

The Whistleblower Provisions of the Sarbanes-Oxley Act of 2002

by

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The Corporate and Criminal Fraud Accountability Act of 2002, better known as the Sarbanes-Oxley Act, establishes a new federal cause of action, “Whistleblower Protection for Employees of Publicly Traded Companies,” designed to shield employees from retaliation when they provide information that they reasonably believe to be a violation of federal securities law, the rules of the SEC or “any Federal law relating to fraud against shareholders.” The legislation weaves a web of complementary provisions encouraging whistleblowers and punishing those who would retaliate against them.

What is particularly striking about Sarbanes-Oxley is that Congress took such an integrated approach to the matter of whistleblowing. Not only does the Act prohibit retaliation against whistleblowers, but it also solicits, encourages and reinforces the very act of whistleblowing. The statute requires public companies not only to adopt a code of business ethics, but also to set up an internal apparatus to receive, review and solicit employee reports concerning fraud and/or ethical violations. The teeth of the statute can be found in an enforcement scheme that includes administrative, civil *and* criminal enforcement mechanisms and provides for both corporate *and* individual liability. Sarbanes-Oxley is certainly not the first federal whistleblower protection law, but given its multi-faceted enforcement scheme, its aggressive potential penalties and its broad application, it is arguably the most forceful and the most important.¹

Who Is Covered?

The statute primarily pertains to public companies and their officers, employees, contractors, subcontractors and agents. Individuals, including officers and other employees of covered companies, are subject to liability in their personal capacities. Depending on how the terms eventually are defined, certain sections of the Act also appear to apply to companies and their agents that do business with publicly traded companies, such as contractors and subcontractors, even if those companies are not publicly traded.² For example, an outside auditor making reports on a public company may engage in activities covered under the Act.³

The Act places quasi-whistleblower disclosure burdens on in-house attorneys at public companies, and perhaps outside lawyers as well.⁴ Finally, both public *and* privately held companies have obligations under Section 1107 of the Act (discussed below).

What Acts Are Protected?

Section 806 of the Sarbanes-Oxley Act creates a new civil cause of action in favor of employees of public companies who are retaliated against for their covered disclosures concerning fraud against shareholders, including accountancy violations, violations of SEC rules and related

matters. Covered disclosures include providing information or assistance in the investigation of conduct that the employee reasonably believes violates securities laws or regulations to a federal regulatory or law enforcement agency, a member of Congress, a congressional committee, any of their supervisors within the company, or any person at the employer with the power to “investigate, discover or terminate misconduct.”⁵ The statute also protects an employee who “assists in any proceeding actually filed or about to be filed relating to securities fraud or fraud against shareholders.”⁶

A separate section of the Act, Section 1107, protects employees of both public and *private* companies who make truthful reports to a “law enforcement officer,” where such disclosures relate to the possible commission of a federal offense.⁷ Section 1107 must be distinguished from Section 806 of the Act, which is both more limited (applies to “covered” activities of employees at *public* companies) and more expansive. Section 806 is triggered not just by reports to law enforcement, but also by reports of wrongdoing to members or committees of Congress⁸ and internal reports to company personnel with supervisory or investigative authority. Section 1107 also appears to apply to reports of wrongdoing involving any federal law, not just fraud against shareholders. Furthermore, Section 1107 prohibits any form of intentional retaliation, “including interference with the lawful employment or livelihood of any person.” This section covers a multitude of employment actions short of actual discharge and may extend beyond employees to cover independent contractors or the employees of vendors. Of course, the overriding distinction between Sections 806 and 1107 is the potential for prison time. Importantly, Section 1107 also is being codified as an amendment to the federal criminal code section prohibiting retaliation against witnesses, victims or informants, which is a “predicate act” under the federal racketeering statute, RICO.⁹ As such, violations of Section 1107 can provide a basis for an affected employee to bring a civil RICO claim against an employer for treble damages.

Interestingly, the Act does *not* protect employee complaints to the news media. Such reports, by themselves, do not constitute whistleblowing under the Act.

