POINT/COUNTERPOINT ON THE SARBANES-OXLEY ACT OF 2002: A VIEW FROM THE EMPLOYER’S AND EMPLOYEE’S PERSPECTIVES

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CHAPTER 3
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POINT/COUNTERPOINT ON THE SARBANES-OXLEY ACT OF 2002: A VIEW FROM THE EMPLOYER’S AND EMPLOYEE’S PERSPECTIVES

“With 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.” McGarrity v. Berlin Metals, Inc., 774 N.E.2d 71, 74 (Ind. Ct. App. 2002).

I. OVERVIEW

In the last two years, we have seen the American economy rocked by corporate scandals. Indeed, the all-too-familiar scandals at Enron, WorldCom, and Arthur Andersen, and the resulting investment losses suffered by employees and shareholders, have devastated public trust and confidence in large corporations and their executives.

A survey conducted by the AFL-CIO and released in August 2002 solidified this public sentiment. See AFL-CIO, Workers’ Rights in America: What Workers Think About Their Jobs and Employers (Sept. 2001), available at http://laborday.aflcio.org/rights/report.pdf. Of the individuals surveyed, 56% responded that new laws were needed to hold corporations responsible for the way they treat employees. Id. 68% of the respondents believed that workers needed “much more” or “somewhat more” protection of their rights. Id. 63% of the individuals surveyed stated that they trusted employers “just some” or “not much.” Id. Importantly, a majority of the respondents, 63%, believed that corporations pursue profits at the expense of loyalty to employees. Id.


The Sarbanes-Oxley Act generally regulates the auditing, financial disclosure, executive compensation, and corporate governance practices of publicly traded corporations. However, the Act also contains several employment-related provisions. Of greatest concern, the Act exposes not only the corporation, but also its officers and employees in their individual capacities, to civil and criminal penalties. The Sarbanes-Oxley Act greatly expands both corporate and personal exposure for civil and criminal sanctions in employment-related investigations.

This paper will detail some of the most significant employment-related provisions of the Act, such as those involving protections for whistleblowers and document retention and destruction. It will then separately discuss views about this law from both the employer’s perspective and the employee’s perspective.

A. Whistleblower Protections


The enactment of the Sarbanes-Oxley Act created new federal protections for whistleblowers. Specifically, Section 806 of the Act provides civil whistleblower protection to employees of publicly traded companies who report acts of fraud to federal officials with the authority to remedy the wrongdoing, or to supervisors or appropriate individuals within their companies. 148 Cong. Rec. S7418-01 (daily ed. July 26, 2002) (statement of Sen. Leahy). The Sarbanes-Oxley Act also created criminal penalties for companies, including their officers and employees, who retaliate against whistleblowers. See 18 U.S.C.A. § 1513(e) (West 2002). In contrast to the civil protections, the criminal protections are not limited to employees of publicly traded companies. Rather, the criminal provisions potentially apply to all companies who retaliate against whistleblowers.

1. Purpose Of The Civil Whistleblower Protection

Congress enacted Section 806 of the Act, Congress recognizing that “[a]lthough current law protects many government employees who act in the public interest by reporting wrongdoing, there is no similar protection for employees of publicly traded companies who blow the whistle on fraud and protect investors. With an unprecedented portion of the American public investing in these companies and depending upon their honesty, this distinction does not serve the public good.” 148 Cong. Rec. S7418-01.

Congress was also concerned that “corporate employees who report fraud are subject to the patchwork and vagaries of current state laws, even
though most publicly traded companies do business nationwide.” 1d. Thus, a whistleblower in one state might be more vulnerable to retaliation than a fellow employee in another state who takes the same actions. 1d. “Unfortunately, companies with a corporate culture that punishes whistleblowers for being ‘disloyal’ and ‘litigation risks’ often transcend state lines, and most corporate employers, with help from their lawyers, know exactly what they can do to a whistleblowing employee under the law.” 1d. Because of this discrepancy among state laws, Congress believed that “U.S. laws need to encourage and protect those who report fraudulent activity that can damage innocent investors in publicly traded companies.” 1d.

2. The Statutory Language
Section 806 pertains to civil protections afforded to whistleblowers and states as follows:

(a) No company with a class of securities registered under section 12 of the Securities Exchange Act of 1934 . . . or that is required to file reports under section 15(d) of the Securities Exchange Act of 1934 . . . 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 [of this Act], 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) any 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.


Thus, Section 806 creates “a new provision protecting employees when they take lawful acts to disclose information or otherwise assist criminal investigators, federal regulators, Congress, their supervisors (or other proper people within a corporation), or parties in a judicial proceeding in detecting and stopping actions which they reasonably believe to be fraudulent.” 148 Cong. Rec. S7418-01.

a. Who Is Protected
Consistent with legislative intent, the whistleblower protection applies to all employees of a publicly traded company.

b. Prohibited Conduct
The Act prohibits a publicly traded company from firing, demoting, suspending, threatening, harassing, or in any other manner discriminating against the whistleblowing individual in the terms and conditions of employment because of any lawful act done in connection with protected conduct.

3. Procedure For Making A Civil Whistleblower Complaint
If an employee believes that his employer has retaliated against him in violation of the Sarbanes-Oxley Act, the Act sets forth an expedited procedure for filing an administrative complaint. The Act adopted the rules and procedures set forth in the employee protection provisions of the Wendell H. Ford Aviation Investment & Reform Act for the 21st Century (“AIR 21”), 49 U.S.C. § 42121 (2000), which was enacted on April 5, 2000, to provide protection to employees against retaliation by air carriers because of protected whistleblowing activities. See 18 U.S.C.A. § 1514A(b)(2)(A) (providing that an action under the whistleblower provisions of the Act will be governed by the rules and procedures set forth in 49 U.S.C. § 42121(b)). Thus, a whistleblower complaint brought under the Sarbanes-Oxley Act must follow the procedure set forth in the AIR 21 statute.

Unfortunately, the federal agency authorized under the Sarbanes-Oxley Act to promulgate regulations interpreting the Act, the Department of Labor (“DOL”), has not yet issued any interim or final regulations. However, the DOL has implemented regulations interpreting the rules and procedures set forth in AIR 21, which may provide guidance by analogy as to the regulations the DOL may eventually implement to govern the Sarbanes-Oxley Act. This paper will discuss some of those regulations. Thus, a
reference in this paper to “the AIR 21 regulations” will refer to the regulations promulgated by the DOL to interpret AIR 21. This paper will also address some of the regulations implemented by the DOL that set forth the procedures for handling whistleblower complaints under other similar federal laws such as the Safe Water Drinking Act, 42 U.S.C. § 300j, the Water Pollution Control Act, 33 U.S.C. § 1367, the Toxic Substances Control Act, 15 U.S.C. § 2622, the Solid Waste Disposal Act, 42 U.S.C. § 6971, the Clean Air Act, 42 U.S.C. § 7622, and the Energy Reorganization Act, 42 U.S.C. § 5851. References in this paper to regulations interpreting other whistleblower laws will refer to those regulations. However, practitioners should be mindful that when referring to both the AIR 21 and other whistleblower regulations, such regulations are not necessarily those that the DOL will adopt to govern the Sarbanes-Oxley Act.

