marketing Research, LLC*, Case No. 14-1913, 25 F. Supp. 3d 74 (E.D. Pa. June 11, 2014). Lawson alleged that she was constructively discharged after raising concerns that certain cost accounting methodologies overstated the expenses associated with operating the mutual funds. *Lawson* at 1164; *Gibney* at 744-45. Zang alleged that he was fired in retaliation for raising concerns about inaccuracies in a draft for a registration statement to be filed with the Securities and Exchange Commission (“SEC”). *Id.* The defendant privately-held advisory and management firms contended that § 1514A was limited to protecting employees of a publicly-traded company from retaliation by the company’s private contractors or subcontractors.

The Supreme Court rejected the defendant's contention based on the text of 18 U.S.C. § 1514A, legislative history of the statute, and environment in which SOX was enacted. The Supreme Court held that "based on the text of § 1514A, the mischief to which Congress was responding, and earlier legislation Congress drew upon, [§ 1514A] shelters employees of private contractors and subcontractors [of publicly-traded companies], just as it shelters employees of the public company served by the contractors and subcontractors." *Lawson*, 134 S.Ct. at 1158; *Gibney* at 745. The Supreme Court noted that Congress borrowed §1514A's retaliation provision from the wording of the 2000 Wendell H. Ford Aviation Investment and Reform Act for the 21st Century (AIR 21), 49 U.S.C. § 42121, and that § 42121 has itself been read to protect the employees of contractors covered by that provision.

In finding that the *Lawson* plaintiffs were covered by SOX, the Supreme Court relied on SOX's overarching goal of preventing fraud by public companies, as well as the unusual structure of mutual funds, which generally have no employees and are managed instead by independent investment advisers. Congress' concern about contractor conduct stemmed from Enron, where law firms, accountants, contractors and the like were *complicit in*, if not integral to, the shareholder fraud and subsequent cover up Enron officers perpetrated. *Lawson*, 134 S.Ct. at 1169; *Gibney*, 25 at 746. (emphasis as in original). Congress recognized that outside professionals bear significant responsibility for the public companies with whom they contract. *Id.* The Supreme Court also concluded that if the *Lawson* plaintiffs were not covered by SOX, it could insulate the entire mutual fund industry from 18 § 1514A, and given the vital role mutual funds play in filing reports to the SEC, such insulation could not have been Congress' intent. *Lawson*, 134 S.Ct. at 1171-72. Hence, finding the that *Lawson* plaintiffs were covered by SOX furthered the statute's goals in preventing publicly-held companies from utilizing outside contractors or related and controlled companies to perpetuate fraud on outside shareholders.

2. Interpretation of *Lawson* and whistleblowing by "contractor" employees in *Gibney v. Evolution Marketing Research, LLC*

Gibney, an early post-*Lawson* decision from the United States District Court for the Eastern District of Pennsylvania, is instructive in this matter. *Gibney* asks whether the coverage that the plaintiff assumes in the complaint – that SOX protects the employees of private companies who contend that their employer overbilled a public company – goes beyond that approved by *Lawson* or contemplated by the SOX statute. *Gibney*, at 747.

In *Gibney*, the plaintiff brought a SOX whistleblower action against his former employer, Evolution Marketing Research ("Evolution"), for wrongful termination. The plaintiff alleged that the defendant's planned billing practices relating to a publicly-traded client (to which the defendant – a non-publicly traded company – was a contractor) were fraudulent.

The plaintiff contended that as an employee of a contractor to a publicly-traded company, and pursuant to the Supreme Court's decision in *Lawson*, his activities were protected under 18 U.S.C. § 1514A. The court reviewed the *Lawson* decision and found that it was clear that whistleblower protection extends to employees of private contractors or subcontractors for a public company. However, the *Gibney* court continued, the plaintiff was advocating "an impermissibly broad definition of SOX protection that was neither intended by Congress nor