Administrative Complaints Procedure

Employees claiming retaliation can file a complaint with the Department of Labor (DOL) within 90 days of an alleged violation, and may, in some cases, file suit in the appropriate federal district court. After receiving a complaint from an employee claiming retaliation, the Secretary of Labor is required to conduct an investigation, except that the Secretary of Labor is not permitted to investigate an employee’s complaint unless the employee makes a *prima facie* showing that his or her protected conduct was a contributing factor in the adverse employment action taken by the employer. If the employee makes this showing, the secretary of labor must nevertheless refuse to conduct an investigation if the employer can demonstrate, by clear and convincing evidence, that it would have taken the adverse employment action despite the employee engaging in protected conduct.¹⁰

If, on the basis of its investigation, the DOL finds that the employee has been subject to retaliation, the DOL must order the employer to immediately reinstate the employee. The intended speed of action contemplated under this Act is ambitious, but perhaps unrealistic. The employee-whistleblower is provided with a federal administrative remedy, which, if

administered properly by the DOL, would ensure that whistleblowers are back on the job within as little as 180 days of discharge. Either an employee or employer may appeal the investigative findings. Upon appeal, the parties are entitled to an on-the-record hearing.¹¹

The DOL has significant experience administering whistleblower claims under a wide variety of labor and employment laws. The department employs approximately 200 employees in seven district offices around the country for this purpose. The DOL's Office of Administrative Law Judges (Office of ALJ) has a Web site that publishes whistleblower decisions and procedures under several federal statutes and will supplement that information as new information becomes available concerning the whistleblower and anti-retaliation provisions of Sarbanes-Oxley.¹² The Office of ALJ of the DOL now processes about 125-150 whistleblower cases each year. Hearings before ALJs are requested in an estimated 10-15 percent of the complaints filed with OSHA.

In the past, the Occupational Safety and Health Administration (OSHA) has reviewed the bulk of the complaints received by DOL, probably because most of the current whistleblower statutes administered by DOL involve allegations of safety violations. OSHA also has significant experience in handling allegations of retaliation. It is possible that a new unit, possibly one with specific financial experience, will be set up to handle initial investigations under Sarbanes-Oxley. However, OSHA currently has jurisdiction. Under current practices, the DOL investigates and then issues a "determination letter." If the letter determination is not accepted by both parties, or the case is not otherwise resolved, the matter is assigned to the Office of ALJ and goes to administrative hearing. These hearings are relatively formal and resemble full-blown trials.

The Sarbanes-Oxley enforcement procedures for handling whistleblower were adopted from those used in administering airline employee whistleblowing claims, but differ in several significant ways. Under Sarbanes-Oxley, employees may bring an action in federal court if the secretary of labor does not resolve the employee's complaint within 180 days (and there is no showing that such delay was due to the bad faith of the employee). Employees are entitled to a trial de novo in any court case. That means that the prior DOL proceedings or findings, if any, will not limit the court. If past experience is any indication, it seems likely that the DOL will frequently fail to complete investigations within the mandated 180-day period. Many employees may choose to allow the agency additional time for investigation, but it is also likely that more complaints will find their way to the courthouse under Sarbanes-Oxley than under other analogous federal whistleblower statutes.

What are the Remedies for Whistleblowers who Suffer Adverse Action?

A protected employee may not be discharged, demoted, suspended, harassed or discriminated against in any other way because of a protected disclosure. This statute prohibits not only the potential retaliatory actions by the publicly traded corporate employer, but also such actions by any officer, employee, contractor, subcontractor or agent of such company. Employees who prevail in whistleblower cases (whether determined by DOL or a court) are entitled to damages, which may include:

- reinstatement to the same seniority status that the employee would have had but for the adverse employment action
- back pay
- interest
- all compensatory damages to make the employee whole
- “special Damages,” including litigation costs, reasonable attorney’s fees and costs, expert witness fees, and “all relief necessary to make the employee whole.”¹³

Sarbanes-Oxley does not provide for punitive damages. The Act does, however, contain a provision making clear that the statute does not preempt state and federal law. We can expect, therefore, that employees will file actions making multiple claims, including public policy and state statutory claims, in conjunction with a claim under Sarbanes-Oxley. Many of these concurrent claims will include the potential for punitive damages. The combination of claims may enhance plaintiff lawyer latitude in jury presentations by making otherwise irrelevant evidence admissible and by allowing plaintiffs to argue their case in the context of more generalized corporate fraud. Most large jury awards are the result of the jury’s desire to “send a message.” Thus, and despite the lack of an express right to punitive damages under Sarbanes-Oxley, the new provisions may well enhance leverage in settlement discussions, and in coordination with other causes of action, may even increase punitive damage potential.

Are There Other Penalties for Retaliation against the Whistleblower?