The Act provides that a “person who alleges discharge or other discrimination by any person in violation of subsection (a) may seek relief . . . by . . . filing a complaint with the Secretary of Labor.” 18 U.S.C.A. § 1514A(b)(1). Like proceedings under AIR 21 and other federal whistleblower laws, the Secretary of Labor has delegated its authority and assigned its responsibility for Sarbanes-Oxley Act whistleblower complaints to the Assistant Secretary for Occupational Health and Safety. See 67 Fed. Reg. 65,008 (Oct. 22, 2002). However, for ease of reference, this paper will refer to the Assistant Secretary as the DOL.

a. Statute Of Limitations

The statute of limitations for a civil whistleblower action is ninety (90) days from the date the alleged violation occurred. 18 U.S.C.A. § 1514A(b)(2)(D). Thus, the aggrieved employee must file his complaint with the DOL within that time frame. The DOL’s comments to the AIR 21 regulations state that the date the violation occurred “is considered to be when the discriminatory decision has been both made and communicated to the complainant. In other words, the limitations period commences once the employee is aware or reasonably should be aware of the employer’s decision.” 67 Fed. Reg. 15,454 (Apr. 1, 2002) (to be codified at 29 C.F.R. pt. 1979).

The AIR 21 regulations provide that the “date of the postmark, facsimile transmittal, or e-mail communication will be considered to be the date of filing; if the complaint is filed in person, by hand-delivery, or other means, the complaint is filed upon receipt.” 29 C.F.R. § 1979.103(d) (2002).

b. Form Of Complaint And Place Of Filing

The AIR 21 regulations provide that no particular form of complaint is required, and the comments to the regulations state that the complaint may be oral. 29 C.F.R. § 1979.103(b); 67 Fed. Reg. 15,454. If the complaint is oral, the comments provide that the oral complaint will be reduced to a writing by the OSHA official receiving the complaint. 67 Fed. Reg. 15,454. In contrast, the regulations under the other whistleblower laws provide that the complaint must be in writing and “should include a full statement of the acts and omissions, with pertinent dates, which are believed to constitute the violation.” 29 C.F.R. § 24.3(c).

The AIR 21 regulations provide that the employee may designate another person, such as an attorney, to act in the employee’s behalf in filing the complaint. 29 C.F.R. § 1979.103(a). The AIR 21 regulations further direct that the complaint should be filed with the OSHA Area Director responsible for enforcement activities in the geographical area where the employee resides or was employed, but it may also be filed with any DOL officer or employee. Id. at § 1979.103(c).

c. Investigation

Upon receipt of a complaint, the DOL must notify the employer in writing of the complaint and of the allegations contained in the complaint. 49 U.S.C. § 42121(b)(1) (2000). The AIR 21 regulations provide that the DOL must also notify the employer of the substance of the evidence supporting the complaint, “sanitized to protect the identity of any confidential informants.” 29 C.F.R. § 1979.104(a). The employer then has ten days to submit to the DOL a written statement and any affidavits or documents substantiating its position. Id. at § 1979.104(c). Within the same ten days, the employer may also request a meeting with the DOL to present its position. Id.

Within 60 days of receiving the complaint, the DOL must conduct an investigation. 49 U.S.C. § 42121(b)(2)(A). The AIR 21 regulations provide that investigations “will be conducted in a manner that protects the confidentiality of any person, other than the complainant, who provides information on a confidential basis.” 29 C.F.R. § 1979.104(d).

After its investigation and prior to the issuance of any findings or orders, the AIR 21 regulations state that if the DOL has reasonable cause, on the basis of information gathered in its investigation, to conclude that the employer has violated the Act, the DOL “will again contact the [employer] to give notice of the substance of the relevant evidence supporting the complainant’s allegations as developed during the course of the investigation.” Id. at § 1979.104(e). “This evidence includes any witness statements, which will be sanitized to protect the identity of confidential informants where statements were given in confidence.” Id. The employer “shall be given the opportunity to submit a written response, to meet with the investigators to present statements from witnesses in support of [its] position, and to present legal and factual arguments.” Id. The AIR 21 regulations further state that the employer “shall present this evidence within ten days of the [DOL’s] notification . . . or as
soon afterwards as the [DOL] and the named person can agree, if the interests of justice so require.” *Id.*

After its investigation, the DOL will issue its findings. 49 U.S.C. § 42121(b)(2). The AIR 21 regulations provide that these are written findings detailing whether reasonable cause exists to believe that the employee was subjected to unlawful discrimination. 29 C.F.R. § 1979.105(a). If the DOL concludes that there is reasonable cause to believe that a violation has occurred, it will issue a preliminary order providing for appropriate relief, which may include reinstatement. 49 U.S.C. § 42121(b)(2). Similarly, if the DOL finds that a violation did not occur, the DOL will notify the parties of that finding as well. 29 C.F.R. § 1979.105(a).

d. **Review Of The Findings And Order**

Any party who desires review—including judicial review—of the findings and preliminary order, or of an award for attorney’s fees, must file objections and request a hearing on the record within thirty (30) days of receipt of the findings and preliminary order. 49 U.S.C. § 42121(b)(2)(A); 29 C.F.R. § 1979.106. Importantly, the “filing of such objections shall not operate to stay any reinstatement remedy contained in the preliminary order.” *Id.*

The AIR 21 regulations provide that the objections and request for a hearing must be in writing and state whether the objection is to the findings, the preliminary order, and/or the award of attorney’s fees. 29 C.F.R. § 1979.106(a). The date of the postmark, facsimile transmittal, or email communication will be considered to be the date of filing; if the objection is filed by hand-delivery or other means, the objections are filed upon receipt. *Id.* Objections must be filed with the Chief Administrative Law Judge of the U.S. Department of Labor in Washington, D.C., and copies of the objections must be mailed at the same time to the other parties of record, the DOL’s designee who issued the findings and order, and the Associate Solicitor, Division of Fair Labor Standards of the U.S. Department of Labor. *Id.*

If a hearing is not timely requested, the preliminary order is deemed final and is not subject to judicial review. 49 U.S.C. § 42121(b)(2)(A). The AIR 21 regulations further provide that if the objections are not timely received, the findings are not subject to judicial review. 29 C.F.R. § 1979.106(b)(2).

If a hearing is requested, it is conducted by an administrative law judge (“ALJ”). *Id.* at § 1979.107(a). Importantly, the AIR 21 regulations provide that neither the DOL’s determination to dismiss a complaint without completing an investigation, nor the DOL’s determination not to dismiss a complaint, is subject to the review of the ALJ, and a complaint may not be remanded for the completion of an investigation on the basis that a determination to dismiss was made in error. *Id.* at § 1979.109(a). “Rather, if there otherwise is jurisdiction, the [ALJ] shall hear the case on the merits.” *Id.*

Upon receipt of an objection and request for a hearing, the Chief Administrative Law Judge will assign the case to a judge who will notify the parties, by certified mail, of the time and place for the hearing. *Id.* at § 1979.107(b). “The hearing is to commence expeditiously, except upon a showing of good cause or unless otherwise agreed to by the parties...[and] hearings will be conducted as hearings de novo, on the record.” *Id.* If both the complainant and the employer objected to the findings or order, the objections will be consolidated for a single hearing before the ALJ. *Id.* at § 1979.107(c). In the hearing, “[f]ormal rules of evidence shall not apply, but rules or principles designed to ensure production of the most probative evidence available will be applied [and] the administrative law judge may exclude evidence which is immaterial, irrelevant, or unduly repetitious.” *Id.* at § 1979.107(d).

