Might the failures of Enron, Global Crossing, Arthur Andersen or WorldCom have been prevented if employee/whistleblowers had been legally protected from retaliation for raising concerns about fraud against shareholders? Congress, and President Bush, appear to think so. On July 30, 2002, President Bush signed into law the Sarbanes-Oxley Act ("the Act"), H.R. 3763, 107th Cong. (2002), which was enacted to address corporate fraud and accountability issues. The Act also contains several significant new protections for corporate whistleblowers.

Section 806 of the Act creates a new federal civil right of action on behalf of any employee of a publicly traded company who is subject to discrimination in retaliation for reporting corporate fraud or accounting abuses. The federal nature of this right of action means that it is available to all employees of public companies across the nation. Section 1107 imposes new criminal penalties on any individual who retaliates against whistleblowers for providing truthful information relating to the commission or possible commission of any federal offense to a law enforcement officer. This criminal penalty is not limited to employees of public companies, is not limited to federal offenses regarding fraud against shareholders, and applies nation-wide. These provisions have already stirred controversy, with the White House issuing a statement interpreting the provisions narrowly, and the sponsoring Senators replying that the statute is intended to be broad.

President Bush Signs into Law New Protections for Corporate Whistleblowers

In addition to Sections 806 and 1107, other provisions of the Act illustrate Congress' belief that employee/whistleblowers are an important part of the overall scheme to prevent fraud against shareholders. Examples include: (1) Section 301, which requires Audit Committees of Boards of Directors to establish procedures for the anonymous submission of employee concerns regarding questionable accounting or auditing matters; (2) Section 501, which prohibits brokers and dealers from retaliating against analysts for preparing unfavorable research reports; and (3) Section 802, which imposes criminal penalties for the destruction, alteration, or falsification of records.

The Act is a significant departure from previous federal and state whistleblower protections. Until now, most federal and state whistleblower laws have protected only employees who complain about public health or safety issues. Most laws have not protected employees who raise concerns about fraud against shareholders because such issues had not been perceived as affecting the public health or safety. Now, with the failure of several major businesses, and the corresponding investment losses suffered by millions of employees and shareholders, Congress has made the judgment that fraud against shareholders is an issue of serious public concern sufficient to justify significant new civil and criminal protections.
In response to these provisions of the Act, public companies should (1) examine their employment policies and procedures to ensure that they prohibit retaliation against whistleblowers who raise concerns about fraud against shareholders, and (2) examine whether their policies and procedures provide effective mechanisms for employees to raise such concerns. All companies, private and public, should review their employment policies and practices with an eye towards minimizing the risks of criminal liability. More details about the whistleblower aspects of the Act, and steps companies may take to respond to the Act, are set forth below.

NEW CIVIL ACTION PROTECTING EMPLOYEE WHISTLEBLOWERS

Section 806 prohibits publicly traded companies1 from discriminating2 against an employee in retaliation for any lawful act done by the employee to:

(1) provide information or otherwise assist in any investigation involving corporate fraud or accounting abuses, provided the investigation is conducted by a federal regulatory or law enforcement agency, any Member of Congress or Congressional Committee, or a person with managerial authority within the publicly traded corporation; or

(2) file, testify, participate in, or otherwise assist in any proceeding related to an alleged violation of corporate fraud laws or regulations.

An employee alleging discharge or other discrimination in retaliation for engaging in any of these protected activities may file a complaint with the U.S. Department of Labor (DOL) not later than 90 days after the date on which the violation occurred. Within 60 days after receiving a complaint, and after giving the employer an opportunity to respond, the Secretary of Labor will conduct an investigation to determine whether the complaint has merit.3 Upon completion of the investigation, the Secretary will issue a preliminary order which may require reinstatement of the complainant, and payment of back pay with interest and compensation for special damages. Within 30 days of notification of the Secretary's findings, either party may file objections to the Secretary's findings and request a hearing. If a hearing is not requested within 30 days, the preliminary order becomes a final order. A hearing will be conducted before a DOL Administrative Law Judge, who will issue a recommended decision, which the Secretary can adopt as a final decision.