In addition to the potential for civil damages, discrimination against whistleblowers is *criminalized* if the whistleblower made a report to law enforcement. The importance that the media has placed on this provision is not an exaggeration; criminal penalties are unprecedented in whistleblower legislation. Furthermore, an employee who successfully prosecutes a civil or administrative whistleblower case can use the record created in those proceedings to convince local U.S. attorneys to prosecute his or her corporate tormentors. By amending the obstruction of justice statute to prohibit employment retaliation, Congress also opened the door for private plaintiffs to use the Racketeer Influenced and Corrupt Organizations Act (RICO) against their employers.¹⁴

The criminal penalties are contained in Section 1107 of the statute and apply to a much broader set of whistleblowing transgressions than just those relating to securities fraud. A retaliatory action becomes a criminal matter under Section 1107 of the Act if the employee provides information to a law enforcement officer concerning the commission of *any* federal offense. Under this section, retaliation includes “interference with the lawful employment or livelihood” of the whistleblower. Thus, employers and their agents may be fined, imprisoned for not more than 10 years, or both if they intentionally retaliate against employees who provide information or otherwise assist law enforcement in a wide variety of investigations that relate to a wide variety of federal “offenses.”¹⁵

New Audit Committee Complaint Procedures

Working hand-in-hand with the whistleblower provisions, Section 301 of the Sarbanes-Oxley Act mandates that audit committees establish procedures for the confidential, even anonymous,

reporting by employees and individuals outside the company of concerns regarding questionable accounting or auditing matters. Under the whistleblower provisions of Sarbanes-Oxley, internal reports to such committees constitute protected activity subject to the anti-retaliation provisions of the Act.¹⁶ There is no other whistleblower statute administered by the Department of Labor that contains such a provision. If the provision is not complied with by the time the SEC issues regulations on Section 301, the company can be delisted from a national exchange, a very tough penalty.

Adding to the web of provisions encouraging whistleblowing is Section 307 and its implementing guidelines, which establish new rules of conduct for any attorney who appears or practices before the SEC. Covered attorneys must report “evidence of a material violation of securities law” or “breach(es) of fiduciary dut(ies)” or “similar violation(s)” to a corporation’s “chief legal counsel” or “chief executive officer.” If these reports do not properly resolve an attorney’s concerns, an attorney is required to further report his or her concerns to a company’s audit committee or a similar committee. Under the whistleblower provisions, all such reports would likely be considered protected activity.

Code of Ethics Requirement for Senior Financial Officers

Section 406 of the Act mandates the adoption of a code of ethics for senior financial officers. Each reporting company also must promptly disclose failure to adopt such rules or any changes in or waivers from their code of ethics.¹⁷ Corporate ethics policies typically include (i) the procedures for handling any conflicts between personal and corporate interests, (ii) corporate theft, (iii) improper use of confidential or insider information, (iv) accurate financial and expense reporting and (v) falsification of company records and financial statements.¹⁸ The SEC recently issued proposed rules under Section 406, which defines a code of ethics as standards “reasonably necessary to deter wrongdoing” and to promote honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships; avoidance of conflicts of interest and potential conflicts of interest and internal disclosure procedures; compliance with applicable governmental laws, rules and regulations; prompt internal reporting of code violations; and accountability for adherence to the code. Significantly, the proposed rules require a public company to report on a current basis amendments to, and waivers from, its code of ethics. While the proposed rules recognize that the Act does not absolutely require that companies institute an ethics code, they do make clear that a public company must disclose the reason for any failure to adopt such a code.¹⁹ Similarly, the New York Stock Exchange (NYSE) and the Nasdaq Stock Market (Nasdaq) also have proposed rules for listed companies concerning requiring the adoption of corporate ethics policies. These rules cover a broader range of topics than those covered in the SEC rules and apply to all employees, not just senior financial officers.²⁰

While the Act requires only that the procedures relate to complaints of accounting, accounting controls and audit matters, companies may choose to incorporate the Act’s reporting procedures into more comprehensive codes of conduct or ethics policies. If these procedures are included in a code of conduct or ethics policy that addresses other ethical standards and areas of conduct, the policy should make clear that the audit committee is specifically responsible for handling and

responding to complaints about accounting, accounting controls and audit matters, whereas company management may have responsibility for compliance with other standards.²¹

Related Document Retention Mandates

The Act tightens document retention requirements in a way that reinforces and complements the whistleblowing provisions by targeting acts that are intended to impede, obstruct or influence other investigations, including acts done in relation to, or contemplation of, any such matter or case. The Act provides:

Whoever knowingly alters, destroys, mutilates, conceals, covers up, falsifies, or makes a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence the investigation or proper administration of any matter within the jurisdiction of any department or agency of the United States or any case filed under Title 11, or in relation to or contemplation of any such matter or case, shall be fined under this title, imprisoned not more than 20 years, or both.²²

Clearly, whistleblowers will be protected when reporting destruction of documentation arguably relevant to a covered investigation. But the prohibition on document destruction “with the intent to obstruct a federal investigation” seems to apply to more than financial or accountancy investigations. It would arguably include such other federal investigations as wage-hour investigations by the Department of Labor or employment discrimination investigations by the Equal Employment Opportunity Commission.