After the hearing, the ALJ will issue a decision. *Id.* at § 1979.109(a). The ALJ’s decision requiring reinstatement or lifting an order of reinstatement issued by the DOL may not be stayed. *Id.* at § 1979.109(c). However, all other portions of the judge’s order can be stayed if a timely petition for review is filed with the Administrative Review Board. *Id.*

The decision of the ALJ becomes the final order of the DOL unless a petition for review is timely filed with the Administrative Review Board, which has been delegated authority to act for the DOL and to issue final decisions under the Sarbanes-Oxley Act. *Id.* at § 1979.110(a); 67 Fed. Reg. 64,272 (Oct. 17, 2002). To be effective, the petition must be received within 15 days of the date of the ALJ’s decision. 29 C.F.R. § 1979.110(a). The petition also must be served on all parties, the Chief ALJ, and the Assistant Secretary of OSHA. *Id.* at § 1979.110(a)-(b).

The final decision of the Board is issued within 120 days of the conclusion of the hearing, which is deemed to end all proceedings before the ALJ. 49 U.S.C. § 42121(b)(3)(A) (2000); 29 C.F.R. § 1979.110(c). The decision is served on all parties, the Assistant Secretary of OSHA, and the Chief ALJ. 29 C.F.R. § 1979.110(c).

Within sixty (60) days of the issuance of the final order by the ALJ, the parties may file a petition for review with the federal circuit court of appeals for the circuit in which the violation allegedly occurred, or in the circuit where the complainant resided on the date of the violation. 49 U.S.C. § 42121(b)(4)(A); 29 C.F.R. § 1979.112(a).

e. **The Role Of The DOL In The Proceedings**

As explained above, the complainant and the employer are named as parties in proceedings under the Sarbanes-Oxley Act. However, the regulations governing AIR 21 and the Energy Reorganization Act (“ERA”), 42 U.S.C. § 5851, further provide that at the discretion of the Assistant Secretary of the DOL, “the Assistant Secretary may participate as a party or may
participate as amicus curiae at any time in the proceedings.” 29 C.F.R. § 1979.108(a)(1) (concerning proceedings under AIR 21); see also 29 C.F.R. § 24.6(f)(1) (concerning proceedings under the ERA). “This right to participate shall include, but is not limited to, the right to petition for review of a decision of an [ALJ], including a decision based on a settlement agreement between the complainant and the [employer], to dismiss a complaint or to issue an order encompassing the terms of the settlement.” Id. “For example, the Assistant Secretary may exercise his or her discretion to prosecute the case in the administrative proceeding before an [ALJ]; petition for review of a decision of an [ALJ], including a decision based on a settlement agreement between the complainant and the [employer], regardless of whether the Assistant Secretary participated before the ALJ; or participate as an amicus curiae before the ALJ or in the Administrative Review Board proceeding.” 67 Fed. Reg. 15,454, 15,455-56 (Apr. 1, 2002) (to be codified at 29 C.F.R. pt. 1979).

The commentary to the AIR 21 regulations further suggest that the Assistant Secretary normally will not participate in the proceedings. Id. However, the commentary states that the Assistant Secretary may choose to exercise his discretion in certain circumstances “such as cases involving important or novel legal issues, large numbers of employees, alleged violations which appear egregious, or where the interests of justice might require participation by the Assistant Secretary.” Id.

These AIR 21 and ERA regulations suggest that the Assistant Secretary, an employee of the DOL, may prosecute a complaint before an ALJ who is also employed by the DOL. Importantly, this practice is similar to that which occurs under the National Labor Relations Act wherein the General Counsel for the National Labor Relations Board prosecutes a case on behalf of a complaining party before an ALJ who is employed by the DOL. However, until regulations are implemented to provide guidance on the DOL’s procedures under the Sarbanes-Oxley Act, it is unclear whether this procedure will be adopted by the DOL in prosecuting cases under the Act.

f. Judicial Action If The DOL Fails To Act Timely

If the DOL does not issue its decision within 180 days of the employee’s complaint, the employee may file suit in a federal district court and may obtain the same remedies that the DOL can award. 18 U.S.C.A § 1514A(b)(1)(B) (West 2002). “Only if there is no final agency decision within 180 days of the complaint” may the employee “bring a de novo case in federal court with a jury trial available.” 148 Cong. Rec. S.7418-01 (daily ed. July 26, 2002) (statement of Sen. Leahy). In this situation, the district court shall have jurisdiction “without regard to the amount in controversy.” 18 U.S.C.A. § 1514A(b)(1)(B). However, “[s]hould such a case be brought in federal court, it is intended that the same burdens of proof which would have governed in the [DOL proceeding] will continue to govern the action.” 148 Cong. Rec. S.7418-01.

4. Burdens Of Proof In Civil Whistleblower Actions

The DOL must conduct an investigation if the employee makes a prima facie showing that his whistleblowing was a contributing factor in the unfavorable personnel action. 49 U.S.C. § 42121(b)(2)(B)(i) (2002). Specifically, the statute states that the DOL “shall dismiss a complaint . . . and shall not conduct an investigation . . . unless the complainant makes a prima facie showing that [the protected conduct] was a contributing factor in the unfavorable personnel action alleged in the complaint.” Id. (emphasis added). The AIR 21 regulations further state that “[t]he complaint, supplemented as appropriate by interviews of the complainant, must allege the existence of facts and evidence to make a prima facie showing as follows: (i) [t]he employee engaged in a protected activity or conduct; (ii) [t]he [employer] knew, actually or constructively, that the employee engaged in the protected activity; (iii) [t]he employee suffered an unfavorable personnel action; and (iv) [t]he circumstances were sufficient to raise the inference that the protected activity was likely a contributing factor in the unfavorable action.” 29 C.F.R. § 1979.104(b)(1) (2002).

“For purposes of determining whether to investigate, the complainant will be considered to have met the required burden if the complaint on its face, supplemented as appropriate through interviews of the complainant, alleges the existence of facts and either direct or circumstantial evidence to meet the required showing, i.e., to give rise to an inference that the [employer] knew (or suspected) that the employee engaged in protected activity and that the protected activity was likely a reason for the personnel action.” Id. at § 1979.104(b)(2). “Normally, the burden is satisfied, for example, if the complaint shows that the adverse personnel action took place shortly after the protected activity, giving rise to the inference that it was a factor in the adverse action.” Id.

If the employee cannot make this showing, the DOL “shall dismiss the complaint . . . and shall not conduct an investigation.” 49 U.S.C. § 42121(b)(2)(B)(i).

Notwithstanding a finding that the complainant has made a prima facie showing, an investigation will not be conducted if the employer demonstrates by clear and convincing evidence that it would have taken the same unfavorable personnel action in the absence of the complainant’s protected behavior or conduct. Id. at § 42121(b)(2)(B)(ii) (emphasis added).

5. Available Civil Remedies For Whistleblowers

An employee prevailing in an action under the whistleblower provisions of the Sarbanes-Oxley Act is broadly entitled “to all relief necessary to make the
employee whole.” 18 U.S.C.A. § 1514A(c)(1) (West 2002). Such relief “shall include” reinstatement with the same seniority status that the employee would have had but for the discrimination, back pay with interest, and compensation for any special damages sustained as a result of the discrimination, including litigation costs, expert witness fees, and reasonable attorneys fees. Id. at § 1514A(c)(2). However, because punitive damages are not specifically provided for by the statute, it appears that whistleblowers may not recover punitive damages under the Act. Furthermore, the availability of potential criminal penalties under the Act largely eliminates the need for punitive damages, which generally serve the purpose of punishing wrongdoers.

