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In Search of Corporate America's Dirty Secrets: Sarbanes-Oxley Act Deputizes Most Employees

By: Pablo Quiñones

From the pages of the Wall Street Journal to the cover of Time magazine, the message being sent to corporate employees is clear: there is something rotten in Corporate America and the first employee to tell all should be seen as a hero. To help clear the air, the Sarbanes-Oxley Act of 2002, among other things, has deputized the employees of companies that work in or with public companies to ensure that their true financial condition is disclosed to the public.

The likelihood that the Sarbanes-Oxley Act will impact your company is relatively certain. As of September 30, 2002, there are approximately 3,800 public companies listed on the NASDAQ, 2,800 public companies listed on the New York Stock Exchange and 680 public companies listed on the AMEX. These companies, in turn, collectively work with millions of employees. Moreover, since the Enron financial scandal, there has been a leap in the number of employees and former employees of public companies disclosing evidence of financial fraud to the SEC. (*See* "Post-Enron Number of Informants Grows, SEC Enforcement Official Newkirk Reports," in 19 Individual Employment Rights No. 5 at 18 (11/26/02.))

In these times of declining bonuses, increasing lay-offs and unprecedented bankruptcy filings, many more employees may feel empowered to expose the next corporate scandal by the Act's creation of a right to sue in federal court to protect against retaliation. If your company is a public company or works with a public company, it should be taking affirmative steps to establish a set of comprehensive procedures for dealing with allegation of wrongdoing in-house. Whistle-blowers that use internal reporting systems should be valued as company protectors rather than ostracized as trouble-makers.

Retaliation for Employee Disclosure Now a Federal Case

Section 806 of the Sarbanes-Oxley Act prohibits a public company or "any officer, employee, contractor, subcontractor, or agent of [a public] company" from discharging, demoting, suspending, threatening, harassing, or otherwise

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Obligations to Employees Called to Military Service

By: Bennett Pine

Against the backdrop of escalating hostilities in the Middle East and reports of President Bush calling-up 100,000 military reservists to active duty, employers should be increasingly concerned with their military leave obligations under the Federal Uniform Services Employment and Reemployment Rights Act ("USERRA"). The 1994 law prohibits discrimination toward returning service members, reservists and National Guard members based on their active military duty or training obligations. This prohibition covers past, present and future military service and extends to most areas of employment, including hiring, promotion, re-employment and employee benefits.

Coverage/Eligibility

USERRA covers all employers regardless of size, and applies to all veterans who perform voluntary or involuntary service in the uniformed services, including active duty, active duty for training, inactive duty, inactive duty for training, and full-time National Guard duty.

Five Year Service Protection

USERRA entitles veterans to serve a total of five years on active military duty without forfeiting their rights to return to

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discriminating against an employee "in the terms and conditions of his employment" because:

(1) the employee discloses information, or assists in a federal regulatory, law enforcement, congressional, or internal company investigation regarding any conduct that the employee "reasonably believes" violates any federal law or regulation relating to fraud against shareholders; or,

(2) the employee files, testifies, participates in or otherwise assists in a proceeding filed or about to be filed relating to an "alleged" violation of federal laws or regulations relating to fraud against shareholders.

Since the law extends to any "any officer, employee, contractor, subcontractor, or agent of [a public] company," the Act may give rise to liability for certain companies doing business with public companies as well as individual liability for officers, managers and supervisors.

An employee who is wrongfully discharged in violation of Section 806 must file a complaint with the Department of Labor (DOL) within 90 days from the date of the wrongful employment action. Only if the DOL has not issued a final decision within 180 days of the filing of the complaint and "there is no showing that such delay is due to the bad faith of the claimant" can the employee bring an action in federal court.

The employee must show that wrongful retaliation for engaging in protected activity was a contributing factor in the adverse employment action. The employer has a high burden of demonstrating by clear and convincing evidence that the adverse employment action would have been taken even in the absence of the employee's protected conduct. If successful, a Sarbanes-Oxley plaintiff may recover "all relief necessary to make the employee whole," such as reinstatement, back pay with interest, and any "special damages … including litigation costs, expert witness fees, and reasonable attorney fees." Punitive damages are not available.

In addition to civil liability, the Act imposes criminal fines and imprisonment for up to 10 years for any persons who retaliate against corporate whistleblowers who provide law enforcement officers any truthful information relating to the commission of a federal offense.

Thus, aside from having to pay an employee damages and watching your company's stock plummet, you could potentially be required to pay significant fines and land in jail.

Preparing for Corporate Employee Disclosure

There are affirmative steps, however, that your company should be taking to decrease the risk that employee disclosure will lead to liability for retaliation, criminal sanctions, or corporate scandal. While what is best for your company should be analyzed on a case specific basis, here are a few general suggestions:

Establish a confidential internal reporting systems, such as a toll-free company hotline, and encourage (yes, encourage) employees to anonymously disclose questionable accounting practices through the internal reporting systems. Make these internal reporting systems known to employees and to outside vendors, agents, or contractors.