The second document-retention provision of Sarbanes-Oxley is more limited in scope. The Act amends a witness-tampering statute and focuses on the destruction of documents involved in an “official proceeding.” An “official proceeding” generally means a proceeding before a judge or court of the United States, a proceeding before Congress or a proceeding before a federal government agency.²³ Specifically, the Act states:

(c) Whoever corruptly —

(1) alters, destroys, mutilates, or conceals a record, document, or other object, or attempts to do so, with the intent to impair the object’s integrity or availability for use in an official proceeding; or

(2) otherwise obstructs, influences, or impedes any official proceeding, or attempts to do so, shall be fined under this title or imprisoned not more than 20 years, or both.²⁴

This provision prohibits not only destruction of documents, but also the alteration or concealing of documents. It may also apply to those making false entries in a covered document.

Open Issues and Some Observations

Certain aspects of the Sarbanes-Oxley whistleblowing provisions are more expansive than many realize. For example, Section 1107 relates to “interference” with the investigation of *any* matter within the jurisdiction of any department or agency of the United States (an investigation of a federal offense.) Although it is not clear exactly how this provision will be applied in practice or interpreted in court, it is arguably broad enough to cover interference with or obstruction of such everyday investigations of employers as those conducted by the Equal Employment Opportunity Commission (EEOC), the Occupational Health and Safety Administration (OSHA), the Wage and Hour Division of the Department of Labor, or even the Immigration and Naturalization Service (INS.) It seems almost certain that officers, agents, supervisors, and employees of publicly held companies accused of participating in retaliatory activities will be sued in their individual capacities and may even face prison time for proven violations of the Act. Some commentators have called these specific provisions “overreaching.” They are certainly unprecedented.²⁵

The Act raises several issues of interpretation that will have to be decided in the first generation of cases brought by whistleblowers. As case in point, Senator Chuck Grassley (R-Iowa) has already engaged in a war of words with the White House and the Solicitor’s office over the scope of coverage of the whistleblower provisions — specifically, whether whistleblowers are protected when they make a report to any member of Congress or whether such report must be made to a member of a committee engaged in or imbued with authority to investigate the issue in question.²⁶

Another pending issue of interpretation will relate to how the burden-shifting rules referenced in connection with Department of Labor investigations will be applied in court actions brought individually by employees claiming retaliation. Under Sarbanes-Oxley, if the employee makes out a *prima facie* case of retaliation, the employer will then have to show by “clear and convincing evidence” that it would have taken the same adverse employment action, even if the employee had not blown the whistle. Under most employment statutes, the employee carries the burden of proof at all times, and it is therefore the employee who has to do the convincing. “Clear and convincing” is a higher standard for employers (and friendlier for employees) than that which is imposed under most federal anti-retaliation laws. Under predecessor laws, the employer’s obligation is to articulate a non-discriminatory business reason for the adverse action, but the ultimate burden of proof remains with the employee. If precedent under these similar statutes is followed in Sarbanes-Oxley cases, it is probable that the whistleblower will have to show that whistleblowing activities were a contributing factor in the adverse employment action alleged.

What Will the Future Bring?

Should we expect a flood of whistleblower claims under Sarbanes-Oxley? Probably not. The provisions are fairly modulated and the procedures encouraging internal and administrative reports should limit the number of claims that get to the courthouse. This prediction must be tempered by a number of factors, however. First and in the short term, we can expect that continued media attention of corporations gone amuck will do as much to generate complaints and litigation as the legislation itself. In fact, the SEC experienced a sharp increase in the number of whistleblower-type e-mail complaints in January and February of 2002, well before

the passage of Sarbanes-Oxley. The agency received 525 complaints per business day in January 2002 immediately after the Enron story broke, compared with a daily average of 365 in 2001. The SEC also reported that the figure leapt to a record 763 e-mails on Feb. 5 — the day that Americans listened to congressional testimony on the results of an internal investigation of the Houston-based energy trader.²⁷

We can also expect — again, in the short term — that courts will be favorably disposed to legal actions by whistleblowers and may lean in favor of such claims in close cases. An example of newfound court sensitivity to the corporate scandal epidemic can be found in the case of *McGarrity; v. Berlin Metals, Incl.*²⁸ The Indiana appellate court reversed summary judgment and reinstated the wrongful discharge claim of a former CFO. The CFO alleged that he had been terminated for refusing to falsify financial and tax records. In recognizing a public policy common law claim in that state, the court made the following comment: “[w]ith the sole exception of the war on terrorism, no issue dominates current thought more than the corporate and accountancy ethical scandals which have rocked our country.”