In retaliation claims litigated administratively under analogous protections in the nuclear industry, “compensatory damages” included “damages . . . designed to compensate not only for direct pecuniary loss, but also for such harms as impairment of reputation, personal humiliation, and mental anguish and suffering.” In the Matter of Marvin B. Hobby, ARB Case Nos. 98-166, 98-169 (Feb. 9, 2001). Thus, it is likely that such damages would be recoverable under the Sarbanes-Oxley Act as well.

6. Criminal Penalties For Retaliation Against Whistleblowers

In addition to civil remedies, Section 1107 of the Sarbanes-Oxley Act amended 18 U.S.C. § 1513 to provide criminal penalties for such violations. The statute now provides for criminal fines and imprisonment for up to ten years for any individual who knowingly retaliates against a person for providing any truthful information regarding the commission or potential commission of any federal offense to any law enforcement officer. 18 U.S.C.A. § 1513(e).

Specifically, the amendment states as follows:

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 for not more than 10 years, or both.

Id. Although the civil provisions of the Act are limited to employees of publicly traded companies who complain about corporate fraud, the new criminal provisions are not restricted to employees of publicly traded companies, nor are they limited to complaints about fraud or accounting abuses. Rather, the criminal provisions potentially extend to all employers and all federal investigations.

7. Remedies Under Other Laws

The Act is clear that its new rights and remedies supplement, rather than preempt, existing rights and remedies. Id. at § 1514A(d). The Act specifically provides that it does not “diminish the rights, privileges, or remedies of any employee under any Federal or State law, or under any collective bargaining agreement.” Id. Indeed, as the legislative history recognizes, the Act “does not supplant or replace state law, but sets a national floor for employee protections in the context of publicly traded companies.” 148 Cong. Rec. S.7418-01 (daily ed. July 26, 2002) (statement of Sen. Leahy).

B. Document Retention And Destruction

The Sarbanes-Oxley Act also strengthens an existing federal law that prohibits document destruction and other forms of obstruction of justice. Prior to the enactment of the Sarbanes-Oxley Act, the federal obstruction of justice law, 18 U.S.C. § 1510 (2000), prohibited individuals from persuading others to engage in obstructive conduct. However, it did not prohibit an act of destruction committed by a defendant acting alone. Other obstruction of justice statutes covered destruction of documents by an individual defendant acting alone, but the courts which interpreted the statutes applied them only when there was a pending proceeding and a subpoena was issued for the destroyed evidence. See United States v. Aguilar, 515 U.S. 593 (1995).

The Sarbanes-Oxley Act closed this loophole by broadening the scope of the former law. 18 U.S.C.A. § 1512(c) (West 2002); Id. at § 1519. These provisions are “meant to apply broadly to any acts to destroy or fabricate physical evidence so long as they are done with the intent to obstruct, impede or influence the investigation or proper administration of any matter, and such matter is within the jurisdiction of an agency of the United States, or such acts done either in relation to or in contemplation of such a matter or investigation.” 148 Cong. Rec. S.7418-01. Congress also recognized that “the current laws regarding destruction of evidence are full of ambiguities and technical limitations that should be corrected” and these new provisions were “meant to accomplish those ends.” Id.

Pursuant to the amendment, an individual who acts alone in destroying documents, instead of acting as part of a conspiracy, now may be prosecuted even if the destruction occurred prior to the issuance of a subpoena. See 18 U.S.C.A. § 1512(c). The Act added criminal fines and imprisonment for up to 20 years for any individual who “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.” Id.

Another provision of the Act provides for criminal fines and up to 20 years imprisonment to anyone who “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.” Id. at § 1519.

II. VIEW FROM THE EMPLOYER’S PERSPECTIVE BY WILLIAM JOHN BUX AND MIRANDA TOLAR

The purpose of this section of the paper is to highlight some areas of importance to employers dealing with issues pertaining to the Sarbanes-Oxley Act. It will also provide some helpful guidance to employers and employers’ counsel for avoiding problems under the Act, and for dealing with problems when they arise. Due to the complexity of the Act and the dire consequences that may result in the event an employer unwittingly violates the Act, it is critically important for employers to obtain the advice of legal counsel before taking any action against a whistleblowing employee, or before destroying any documents related to the employee or to other similarly situated employees.

A. Employer’s Perspective On The Whistleblowing Provisions Of The Act

1. Civil Whistleblower Protection For Private Sector Employees

In Texas, public sector employees have had whistleblower protection for quite some time. TEX. GOV’T CODE ANN. § 554.001, et seq. (Vernon 1994). However, the Texas Supreme Court has repeatedly refused to create a judicial exception to the employment at-will doctrine for private sector whistleblowers. See Austin v. HealthTrust, Inc., 967 S.W.2d 400 (Tex. 1998) (declining to create a judicial exception to the at-will doctrine by recognizing a cause of action for private sector whistleblowers); Winters v. Houston Chronicle Publ’g Co., 795 S.W.2d 723 (Tex. 1990) (same). Similarly, there was no specific federal law for general whistleblower protection applicable to private sector employees until the Act, but certain federal laws such as Title VII, the ERA, and OSHA did allow a private whistleblower or retaliation action for specific types of protected conduct.

With the enactment of the Sarbanes-Oxley Act, private sector employees now enjoy a private cause of action for retaliation against whistleblowers who make allegations of fraud. The likely consequence of this new right is that Plaintiff’s attorneys, who know the employee may not have any other supportable claim, may fashion the claim to encompass retaliation for the employee raising some issue, no matter how minor, relating to corporate fraud or accounting practices. One could anticipate that the number of wrongful termination lawsuits will rise dramatically. Given the current climate and perception of business in general, courts may also be more likely to find wrongdoing based on retaliation against whistleblowing.

2. Protected Conduct

There are essentially two types of conduct that are protected by the civil whistleblower provisions of the Act. The first type of protected conduct involves disclosing information or otherwise assisting in an investigation of conduct that the employee reasonably believes is a violation of federal mail fraud, wire fraud, bank fraud, securities fraud, any SEC rule, or any federal law relating to fraud on shareholders. The language referring to “any provision of Federal law relating to fraud against shareholders” suggests that the provision could apply to violations of the Sarbanes-Oxley Act itself. See 18 U.S.C.A. § 1514A(a)(1) (West 2002).

However, this first type of whistleblower protection is also limited to disclosures made to, or investigations conducted by, a Federal regulatory agency, a Federal law enforcement agency, any Member of Congress, any committee of Congress, or any person with supervisory authority over the whistleblowing individual. The “Member of Congress” or “committee of Congress” language was interpreted by the executive branch to mean “investigations authorized by the rules of the Senate or the House of Representatives and conducted for a proper legislative purpose.” Press Release, Statement by George W. Bush (July 30, 2002), at http://www.whitehouse.gov/news/releases/2002/07/20020730-10.html. However, the Senators who authored the whistleblower provisions of the Act, Senators Patrick Leahy and Charles Grassley, publicly released a letter stating that this interpretation was contrary to the plain language of the statute. Kelly Wallace, Senators: Bush Could Undercut Whistleblowers (July 31, 2002), at http://www.cnn.com/2002/ALLPOLITICS/07/31/bush.leahy.corporate/index.html. The Senators expressed the view that “there is no limitation either to ongoing investigations of Congress or to matters within the jurisdiction of any Congressional Committee.” Press Release, Grassley, Leahy Continue Whistleblower Talks With White House (Aug. 1, 2002), at http://www.senate.gov/~grassley/releases/2002/p02r8-01.htm#. They further stated as follows:

The reason for this is obvious. Few whistleblowers know, nor should they be expected to know, the jurisdiction of the various Committees of Congress or the matters currently under investigation. The most common situation, and one that the recent Administration’s statement excludes from protection, is a citizen reporting misconduct to his or her own Representative or Senator, regardless of their committee assignments. Such disclosures are clearly covered by the terms of the statute.
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In response to the Senators’ letter, the Executive Branch issued another statement further explaining their position:

An employee who works at a publicly traded company provides information to a Member of Congress (and assume... the Member is not a chairman or ranking member of a Committee and is not a member of a Committee with jurisdiction) regarding a violation ...Finally, assume that there is no investigation being conducted by the Member at the time the information is provided...There is no question in our minds that the Congressional intent (and the clear language of the statute) is that the answer to the above scenario is . . . the employee is protected, whether there is an investigation pending or not. Our desire is to protect the well-intentioned employee who contacts his elected representatives (or any representative for that matter) and NOT require the employee to consult the Congressional Directory and Congressional Record prior to making his call to determine whether he/she will be afforded the whistleblower protections of the Act.