Establish policies and procedures for promptly investigating all employee complaints and create an internal reward system for legitimate complaints. A prompt response time is essential. The employee who reported the problem will know if anything is being done to investigate it and, if nothing is, may conjure up images of a corporate conspiracy to stonewall and feel compelled to expose the corporate secrecy.

Revise and redistribute company policies on retaliation and educate supervisory employees, directors and officers, on the consequences to the company and to them individually of retaliating against complaining employees.

Now, more than ever, consistently and fully document all the performance problems of your employees. If you cannot clearly and convincingly prove your company would have engaged in the adverse employment action in the absence of the employee's disclosure, the DOL or a court may find that you retaliated against the employee.

Review existing insurance policies, such as Employment Practices Liability Insurance or Director's and Officer's Liability policies, to make sure you and your company are covered for some, if not all, of the litigation costs and damages for a Sarbanes-Oxley claim.

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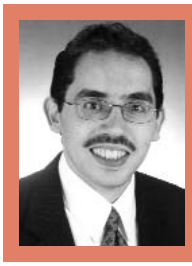
These suggestions provide a starting point for knowing whether your company could be the next victim of a corporate scandal before the employee airs your corporate secrets on the evening news or in a congressional hearing. A fresh look at your company's practices and procedures may also help to prepare your company for handling the truth—whether it is financial irregularity or a disgruntled employee looking for a payday—before your company is consumed by the perception of corporate wrongdoing. ■



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their civilian jobs with full seniority, and attendant benefits. There are a number of conditions under which the 5 year period may be extended.

Applying for Reinstatement

Length of military service determines when a veteran must report back to work or apply for re-employment. If length of service is 30 days or less, a veteran must return to work by the next regularly scheduled working day. If length of service is between 31 days and 180 days, a veteran must apply for re-employment within 14 days of completing military service. If length of service is 181 days or more, a veteran must reapply for employment within 90 days of completing military service. Veterans hospitalized for an injury incurred or aggravated during military service have up to two years to seek re-employment.

Re-employment Position

While the position to which a returning veteran must be reinstated depends upon the duration of the military service, generally speaking a returning veteran must be re-employed in their prior position or the position he or she would have attained, but for the military service.

Returning Status: The "Escalator"

USERRA incorporates the "escalator" principle which requires that qualified veterans returning to work be, with some exceptions, re-employed at the "precise point" they would have attained had their employment not been interrupted by military service. This escalator principle seeks to ensure that veterans receive the "perquisites of seniority" —changes and advancements in job status that necessarily occur "simply by virtue of continued employment." Such perquisites of seniority typically include pensions, severance pay, health benefits, employee stock option plans, and bonuses.

Restrictions on Termination Following Reinstatement

Regardless of an employer's at-will policy, an employee who has been re-employed after service lasting between 30 and 180 days is entitled to at least six months of employment protection under USERRA's statutory "cause" scheme. If an employee's service exceeded 180 days, he is entitled to at least a year of such protected employment. While the Act is silent on what standard of "cause" is to be applied, the traditional definition of "just cause" employed by labor arbitrators would generally apply.

Waiver of Re-Employment Rights

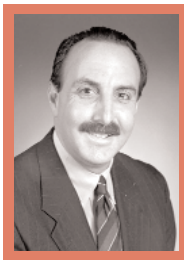
Veterans who fail to report or apply for re-employment within the prescribed period do not automatically waive re-employment rights, but are subject to employers' policies concerning absence from work. Veterans can waive protections under USERRA. The waiver, however, must be "clear and unequivocal." Veterans waive their re-employment rights when, prior to leaving for military service, they knowingly provide clear, written notice of their intent not to return to work. USERRA protections end if a veteran separates from military service with a dishonorable or bad-conduct discharge, under other than honorable conditions, or by sentence of a general court-martial.

Enforcement and Remedies

Relief that can be sought and granted under the act include compliance, damages in the amount of pay or benefits wrongfully denied; and liquidated damages, when the violation of USERRA is willful.

* * *

Given the large number of reservists who have been, or will be, called to active service in the current climate, it is essential that all employers understand their legal obligations to their employees in military service. ■



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Legislative Update: New York State Bans Sexual Orientation Bias

New York Governor George Pataki has assigned a bill, effective January 17, 2003, that prohibits discrimination throughout New York State based on actual or perceived sexual orientation. The ban will apply to employment, as well as housing, public accommodations, education and credit. Previous laws prohibiting such discrimination in the state were limited to New York City, certain other municipalities and employees of the New York State government.