Another issue influencing the level of whistleblower claims we might expect under Sarbanes-Oxley is somewhat anecdotal. It appears that generically speaking, retaliation claims have been on the rise for at least a decade. For example, retaliation charges received by the EEOC (such charges typically claim that the employee has been the victim of retaliation for protesting the employer’s alleged unlawful employment practices) increased more than 200 percent between 1991 and 1998, according to that agency. Retaliation claims have been popular at the courthouse based on the apparent fact — noticed by attorneys on both sides of the bar — that a retaliation allegation is more likely to get to trial and conversely less likely to be dismissed on summary judgment. One reason for this trend may be that retaliation claims are usually not contingent on the success of the underlying complaint (upon which the retaliation claim is based).²⁹ The retaliation claim is seldom considered frivolous because these cases are built on timing, subjectivity and inference. We can expect a similar experience under Sarbanes-Oxley. Similar to retaliation claims under Title VII of the Civil Rights Act of 1964³⁰, Sarbanes-Oxley whistleblowers are entitled to protection from retaliation even if their reports of “wrong-doing” turn out to be inaccurate. In order to claim protection under the Section 806, the employee providing information need only “reasonably believe” that what he or she is reporting may constitute a violation of the various covered laws. Whether the employee is reasonable is an objective test, but it will probably depend on the specific facts as known from the employee’s perspective. Similarly, under Section 1107 of the Act, the employee has an obligation to provide “truthful” information to law enforcement, but it is likely that courts will consider a report “truthful” if the employee subjectively believes the report to be truthful. Employers who suspect that a charge is being made in bad faith may well find their suspicion difficult to prove.

Given this proof problem, an employee who believes himself or herself to be on the verge of discharge — perhaps for nondiscriminatory reasons like performance or unexcused absence — may opportunistically “trump up” a whistleblower complaint. By recasting his or her job problems as being related to concerns about company wrongdoing, such an employee transforms a routine performance issue into a potential retaliation claim. Employers have often complained that employees raising even patently frivolous concerns are nonetheless “bulletproof” — that is,

the employer feels it cannot exercise normal supervisory control without substantial risk of expensive litigation.

While it is true that even meritless retaliation claims can be a defense challenge, sophisticated employers can do much to protect themselves. Clear, well-publicized standards and training protocols, along with consistent internal documentation, will serve to protect reasonable management prerogative. One more caution: unlike some analogous employment statutes and state common law actions, Sarbanes-Oxley appears to apply to “retaliation” short of actual termination or final “adverse employment action.” Thus, the Act places additional emphasis on the need to be able to justify even interim personnel decisions, performance evaluations and temporary assignments.

Suggestions for Modifying Company Policy and Practice

What should companies do to comply with the whistleblowing provisions of Sarbanes-Oxley? Here are some suggestions:

Create an Open-Door Policy for Reports of Corporate Fraud. Policies will need to be reviewed, revised or created to reflect the focus of the Act on accounting and auditing matters. Also, you will need to ensure that your company has a confidential, anonymous complaint procedure that is capable of receiving and acting on complaints. Many companies have ethics hotlines in place, which may be modified to address the new mandates under the Act.

Establish a Complaint and Investigation Protocol. The company must investigate allegations of corporate fraud and other ethical breaches. A protocol, designed to assure competent and independent investigation and review of relevant facts, and for determining who should investigate, is essential. Common sense must be used to avoid conflicts of interest. Do not ask someone to investigate his or her boss or events in which they themselves have a stake. In order to assure compliance, the process must not only be fair, but it also must have the appearance of fairness.

Create an Ethics and Conflict-of-Interest Policy. Although the Act focuses on senior financial management, these policies are advisable for all employees. Employers should consider adopting a broader ethics policy than that which is required under the Act. Customization of the policy to take into account the particular business and culture is advisable. An effective ethics and compliance program also can assist in reducing fraud and eliminating or reducing criminal sentences under the Federal Organizational Sentencing Guidelines.