Press Release, Grassley Asks for Response from White House on Corporate Whistleblower Protections (Oct. 31, 2002), at http://www.senate.gov/~grassley/releases/2002/p02r10-31.htm. Thus, it remains to be seen how broadly the terms of the Sarbanes-Oxley Act will be applied.

The second type of protected conduct involves the filing of, participation in, or assistance in a proceeding relating to an alleged violation of federal mail fraud, federal wire fraud, bank fraud, securities fraud, any SEC rule, or federal laws prohibiting fraud against shareholders. See 18 U.S.C.A. § 1514A(a)(2).

3. Predictions About The Burdens Of Proof

As is evident, the Act provides a fairly employee-friendly burden of proof. The employee is not required to demonstrate that the protected action was the sole reason or even a significant factor in the action taken against him. Rather, he need only show that his whistleblowing was a “contributing factor” in the employment action.

The employer’s burden of proof (“clear and convincing evidence”) is much more onerous than that borne by the employee. The employer’s burden of proof under the Act is substantially different from that of most other employment-related laws and creates unusual and difficult legal and litigation strategy issues. For instance, although summary judgment is often granted to employers in employment discrimination cases, particularly in the Fifth Circuit, it may be more difficult for employers to obtain summary judgment under the Act. The practical impact of this burden of proof, along with the financial cost of litigation, may force an employer to consider settling early or otherwise avoiding most whistleblower claims that come along.

The impact of these burdens of proof leave many questions regarding the manner in which courts will apply the burden of proof. Unfortunately, there are no cases or Department of Labor opinions applying the Sarbanes-Oxley Act to a claim brought by an employee for alleged retaliation in response to a whistleblower claim. There are also no reported cases providing any substantive discussion of the burden of proof under AIR 21. However, cases decided under similar laws such as the ERA, which protects whistleblowers employed in the nuclear power industry, may provide some guidance, particularly since the ERA contains the same burdens of proof for employees (“contributing factor”) and employers (“clear and convincing evidence”) as the Sarbanes-Oxley Act. See 29 C.F.R. § 24.5(b)-(c) (2002).

For example, courts have applied the familiar McDonnell Douglas burden-shifting framework utilized in Title VII cases to whistleblower cases under the ERA. See Carroll v. United States Dep’t of Labor, 78 F.3d 352, 356 (8th Cir. 1996) (applying Title VII burden-shifting framework to a whistleblower retaliation case under the ERA); Bartlik v. United States Dep’t of Labor, 73 F.3d 100, 103 n.6 (6th Cir. 1996) (same); Kahn v. Sec’y of Labor, 64 F.3d 271, 277 (7th Cir. 1995) (same); see also Clean Harbors Envtl. Servs., Inc. v. Herman, 146 F.3d 12, 21 (1st Cir. 1998) (applying Title VII’s burden-shifting framework to a whistleblower retaliation case brought under the Safety Transportation Assistance Act). Under this framework, a complainant in an ERA whistleblower case must satisfy the initial burden of establishing a prima facie case of retaliation. Carroll, 78 F.3d at 356. The burden of production then shifts to the employer to articulate a legitimate non-discriminatory reason for discharging the complainant. Id. If the employer satisfies this burden, the presumptions disappear and the onus is on the complainant to prove that the proffered legitimate non-discriminatory reason is a mere pretext for the challenged employment action. Id. Because courts apply this burden-shifting framework to actions involving whistleblower retaliation under a similar law administered by the DOL, one could argue that the same burden-shifting framework should also apply to civil whistleblower actions under the Sarbanes-Oxley Act.

Additionally, court decisions interpreting whistleblower retaliation provisions under other statutes can provide some guidance as to what might constitute legitimate non-discriminatory reasons for an adverse employment decision under the Sarbanes-Oxley Act. For example, the Eighth Circuit concluded that a general decline in available work for which the employee was qualified, coupled with the employer’s
policy of retaining more highly qualified employees, constituted a legitimate non-discriminatory reason for the whistleblowing employee’s discharge under the ERA. *Carroll,* 78 F.3d at 356. The Seventh Circuit found that an employee’s abusive and inappropriate behavior toward his co-workers and supervisors, rather than his whistleblowing activity, was a legitimate non-discriminatory reason for his termination under the ERA. *Kahn,* 64 F.3d at 278-79. Finally, the Ninth Circuit examined an alleged violation of the whistleblower provisions of the Toxic Substances Control Act, Safe Drinking Water Act, and Clean Water Act, and concluded that a change in employee qualification requirements provided a legitimate non-discriminatory reason for an employee’s termination. *Sipes v. United States Dep’t of Labor,* No. 01-70024, 2002 WL 1963465 (9th Cir. Aug. 23, 2002).

It remains to be determined, however, whether other Title VII concepts will apply to cases of harassment or retaliation under the Sarbanes-Oxley Act. For example, two Supreme Court decisions provided employers with an affirmative defense to harassment complaints under Title VII if the employee suffered no tangible employment action, the employer had a written policy against harassment, and the employer took reasonable measures to prevent and correct harassment, if it occurred. See *Faragher v. City of Boca Raton,* 524 U.S. 775 (1998); *Burlington Indus., Inc. v. Ellerth,* 524 U.S. 742 (1998).

One could argue that if an individual officer, manager, or supervisor harassed an employee in violation of the Sarbanes-Oxley Act but no tangible employment action occurred, the employer should be entitled to an affirmative defense if it had a policy prohibiting harassment that was communicated to employees, and if it took prompt remedial action to correct any harassment that occurred. However, it is unclear whether these concepts will apply to actions brought under the Act.

4. A Note About Reinstatement Rights Under The Civil Whistleblower Provision of the Act

It is likely that many whistleblower complaints under the Sarbanes-Oxley Act will be filed following an employee’s termination from employment. In this scenario, the employee will file a complaint with the DOL alleging that his employment was terminated due to unlawful retaliation in response the employee’s protected whistleblowing activities.

Upon receiving the complaint, the Assistant Secretary for OSHA, pursuant to the authority granted to it by the DOL, will conduct an investigation to ascertain whether reasonable cause exists to believe that the employee was subjected to unlawful discrimination. 49 U.S.C. § 42121(b)(2)(A); 67 Fed. Reg. 65,008 (Oct. 22, 2002). After the investigation, OSHA will issue its findings and, if it believes that unlawful discrimination occurred, a reinstatement order requiring the employer to reinstate the employee to his former position. 49 U.S.C. § 42121(b)(2).

