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Whistle-blowers may cause trouble; so does firing them

Did you know 10-year prison sentences may now be imposed on individual managers who retaliate against employees who report potential violations of federal criminal law to appropriate law enforcement officials?

This criminal penalty applies not only to publicly traded companies which might expected in the wak of Enron, WorldCom and so on — but also to privately held com panies where there is no possibility of fraud against public shareholders.

Besides creating this new crime, the Sarbanes-Oxley Act passed last year also exposes publicly traded companies to civil monetary damages if they retaliate against employees who blow the whistle on accounting or financial fraud.

How did this happen? And what can businesses do to reduce their exposure to civil and criminal whistle-blower penalties?

THE EVOLUTION OF THE PROTECTIONS

Until about 30 years ago, under the traditional rule of employment "at will," companies could fire whistle-blowing employees without fear of being sued.

Gradually, the law evolved on the state and federal levels to protect government employees who complained about waste of taxpayer funds and private-sector employees who voiced concerns about practices that presented risks to public health and safety.

Until Sarbanes-Oxley, however, most state and federal laws did not protect private-sector employees who voiced concerns about financial issues. Unlike government employees whose concerns involved taxpayer dollars, corporate financial issues were not perceived as affecting the public welfare.

But after Enron, WorldCom and other corporate scandals, Congress determined that fraud against shareholders was important enough to justify stiff new penalties, including criminal sanctions, in the hope of deterring financial abuses. It placed new requirements on public accounting firms, corporate officers and corporate audit committees, all of whom oversee preparation of a company's financials.

However, because the traditional mechanisms of "oversight" failed to prevent Enron et al., Congress also created "undersight" mechanisms to encourage employees, looking upward, to express their concerns about financial fraud.

The Securities and Exchange Commission recently issued a rule requiring publicly traded companies to disclose whether they have codes of ethics applicable to senior executives. Those codes must contain a whistle-blower component allowing employees to speak up when they think there's been an ethical violation.

NEW PROTECTIONS HIT HOME

Businesses in the Washington area must also be alert to new protections for whistle-blowers in Maryland and Virginia.

Last year, the highest court in Maryland ruled in Wholey v. Sears Roebuck that employees dismissed for reporting suspected legal violations to appropriate law enforcement officials may sue their employers for wrongful termination.

Also in 2002, the Virginia General Assembly enacted the Fraud Against Taxpayers Act, which protects whistle-blowers who report their employers' false claims for payment of funds from state or local government.

'YEAR OF THE WHISTLEBLOWER'

Concurrent with these legal developments, the media's portrayal of whistle-blowers has changed significantly. Whistle-blowers have been elevated to the stature of public heroes.

The Dec. 16 issue of Business Week chris-tened 2002 as the "Year of the Whistleblower." Just days later, the Dec. 30, issue of Time magazine declared three whistle-blowers — Sherron Watkins of Enron, Colleen Rowley of the FBI, and Cynthia Cooper of World-Com — "Persons of the Year."

Contrast this public adulation with the Sept. 4, 1995, cover story in Fortune magazine about Mark Whitacre, the former whistle-blowing executive of Archer Daniels Midland. The story skeptically asked "So who is this Mark Whitacre?" and noted he was alleged to have embezzled $2.5 million from his employer.

Somehow, between 1995 and 2003, it may have become socially acceptable to a whistle-blower.

POLICIES TO REDUCE EXPOSURE

Just as savvy employers have adopted policies forbidding sexual harassment, they should now consider policies forbidding retaliation against whistle-blowers. Those policies may help avoid whistle-blower litigation and negative publicity.

Policies against retaliation also may help companies if they are criminally prosecuted. The criminal law requires proof of intent to retaliate. The "intent" of a legal entity like a corporation may be expressed in its policies.

If a federal prosecutor calls a company to investigate the allegedly wrongful termination of a whistle-blower, the company at a minimum should be prepared to state that its policies forbid such acts.

Perhaps even more important, managers should be trained regarding the new

penalties for retaliation against whistle-blowers so they do not inadvertently expose themselves, or their companies, to criminal prosecution or civil penalties.

And, of course, companies should contemporaneously document the performance issues of problem employees. Raising long-standing performance issues only after an employee has engaged in whistle-blowing will be powerful evidence of retaliation.

Employment lawyers have been advocating timely written employee feedback for decades, so employment discrimination cases may be appropriately defended. Now that there is potential criminal liability and a high degree of media attention to whistle-blowers, the stakes have been raised significantly.

These legal and social developments provide compelling reasons for businesses to adopt policies against retaliation.

Besides reducing exposure, policies against retaliation may be powerful tools for communicating to employees in the post-Enron era that their employer places a high value on corporate integrity and on protecting employees who voice their concerns about the same.

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