Publicize Policy Prohibiting Retaliation. This message must be communicated to employees in writing and through training. As with other forms of protected conduct such as complaints of discrimination or harassment, employees who complain of corporate fraud must be protected from retaliation.

Create or Amend Your Document Retention Policy. Companies must implement a document retention policy or ensure that their existing policy addresses the requirements of the Act. Documents should not be destroyed in contemplation or in the midst of a federal investigation,

official proceeding or Chapter 11 bankruptcy proceeding. Make certain that all appropriate documents and document keepers are covered. Few companies are able to completely centralize document retention in this era of electronic communications. Since document retention obligations are affected by pending and anticipated investigations (some of which may be known to the corporation but not necessarily to individual document holders, your policy must be carefully crafted and must also include training and protocols for communicating fluid retention obligations. Many other considerations will impact your company's policy and are beyond the scope of this article.

Train Employees About Complaint Procedures and Company's Anti-Retaliation Commitment. Policies are meaningless unless employees know about them. Make certain that employees understand that the stakes are high, with personal criminal penalties looming. Training will be particularly important for those employees who have the authority to terminate, demote or reassign employees. These employees must be trained on the type of conduct that would violate the Act and the type of documentation that might help a company from being wrongly accused or convicted. In proving that an employee's termination was unrelated to his or her complaint about company practices, documentation of the real reason for discharge is key. Contemporaneous documentation is most advantageous. Where documented work-related problems predate any protected activity by the employee, the employer may be able to prevail on a causation defense.

Monitor Compliance. Consider designation of a well-trained compliance officer responsible for implementing the program and overseeing compliance matters. Consider internal compliance audits performed on a regular basis beyond those required by law. Consider annual written certifications by employees that they have reviewed, understood and will comply with applicable compliance policies. Review hiring policies to assure that the company conducts reasonable due diligence to avoid hiring employees prone to fraud.

Check Insurance Coverage. In addition to the above, employers should review insurance policies to determine whether officers and agents are covered under existing coverage for allegations of whistleblower violations or interference with employment violations. Consider whether your company needs special employment practice liability insurance (EPLI). This coverage may provide you some degree of protection defending against whistleblower and retaliation claims when the company already has established policies and procedures. Be cautious, however, before accepting a policy that interferes with your right to select counsel and/or your right to decide whether to settle non-meritorious claims. There may be consequences to settlement or how a claim is handled, beyond the normal "cost-benefit" analysis performed by an insurance company.

Conclusion

Insiders have always been in the best possible position to blow the whistle on corporate wrongdoing. With the Sarbanes-Oxley Act of 2002, Congress has used a variety of sticks and carrots to pursue a fundamental change in corporate culture. For some companies the culture shift provoked by Sarbanes-Oxley could be revolutionary. Thomas Huxley is quoted as saying, "[i]t is not who is right, but what is right, that is of importance." The statement is true, but

sometimes doing right still depends on an *individual* stepping forward. Knowing what is right is not enough. To paraphrase Edmund Burke, evil triumphs when good people do nothing.³¹ Rather than fearing the whistleblower provisions of Sarbanes-Oxley, companies ought to consider the Act a wake-up call. Going beyond the technical requirements of the Act, companies should recognize their business interest in creating an ethically aware workforce where employees are willing, even encouraged, to come forward with their concerns about fraud, self-dealing, and other violations of law or company policy. Embracing a corporate culture of openness and integrity will not only provide management with an early warning of actual problems, but will likely result in corporations receiving that warning in advance of outside regulators or law enforcement.

¹The Sarbanes-Oxley whistleblowing provisions join a growing list of federal whistleblower statutes applicable to blowing the whistle on health care statute violations, environmental transgressions, workplace safety, and other issues of public or state interest. In addition to the statutory provisions listed below, several federal statutes—Title VII of the Civil Rights Act of 1963 and the Employee Retirement Income Security Act (ERISA) among them—contain specific “anti-retaliation provisions. These provisions prohibit retaliation for filing claims or participation in activities protected by those particular statutes. The first whistleblower statute was enacted in 1863, at the height of the Civil War. The False Claims Act was aimed at punishing corrupt defense contractors who were overcharging the Union Army for its supplies. This statute actually empowered ordinary citizens to sue *qui tam* (in the name of the sovereign) and allowed them to keep a portion of damages awarded. The law survives today and has won whistleblowers more than \$200 million in the past 30 years alone. Several states have enacted whistleblower statutes. Most of these statutes protect employees of the government or their subcontractor. Some, like the one in California, also provide general protection to whistleblowers working in the private sector. In addition to those mentioned above, federal whistleblower statutes include:

- 5 U.S.C. §§ 2302 (b)(8), (9) - Protecting government employees
- 42 U.S.C. § 7622 - Air Pollution and Control Act
- 15 U.S.C. § 1674 - Consumer Protection Act
- 42 U.S.C. § 5851 - Energy Reorganization Act
- 33 U.S.C. § 948 - Longshoremen's and Harborworker's Act
- 30 U.S.C. § 815 - Mine Safety Act
- 29 U.S.C. § 660 - Occupational Safety and Health Act
- 45 U.S.C. § 441 - Railroad Safety Act
- 42 U.S.C. § 300 - Safe Drinking Water Act
- 38 U.S.C. § 2021 - Selective Service Act
- 42 U.S.C. § 6971 - Solid Waste Disposal Act
- 49 U.S.C. § 2305 - Surface Transportation Assistance Act of 1982
- 15 U.S.C. § 2622 - Toxic Substances Control Act
- 29 U.S.C. § 793 - Vocational Rehabilitation Act
- 33 U.S.C. § 1397 - Water Pollution Control Act
- 49 U.S.C. § 42121 - Aviation Whistleblower Protection Procedures

² 18 U.S.C. § 1514A(a).

³ 18 U.S.C. § 1514A(a). See also, *Mackowiak v. University Nuclear Systems*, 735 F.2d 1159 (9th Cir. 1984).

⁴ In-house attorneys are required to disclose certain information to specific in-house officials or committees. The failure of an attorney to abide by these disclosure provisions could open that attorney to severe personal sanctions. Sarbanes-Oxley Act § 307. The SEC issued proposed rules regarding attorney obligations on November 6, 2002. The proposed rules do not significantly flesh out the “up the ladder” reporting requirement imposed by the statute. The SEC takes an expansive view of who is an attorney subject to the rule, covering all attorneys who are admitted, licensed or otherwise qualified to practice law, whether employed in-house by an issuer or retained to perform legal work on behalf of an issuer. See <http://www.sec.gov/news/press/2002-158.htm>.

⁵ Sarbanes-Oxley Act § 806 (a); 18 U.S.C. 1514A.

⁶ Section 806 is implicated any time a covered employee lawfully acts:

(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) a 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. Sarbanes-Oxley Act § 806 (a).

The reference in the statute to “section 1341, 1343, 1344, or 1348” refers to Title 18 of the United States Code, which addresses mail fraud; wire, radio or television fraud; bank fraud; and securities fraud.

⁷ Sarbanes-Oxley Act § 1107.

⁸ But see endnote 28, *infra*.

⁹ Section 1107 of Sarbanes-Oxley is being codified at 18 U.S.C. § 1513(e), which is a listed act of “racketeering activity” under the Racketeer Influenced and Corrupt Organizations Act (“RICO”), 18 U.S.C. § 1961(1) *et seq.*

¹⁰ The DOL procedures are adapted from the statute providing airline employees whistleblower protection. 49 U.S.C. 42121(b).

¹¹ The DOL hearing procedures are set forth in 29 C.F.R. Part 18.

¹² Detailed information about the Office of ALJ, which administers whistleblower complaints, and its decisions, can be found at www.oalj.dol.gov.

¹³ Sarbanes-Oxley Act § 806 (c).

¹⁴ See endnote 9, *supra*. This provision exempts Sarbanes-Oxley whistleblowers from the effect of *Beck v. Prupis*, 529 U.S. 494 (2000) (finding that whistleblowers can’t use RICO without an overt act that is also a RICO predicate act). For more information, see Mueller, Michael J, “Can Employees Still Sue for Racketeering?” *The Metropolitan Corporate Counsel* (June 2000).

¹⁵ Section 1107 of The Sarbanes-Oxley Act of 2002 amends 18 U.S.C. § 1513 to add the following:

(e) Whoever 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, shall be fined under this title or imprisoned not more than 10 years, or both. 18 U.S.C. 1513(e).

¹⁶ See 18 U.S.C. 1514A(a)(1).