The Act provides employers with the right to file objections to the findings and order. 49 U.S.C. § 42121(b)(2)(A). Of particular concern to employers, though, is the filing of objections does not operate to stay the reinstatement remedy. *Id.* Thus, at this preliminary stage before any judicial tribunal has the opportunity to review the findings, the employer is required to reinstate the employee. Further, the employer is then required to retain the employee unless and until the DOL or the court conclude that a violation did not occur and/or that reinstatement is not required. This reinstatement requirement is particularly unfair to employers when one considers that the aggrieved employee may recover back pay in the event that a violation is found.

The harsh nature of this reinstatement remedy is evident when considering the same procedure in the context of EEOC proceedings. For example, assume that an employee files a Charge of Discrimination against his employer with the EEOC alleging discrimination on the basis of his race and retaliation. Further assume that the EEOC finds cause to believe that discrimination has occurred and issues the employee a right to sue letter. If the procedure adopted by the Sarbanes-Oxley Act applied in this context, the employer would be required, based solely upon the EEOC’s findings, to reinstate the employee prior to any review by a judicial tribunal.

5. Limitations On The Civil Whistleblower Protection

As explained above, the Act protects an employee if he provides information that he “reasonably believes” constitutes a violation of federal securities laws, SEC laws, or federal laws prohibiting fraud against shareholders. 18 U.S.C.A. § 1514A(a)(1) (West 2002). The reasonableness test provided under subsection (a)(1) was “intended to impose the normal reasonable person standard used and interpreted in a wide variety of legal contexts.” 148 Cong. Rec. S7418-01 (daily ed. July 26, 2002) (statement of Sen. Leahy).

Thus, in order to be protected, the employee must reasonably believe that the conduct constitutes a violation of law. Accordingly, if an employee falsely or maliciously makes a report about conduct that he knew or should have known was not a violation of the law, the employee should have no protection under the civil whistleblower provisions.

However, the employee’s burden of demonstrating reasonableness is light. As long as the individual has provided information regarding conduct that he reasonably believes to constitute a violation of various securities laws, he is protected. The employee need not correctly identify fraud to be protected. The legislative history indicates that “any type of corporate or agency action taken based on the information, or the information constituting admissible evidence at any
later proceeding would be strong indicia that it could support such a reasonable belief.” *Id.* “The threshold is intended to include all good faith and reasonable reporting of fraud, and there should be no presumption that reporting is otherwise, absent specific evidence.” *Id.*

A further limitation involves the requirement that the employee suffers an adverse action because of a “lawful act.” 18 U.S.C.A. § 1514A(a). Because the whistleblower provision only protects “lawful acts,” the provision would not protect illegal actions such as the improper disclosure of a company’s trade secret information. *Id.*

### 6. Individual Civil Liability

As explained above, the Act states that no publicly traded company “or any officer, employee, contractor, subcontractor, or agent of such company” may retaliate against a whistleblower. *Id.* This language appears to provide for individual liability against officers, employees, contractors, subcontractors, and agents. Additionally, the Act protects employees who complain to any person at the company who has the authority to investigate, discover, or terminate misconduct. *Id.* at § 1514A(a)(1)(C). This language likely extends to corporate counsel, HR professionals, executives, supervisors, and managers.

### 7. Individual Criminal Liability

As is evident from the statutory language itself, the criminal whistleblower provisions are extremely broad. The provisions are not limited to publicly traded companies or to matters involving corporate fraud or accounting abuses. Criminal liability also exists for any adverse action taken against an employee that interferes with his lawful employment or livelihood. 18 U.S.C.A. § 1513(e) (West 2002). Finally, the language protecting any person who provides “any truthful information relating to the commission or possible commission of any Federal offense” could encompass information given in any official proceeding, including actions by the DOL, EEOC, OSHA, INS, or NLRB. *Id.* Moreover, it protects employees who provide information on the commission or possible commission of “a Federal offense,” presumptively encompassing the entire federal criminal and civil codes into the Act. *Id.*

Perhaps most troubling is that the criminal provisions of the Sarbanes-Oxley Act potentially apply to anyone who knowingly retaliates against “any person.” *Id.* Therefore, these criminal provisions could apply to anyone involved in the termination of a whistleblowing employee including, for example, an employer’s human resources personnel or in-house counsel. Additionally, the language also suggests that the criminal provisions could protect individuals who were not even employed by the potential defendant, and who were actually retaliated against by a separate employer. It remains to be seen how these broad criminal penalties will be applied by the courts.

### 8. Extraterritorial Application Of The Whistleblower Protections

One concern that companies with international offices may face involves the extraterritorial application of the Sarbanes-Oxley Act, both for U.S. citizens working for U.S. companies abroad and for foreign nationals working abroad for U.S. companies. For example, suppose a U.S. citizen works exclusively in China for a U.S. company and blows the whistle in China about practices occurring solely in China. Is that employee protected by the Sarbanes-Oxley Act? Similarly, suppose a Chinese citizen works exclusively in China for a U.S. company and blows the whistle in China about alleged violations that occurred only in China. What protections are available for that employee?

Unfortunately, the statute does not provide any guidance as to whether its whistleblowing provisions could apply extraterritorially. Several provisions of the Act suggest some extraterritorial effect, such as those provisions pertaining to foreign accounting firms and foreign attorneys. See 15 U.S.C.A. § 7216; *Id.* at § 7241.

In an employment case involving another federal statute that was silent on the issue of extraterritorial effect, Title VII of the Civil Rights Act of 1964, the United States Supreme Court found that it did not apply extraterritorially to regulate the employment practices of United States firms that employ U.S. citizens abroad. *EEOC v. Arabian Am. Oil Co.*, 499 U.S. 244 (1991).

In *Arabian American Oil*, a U.S. citizen working in Saudi Arabia for Arabian American Oil Company, a Delaware corporation, brought suit alleging that his employer terminated him in violation of Title VII. *Id.* at 247. The district court dismissed his case, ruling that it lacked subject matter jurisdiction, and the court of appeals affirmed. *Id.* The employee then appealed the case to the Supreme Court. *Id.*

The Court noted at the outset that Congress has the authority to enforce its laws beyond the territorial boundaries of the United States. *Id.* at 248. However, whether Congress has actually exercised that authority is a matter of statutory construction. *Id.* The Court reiterated the “longstanding principle of American law that ‘legislation of Congress, unless a contrary intent appears, is meant to apply only within the territorial jurisdiction of the United States.’” *Id.* (quoting *Foley Bros., Inc. v. Filardo*, 336 U.S. 281, 285 (1949)). In fact, this principle is so strong that the Court recognized a “presumption against extraterritoriality.” *Id.* Unless an affirmative intention of Congress is clearly expressed, the Court stated that it would presume that a statute is primarily concerned with domestic relations and does not apply extraterritorially. *Id.*

The Court listed some factors that it considered in its analysis of the extraterritorial applicability of Title VII, including: (1) whether the statute as a whole indicates a concern that it not duly interfere with the
sovereignty and laws of the States; (2) whether the statute mentions foreign nations or foreign proceedings; (3) whether the statute provides any mechanism for overseas enforcement; (4) whether the statute addresses conflicts with foreign laws and procedures; and (5) whether the administrative agency charged with enforcement of the law contends that it applies extraterritorially. *Id.* at 255-56.