contemplated by the Supreme Court in *Lawson*.” *Gibney*, at 747. First, the court noted that unlike *Lawson*, the instant case did not implicate the peculiar structure of the mutual fund industry, where there are no “employees.” *Id.*; *Lawson*, at 1171. Second, the complaint did not allege fraud by the publicly-traded company or that the defendant contractor abetted fraud by the publicly-traded company. Rather, the complaint alleged that there was fraud being committed *against* the publicly-traded company. Congress, the court noted, “was specifically concerned with preventing shareholder fraud either by the public company itself or *through* its contractors.” *Gibney*, at 747 (emphasis as in original). The district court stated that it does not believe SOX was intended to reach the type of scenario in *Gibney*, “where there are allegations of fraudulent conduct between two companies who are a party to a contract, and one of those companies just happens to be publicly-traded.” *Id.* Thus, the district court found that Evolution was not a covered respondent/defendant, and it granted Evolution’s motion to dismiss.

2. Interpretation of *Lawson* and whistleblowing by “contractor” employees in *Anthony v. NW Mut. Life Ins.*

Tronco Financial, a private company, was a contractor for and sold and marketed NW Mutual Funds. Plaintiff was an employee of Tronco. Her responsibilities included insuring compliance with the regulations and rules of NW Mutual Funds’ regulatory bodies and governmental agencies, including the SEC, FINRA, and state and federal securities laws. Plaintiff brought forward numerous compliance issues regarding the conduct of Tronco representatives.

In granting a motion to dismiss, the Court held that a private company’s fraudulent practices do not become subject to §1514A merely because that company incidentally has a contract with a public company. Plaintiff’s allegations failed to state a claim under § 1514A because she never alleged that she reported any wrongdoing committed by NW Mutual Funds or on their behalf. “§1514A is concerned with public company fraud, whether committed by the public company itself or through its contractors... The effect of these limitations is to restrict §1514A to situations where a contractor employee is functionally acting as an employee of a public company, and in that capacity, is a witness to fraud by the public company.” *Anthony v. NW Mut. Life Ins.*, 130 F.Supp. 3d 644 (N.D.N.Y. 2015).

D. Complainant Is Not a Covered Employee and H&M Is Not a Covered Respondent under SOX

I agree with Respondent regarding the Supreme Court’s reading of “contractor” in *Lawson*, and that this reading does not make SOX applicable to Complainant. As stated by Justice Ginsburg in *Lawson*, “Congress enacted §1514A [SOX] aiming to encourage whistleblowing by contractor employees who suspect *fraud involving the public companies with whom they work*,” and “SOX’s purpose is to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws.” (emphasis added). (*Lawson*, 134 S.Ct. at 1170, 1172). Also, Justice Ginsburg’s chief concern in granting SOX coverage to the *Lawson* plaintiffs was the effect on potentially insulating the entire mutual fund industry from § 1514A, “and given the vital role mutual funds play in filing reports to the SEC,”

“such insulation could not have been Congress’ intent.” (*Id.* at 1171). Similar concerns about insulating an entire industry are not present in this matter.

I also agree with the Eastern District of Pennsylvania’s emphasis on a narrow reading of contractor in *Gibney*, as opposed to “an impermissibly broad definition of SOX protection that was neither intended by Congress nor contemplated by the Supreme Court in *Lawson*.” *Gibney*, at 747. Also, the district court continued,

Nothing in the text of § 1514A or the *Lawson* decision suggests that SOX was intended to encompass every situation in which any party takes an action that has some attenuated, negative effect on the revenue of a publicly-traded company and, by extension decreases the value of a shareholder’s investment.

Id. at 748.

To extend SOX protection to a privately-held company such as Respondent based on these activities, which are two or three steps removed from potentially affecting a shareholder’s investment, would turn SOX into a general fraud statute, which it is not.

Through his attorney, Complainant has filed a well-written, detailed factual complaint. These facts are summarized in his Reply. Like the plaintiff in *Gibney*, Complainant is advocating “an impermissibly broad definition of SOX protection that was neither intended by Congress nor contemplated by the Supreme Court in *Lawson*.” *Gibney*, at 747. Like *Gibney*, the instant case did not implicate the peculiar structure of the mutual fund industry, where there are no employees. As in *Gibney*, the instant complaint does not allege fraud *by* the publicly-traded company or that Respondent abetted fraud *by* the publicly-traded company. Rather, the complaint alleges that there was fraud being committed *against* the publicly-traded company.