If the Secretary has not issued a final decision within 180 days of the filing of the complaint, the complainant may bring an action in the appropriate federal district court, without regard to the amount in controversy.4 The employee may recover compensatory damages, including back pay with interest, and special damages sustained as a result of the discrimination, including litigation costs and attorneys' fees. In addition, a prevailing complainant would be entitled to reinstatement with the same seniority status the complainant would have had but for the discrimination.

NEW CRIMINAL PENALTIES FOR RETALIATION AGAINST WHISTLEBLOWERS

In addition to the protections afforded to whistleblowers by Section 806, Section 1107 of the Act, titled "Retaliation Against Informants," imposes criminal penalties on any individual who "knowingly, with the intent to retaliate, takes any action harmful to any person, including interference with the lawful employment or livelihood of any person, for providing to a law enforcement officer any truthful information relating to the commission or possible commission of any
Federal offense." This provision supplements the existing federal criminal penalties for witness intimidation. The penalties include a fine and/or imprisonment up to 10 years. In contrast to the civil remedies created by Section 806, the criminal provisions of Section 1107 are not limited to the actions of publicly traded companies, nor are they restricted in scope to matters involving corporate fraud or accounting abuses.

AVOIDING WHISTLEBLOWER CLAIMS

The civil and criminal penalties provided in the whistleblower protection provisions of the Act represent only some of the potential costs of a whistleblower claim. In the current climate, a whistleblower claim can generate negative publicity, thereby undermining investor confidence, drawing the attention of regulators, and weakening employee morale and loyalty. The following are some steps companies can take to avoid such claims:

Establish an Employee Concerns Program. Establishing a forum in which employees can raise concerns and have some assurance that their concerns will be investigated is an effective means of resolving an employee’s grievance before the employee files a complaint. In addition, an Employee Concerns Program (ECP) can help alert management of wrongdoing early on, thereby providing an opportunity to intervene and prevent further damage.

Train Managers and Supervisors to Instill a Corporate Culture Conducive to Employees Raising Their Concerns. One of the lessons of the recent accounting scandals is the importance of maintaining a culture conducive to raising concerns. Indeed, Congress appears to have concluded that many of the companies whose conduct precipitated the Act had cultures in which employees were discouraged from raising concerns and dissent was suppressed. Managers and supervisors should be trained to encourage employees to raise concerns and question activities without fear of reprisal.

Take Disciplinary Action Against Those Who Engage in Retaliation. All employees should be put on notice (e.g. through training and the employee handbook) that if they harass or discriminate against another employee for raising a concern, they will be subject to disciplinary action.

Document Performance Issues. In defending against a whistleblower claim, it is critical to have thorough, unambiguous evidence demonstrating that the same unfavorable personnel action would have been taken in the absence of the complainant’s protected conduct. Accordingly, managers should thoroughly document performance issues on a routine basis.

Shaw Pittman has extensive experience representing companies faced with whistleblower claims brought under federal and state statutes, and establishing programs and procedures designed to prevent such claims. In particular, Shaw Pittman has advised companies in the nuclear power, health care, and aviation industries, which have experienced whistleblower claims for many years, regarding avoiding and litigating such claims. Shaw Pittman regularly provides advice and counsel to assist companies in implementing personnel actions in a manner which minimizes the possibility of civil and white-collar criminal litigation, and regularly defends companies before federal and state courts and agencies when litigation cannot be avoided.

1. Under the Act, any company that must either register its securities or file reports under the Security Exchange Act of 1934 is considered a publicly traded company.

2. Discriminatory conduct includes harassment, demotion, suspension, and termination.
3. Section 806 does not set forth the procedures governing complaints filed thereunder. Instead, such complaints will be governed by the procedures set forth in a whistleblower protection statute for workers in the aviation industry, codified at 49 U.S.C. § 42121.

4. Section 806 does not supplant or replace other remedies available to employees under Federal or State law, or under any collective bargaining agreement.

If you have any questions regarding this Alert or any other related matter, please contact:

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