In *Arabian American Oil*, the Court found that these factors demonstrated the intent of Congress that Title VII apply domestically and not extraterritorially. *Id.* at 258. The Court also pointed out that “[w]hen it desires to do so, Congress knows how to place the high seas within the jurisdictional reach of a statute.” *Id.* (quoting *Argentine Republic v. Amerada Hess Shipping Corp.*, 488 U.S. 428, 440 (1989)). The Court left it to Congress to amend Title VII if it chose to do so. *Id.* at 259. As a result of this case, Congress amended Title VII to specifically apply to U.S. citizens employed abroad by U.S. employers, but not to foreign nationals employed by U.S. employers abroad. See 42 U.S.C. § 2000e(f) (2000).

In examining the factors enunciated in *Arabian American Oil* in conjunction with the Sarbanes-Oxley Act, it is unclear whether a court would conclude that the Act applies extraterritorially. With regard to the first factor, the whistleblower provision of the Act demonstrates an intent that it not preempt the laws of the states. 18 U.S.C.A. § 1514A(d) (West 2002). The Act does not address conflicts with foreign laws or procedures, and the DOL has not issued any regulations or other guidance regarding the applicability of the Act overseas.

However, with regard to the second and third factors, the Act does mention foreign nations and foreign proceedings, which would indicate that the Act could apply extraterritorially. For example, Section 106 pertains to foreign accounting firms and provides that “[a]ny foreign accounting firm that prepares or furnishes an audit report with respect to any issuer, shall be subject to this Act and the rules of the Board . . . . in the same manner and to the same extent as a public accounting firm that is organized and operates under the laws of the United States or any state.” 15 U.S.C.A. § 7216(b). This Section further provides that the “Board may, by rule, determine that a foreign public accounting firm . . . . that does not issue audit reports nonetheless plays such a substantial role in the preparation and furnishing of such reports for particular issuers, that it is necessary or appropriate, in light of the purposes of this Act and in the public interest or for the protection of investors, that such firms . . . should be treated as a public accounting firm . . . . for purposes of registration under, and oversight by the Board.” *Id.* at § 7216(a)(1). This Section further provides that the “Board may, by rule, determine that a foreign public accounting firm . . . . that does not issue audit reports nonetheless plays such a substantial role in the preparation and furnishing of such reports for particular issuers, that it is necessary or appropriate, in light of the purposes of this Act and in the public interest or for the protection of investors, that such firms . . . should be treated as a public accounting firm . . . . for purposes of registration under, and oversight by the Board.” *Id.* at § 7216(a)(2). The Act also provides a mechanism and procedure for obtaining audit work papers prepared by foreign accounting firms and states that, by issuing opinions or performing material services upon which a registered public accounting firm relies, a foreign accounting firm is deemed to have subjected itself and consented to the jurisdiction of the courts of the United States. *Id.* at § 7216(b).

Another provision of the Act, Section 302, pertains to a corporate requirement to file periodic SEC reports. *Id.* at § 7241. This Section expressly states that these filing requirements remain in force and are not affected by a company’s foreign reincorporation, or by the company engaging in any action that results in the transfer of the corporate domicile or offices from inside the United States to outside the United States. *Id.* at § 7241(b).

These provisions of the Sarbanes-Oxley Act could be used to assert that the Act was intended to apply extraterritorially. Until (1) Congress clarifies the scope of the Act, (2) the DOL issues regulations on the subject, or (3) case law develops regarding the extraterritorial application of the law, employers would be well advised to proceed cautiously and obtain legal advice before taking any employment action against any employee who reports any corporate misconduct overseas, no matter how minor the alleged misconduct.

9. Rights Of Employers To Recover For Frivolous Claims

The Act is not all one-sided in favor of employee whistleblowers, but relief for employers is limited. If the Secretary of Labor finds that a complaint was frivolous or brought in bad faith, the Secretary may award to the prevailing employer a reasonable attorney’s fee not to exceed $1,000. See 49 U.S.C. § 42121(b)(3)(C) (2000).

10. Tips For Avoiding And/Or Dealing With Whistleblower Actions

- Establish or reissue policies pertaining to retaliation, communicate the policies to all employees, and train supervisors on the appropriate response to employee complaints.
- Make sure that any current policies on harassment or retaliation include prohibitions for harassment or retaliation against whistleblowers.
- Ensure that officers, managers, supervisors, and HR representatives are knowledgeable about the Act’s provisions. Ignorance of the law will not be a defense to its violation.
- Review insurance policies to determine whether coverage exists for officers, managers, and employees accused of violations of the Act’s whistleblower provisions.
- Treat all complaints of fraud seriously. Investigate and resolve these complaints in the same manner and with similar procedures currently used for sexual harassment complaints.
- Anticipate having to prove by clear and convincing evidence that any employment action taken against a whistleblowing employee would
have been taken in the absence of such conduct. Now more than ever, proper documentation of performance, misconduct, or other employment issues with an employee is extremely important because such an employee may attempt to avoid unfavorable employment actions by making covered complaints.

• Most importantly, if you are involved in terminating an employee who has complained about securities fraud or other related matters, obtain legal advice before acting. For years, employment attorneys have been handling retaliation and wrongful discharge claims, dealing with federal agencies such as the DOL, and creating and implementing policies to bring employers into compliance with federal and state laws. Consequently, employment attorneys are particularly well-suited for providing guidance and defending claims brought under the whistleblower provisions of the Sarbanes-Oxley Act. However, employers and their attorneys must be particularly cautious because of the potential criminal penalties involved.

B. A Note About Record Keeping And Destruction

As explained above, the Act makes it unlawful not only to destroy or conceal a document, but also to falsify or make a false entry in a document. Further, the broad definition of the word “document” could encompass anything that might be relevant to an EEOC charge, a wage and hour investigation, or an unfair labor practice charge.

Companies would be well-advised to have legal counsel examine their existing document retention policies and to update the policies in accordance with the new mandates of the Sarbanes-Oxley Act. As always, employers should also comply with the record-keeping requirements under already existing federal and state employment laws. However, when an employee has blown the whistle, the employer should be exceedingly careful about destroying any documents that could relate to the employee. Employers should also exercise extreme caution in creating any documents that relate to the employee after the whistleblowing has occurred because the Act makes it unlawful for an employer to falsify or make a false entry in a document.

Another danger faced by employers under the Act involves the possibility that the employer could be required to defend two simultaneous proceedings related to the same employee before two different federal agencies at the same time. For example, a whistleblower could file a Charge of Discrimination under Title VII with the EEOC, and file a separate claim under the Sarbanes-Oxley Act with the DOL alleging that the employer filed a false statement of position to the EEOC or destroyed documents relevant to his claim. If the EEOC issued a right to sue letter and if the DOL did not act timely, the employee could potentially have two cases at the same time in two different forums. This threat may provide an employee with leverage in obtaining a settlement from the employer.

C. Anonymous Reporting

Another provision of the Sarbanes-Oxley Act, Section 301, requires publicly traded companies to establish an audit committee for employees to anonymously report concerns about questionable accounting or auditing matters. Specifically, the statute states as follows:

Each audit committee shall establish procedures for (A) the receipt, retention, and treatment of complaints received by the issuer regarding accounting, accounting controls, or auditing matters; and (B) the confidential, anonymous submission by employees of the issuer of concerns regarding questionable accounting or auditing matters.

15 U.S.C.A. § 78j-1(m)(4) (West 2002). Any publicly traded company that fails to implement the audit committee and the appropriate anonymous reporting system by April 26, 2003 will be delisted from the exchange. Id. at § 78j-1(m)(1)(A).