¹⁷ The Securities and Exchange Commission (the SEC) issued proposed rules on October 22, 2002, relating to the Code of Ethics provisions of Section 406 of the Sarbanes-Oxley Act of 2002. The proposed rules would require companies subject to the reporting requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, to disclose whether or not, and if not why not, they had adopted a written code of ethics for their principal executive officer, principal financial officer, principal accounting officer or controller, or persons

performing similar functions (collectively, the “senior financial officers”). The proposed rules also go beyond the provisions of Section 406 of the Act by requiring a company to include its chief executive officer within the coverage of its code of ethics and by requiring it to file the code of ethics as an exhibit to its annual report. If adopted, the proposed rules would require companies to disclose, pursuant to new Item 406 of Regulations S-B and S-K, Item 15(c) of Form 20-F or Instruction B.(9) of Form 40-F:

- whether the company has adopted a written code of ethics that applies to the company’s principal executive officer and senior financial officers; and
- if the company has not adopted a code of ethics, the reasons why it has not done so.

In order to help investors better understand the ethical principles that govern the executives of the companies in which they invest, the proposed rules would require each company to file a copy of its code of ethics as an exhibit to its annual report on Form 10-K, 10-KSB, 20-F or 40-F. In addition, the proposed rules would require companies to publicly disclose whether they had made changes to, or granted a waiver from, their code of ethics and would require companies to file a copy of their code of ethics as an exhibit to their annual report filed with the SEC.

¹⁸ The New York Stock Exchange (NYSE) and the Nasdaq Stock Market (NASDAQ) have also submitted corporate governance rules to the SEC for approval (the SRO Proposals). The SRO Proposals would require a listed company to, among other things, (1) adopt a code of conduct, which would apply to all directors, officers and employees of the listed company, (2) make the code publicly available (the rule would require posting on the company’s Web site) and (3) promptly disclose any waiver of the code granted to a director or executive officer. For example, any waiver of the code of conduct for directors and executive officers must be approved by the listed company’s board of directors or a committee thereof. In addition, the SRO Proposals would require that a listed company’s code contain compliance standards and procedures that would facilitate the effective operation of the code. It is important to note that listed companies would need to comply with both the SEC’s final rules and the applicable SRO Proposal.

¹⁹ The full text of the proposed rules on Disclosure Required by Sections 404, 406 and 407 of the Sarbanes-Oxley Act of 2002 can be found at <http://www.sec.gov/rules/proposed/33-8138.htm>.

²⁰ A summary comparison of these rules and links to the full rules can be found at <http://www.calpers.ca.gov/whatshap/calendar/board/invest/200209/Item07a-03.2.pdf> (last visited November 11, 2002).

²¹ On a related note, The American Institute of Certified Public Accountants has issued a new standard, SAS 99: ‘Consideration of Fraud in a Financial Statement Audit,’ which replaces SAS 82. SAS 99 is effective for audits of financial statements for periods beginning on or after December 15, 2002.

²² Sarbanes-Oxley Act § 802(a).

²³ 18 U.S.C. § 1515.

²⁴ Sarbanes-Oxley Act § 1102.

²⁵ See, for example, Westman, Daniel, “Restoring Trust in the Market,” *The Motley Fool.com* (September 22, 2002) <http://www.fool.com/Specials/2002/02092600trust.htm> (Web site last visited November 11, 2002).

²⁶ As recently as October 31, 2002, Senator Chuck Grassley (R-Iowa) sent a follow-up letter to the White House asking for a detailed response to a letter sent in August to White House Counsel Alberto Gonzales. The August letter asked for clarification of the administration’s interpretation of the corporate whistleblower provisions in the Corporate and Criminal Fraud Accountability Act. Senator Grassley specifically disputes the White House’s position on whether a report to Congress must be to a member or committee with specific or active investigatory authority over the issue. Senator Grassley asserts that the Act is intended to cover a report to any member of Congress. Senator Grassley also expressed concern about certain remarks made by Solicitor Eugene Scalia in an

amicus brief filed by the Department of Labor. Details of the dispute can be found at <http://grassley.senate.gov/releases/2002/p02r10-31.htm> (Web site last visited November 11, 2002).

²⁷ Fairbank, Katie, “Enron sets nation to whistle-blowing,” *The Dallas Morning News* (Wednesday, February 27, 2002) and Banstetter, Trebor, “SEC getting more whistleblower complaints since Enron,” *Fort-Worth Star Telegram* (Feb. 21, 2002).

²⁸ Case No. 45D05-9812 CT-2564 (C.A. Ind. Aug. 6, 2002).

²⁹ For example, it is well established under Title VII of the Civil Rights Act of 1964 that a retaliation claim may go forward even if the underlying protected act is determined to be faulty.

³⁰ See 42 U.S.C. Section 2000e-3(a).

³¹ With apologies to Edmund Burke, the original form of his well-known statement is: “The only thing necessary for the triumph of evil is for good men to do nothing.”