In summary, the Court finds that Complainant’s allegations do not state a claim under §1514A of SOX. Complainant has not alleged any fraud committed by Spectra Energy or that H&M abetted fraud by Spectra Energy.

III. ORDER

IT IS HEREBY ORDERED that Respondent's Motion to Dismiss for Failure to State a Claim is **GRANTED** and this matter is **DISMISSED** for lack of jurisdiction (Federal Rule of Civil Procedure 12(b)(1)) and/or failure to state a claim upon which relief can be granted (Federal Rule of Civil Procedure 12(b)(6)).

YOU ARE HEREBY NOTIFIED that a formal hearing on the merits of the above proceeding which was scheduled to commence at **9:00 a.m.** on **December 18, 2017**, in **Houston, Texas**, is **CANCELLED**.

SO ORDERED.

LARRY W. PRICE
ADMINISTRATIVE LAW JUDGE

NOTICE OF APPEAL RIGHTS: To appeal, you must file a Petition for Review ("Petition") with the Administrative Review Board ("Board") within fourteen (14) business days of the date of issuance of the administrative law judge's decision. The Board's address is: Administrative Review Board, U.S. Department of Labor, Suite S-5220, 200 Constitution Avenue, NW, Washington DC 20210. In addition to filing your Petition for Review with the Board at the foregoing address, an electronic copy of the Petition may be filed by e-mail with the Board, to the attention of the Clerk of the Board, at the following e-mail address: ARB-Correspondence@dol.gov.

Your Petition is considered filed on the date of its postmark, facsimile transmittal, or e-mail communication; but if you file it in person, by hand-delivery or other means, it is filed when the Board receives it. *See* 29 C.F.R. § 1980.110(a). Your Petition should identify the legal conclusions or orders to which you object. You may be found to have waived any objections you do not raise specifically. *See* 29 C.F.R. § 1980.110(a).

At the time you file the Petition with the Board, you must serve it on all parties as well as the Chief Administrative Law Judge, U.S. Department of Labor, Office of Administrative Law Judges, 800 K Street, NW, Suite 400-North, Washington, DC 20001-8002. You must also serve the Assistant Secretary, Occupational Safety and Health Administration and on the Associate Solicitor, Division of Fair Labor Standards, U.S. Department of Labor. *See* 29 C.F.R. § 1980.110(a).

You must file an original and four copies of the petition for review with the Board, together with one copy of this decision. In addition, within 30 calendar days of filing the petition for review

you must file with the Board: (1) an original and four copies of a supporting legal brief of points and authorities, not to exceed thirty double-spaced typed pages, and (2) an appendix (one copy only) consisting of relevant excerpts of the record of the proceedings from which the appeal is taken, upon which you rely in support of your petition for review.

Any response in opposition to a petition for review must be filed with the Board within 30 calendar days from the date of filing of the petitioning party's supporting legal brief of points and authorities. The response in opposition to the petition for review must include: (1) an original and four copies of the responding party's legal brief of points and authorities in opposition to the petition, not to exceed thirty double-spaced typed pages, and (2) an appendix (one copy only) consisting of relevant excerpts of the record of the proceedings from which appeal has been taken, upon which the responding party relies, unless the responding party expressly stipulates in writing to the adequacy of the appendix submitted by the petitioning party.

Upon receipt of a legal brief filed in opposition to a petition for review, the petitioning party may file a reply brief (original and four copies), not to exceed ten double-spaced typed pages, within such time period as may be ordered by the Board.

If no Petition is timely filed, the administrative law judge's decision becomes the final order of the Secretary of Labor pursuant to 29 C.F.R. §§ 1980.109(e) and 1980.110(b). Even if a Petition is timely filed, the administrative law judge's decision becomes the final order of the Secretary of Labor unless the Board issues an order within thirty (30) days of the date the Petition is filed notifying the parties that it has accepted the case for review. *See* 29 C.F.R. § 1980.110(b).