Publicly traded companies that have existing employee hotlines may be able to use their existing hotlines for this purpose. However, the final decision regarding the appropriateness of a hotline for this purpose will be left to the audit committees. Many employers who have or implement hotlines could find that, at some point and regardless of their stated intent, hotlines become a place for employees to vent general employment-related complaints. Thus, some employee complaints that have nothing to do with corporate fraud or accounting practices may surface through the hotline. Consequently, employers should make sure that non-fraud complaints are sent to the appropriate corporate department, such as human resources, for handling.

D. Conclusion

Most, if not all, employers will seek to comply with the Sarbanes-Oxley Act and to treat employees fairly. However, with any termination involving any employee who has made any complaint that could even arguably fall within the provisions of the Act, the employer must exercise extreme caution to ensure that the termination is not retaliatory. Importantly, just because an employee is a whistleblower does not mean that the employee is excused from complying with the employer’s reasonable policies and procedures. The key is to have policies in place, to strictly follow the policies, and to make sure that the whistleblowing employee is not treated differently than other similarly situated employees.
III. VIEW FROM THE EMPLOYEE’S PERSPECTIVE BY JOSEPH Y. AHMAD AND AMIR H. ALAVI

The purpose of this section of the paper is to discuss the Sarbanes-Oxley Act from the employee’s perspective.

Protection for private sector whistleblowers in Texas is long overdue. The Texas Supreme Court has consistently refused to create an exception to the at-will doctrine for private-sector employees. *Austin v. HealthTrust, Inc.*, 967 S.W.2d 400 (Tex. 1998) (refusing to create a cause of action for private whistleblowers).

The Texas legislature seems unconcerned with corporate ethics. Even with all the attention focused on Enron and alleged ethical lapses by other Texas companies, the Texas legislature has failed to pass legislation protecting private sector whistleblowers. The chances for any legislation in the future are slim to none.

In that context, the Sarbanes-Oxley Act is welcome relief for Texas employees. Before Sarbanes-Oxley, whistleblowers in Texas had no protection from retaliation unless they refused to perform an illegal act or were protected by other federal whistleblower statutes. *See, e.g., Sabine Pilot*, 687 S.W.2d 733 (recognizing an exception to at-will employment when an employee is terminated for refusing to perform an illegal act); 42 U.S.C. § 5851 (whistleblower provisions under the ERA); 29 U.S.C. § 1140 (whistleblower provisions under ERISA).

The Sarbanes-Oxley Act, however, is far from a panacea for those who believe that protection for whistleblowers is a key ingredient to reforming corporate governance. Although the Act provides some protection for private sector employees, it is incomplete. Private companies, significant employers in Texas, are not covered by the Act. 18 U.S.C. § 1514A(a) (limiting coverage to companies “with a class of securities registered” under the Securities and Exchange Act of 1934). As a result, a number of employees simply have no protection under the Act.

The Sarbanes-Oxley Act is also limited in that it is primarily concerned with improper conduct that are covered by laws governing securities fraud. Unless the employer’s alleged conduct potentially violates federal mail fraud, wire fraud, bank fraud, securities fraud, an SEC rule, or any federal law relating to fraud on shareholders, the Act does not apply. 18 U.S.C. § 1514A(a)(1)-(2). Although the coverage may be extensive, as discussed below, not all improper or even criminal conduct is necessarily covered.

A. When Is A Whistleblower Protected

To qualify as a whistleblower under The Sarbanes-Oxley Act, an employee is faced with two hurdles. First, the Act is limited to certain types of conduct by the whistleblower. Second, the Act is also limited to alleged violations of certain enumerated federal securities and fraud laws.

1. Protected Conduct By The Employee


As a practical matter, Section (a)(1) of the Act provides employees with the most protection. This provision provides employees with recourse if they are retaliated against for providing information or assisting in an investigation of conduct that the employee reasonably believes is a violation of federal mail fraud, wire fraud, bank fraud, securities fraud, any SEC rule or regulation, or “any law relating to fraud against shareholders.” Section (a)(2), on the other hand protects employees who participate in a proceeding regarding alleged violations of the same laws. Even without the Sarbanes-Oxley Act, it is the rare employer who will retaliate against an employee who participates or testifies in a criminal or civil proceeding. Most retaliation claims arise when an employee either reports misconduct to management or to the authorities.

In that practical sense, Section (a)(1) provides employees with significant protection by covering the majority of ways in which an employee might report misconduct. The Act protects not only employees who report to regulatory agencies, law enforcement agencies, and Congress, but also those who report to management within the company. The Act specifically protects employees who report alleged misconduct to their supervisor or any person who has the authority to investigate, discover, or terminate misconduct. In many companies, this will include most members of management, the human resources department, and the legal department.

2. Limitation Of Whistleblower Coverage To Specific Violations Of Federal Law

Whistleblower coverage under the Sarbanes-Oxley Act is further limited to a company’s alleged violations of enumerated federal fraud and securities laws. The types of wrongdoing that fall within the Act’s coverage are potentially broad. Sections (a)(1) and (a)(2) specifically include fraud statutes covering mail fraud, wire fraud, bank fraud and securities fraud in the Act’s coverage. In addition the Act covers any violation of SEC rules and regulations or “any law relating to fraud against shareholders.”

These last provisions cover significant ground. For example, Section 13 of the Securities Act of 1934, a
law that is potentially covered by the Sarbanes-Oxley Act, contains the following provisions:

(2) Every issuer which has a class of securities registered pursuant to section 12 of this title and every issuer which is required to file reports pursuant to section 15(d) of this title shall—

(A) make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer; and

(B) devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that—

(i) transactions are executed in accordance with management’s general or specific authorization;

(ii) transactions are recorded as necessary (I) to permit preparation of financial statements in conformity with generally accepted accounting principles or other criteria applicable to such statements, and (II) to maintain accountability for assets.

** **

(5) No person shall knowingly circumvent or knowingly fail to implement a system of internal accounting controls or knowingly falsify any book, record, or account described in paragraph (2).


A violation of Section 13 could include simple matters such as a manager hiring a relative in violation of company policy or circumventing the company’s travel policy for personal gain. It can also encompass criminal conduct such the payment of bribes to government officials. See e.g., In re Baker Hughes, Inc., Exchange Act Release No. 44,784 (SEC Sept. 12, 2001) (finding that bribes to government officials violated Section 13). Materiality appears not to be an issue as a misclassification of payments as low as $10,000 have been found to violate the statute. Id. (finding that a $15,000 to an agent that may or may not have gone to a government official and was not properly recorded in the company’s books violated Section 13); id. (finding that a $10,000 to an agent that may or may not have gone to a government official and was not properly recorded in the company’s books violated Section 13).

In connection with Section (a)(1), the Act does not require that the employee report an actual violation of any law. Instead, the Act only requires that the employee have a reasonable belief that the company’s conduct violate one of the enumerated laws. 18 U.S.C. § 1514A(a)(1). The reasonable belief requirement eliminates the need to prove an actual violation of any law. Instead, the focus will be on the employer’s conduct towards the employee and the purported legitimate reasons for that conduct.

B. Individual Liability

An important consideration for employees is that the Act imposes liability not only on the employer but also on “any officer, employee, contractor, subcontractor, or agent” of the employer. 18 U.S.C.A. § 1514A(a). In the event that courts decide to impose the affirmative defense (in claims where no tangible employment action has occurred) provided to employers under Faragher and Ellerth, individual liability for decision makers takes the sting out of such a decision. Faragher v. City of Boca Raton, 524 U.S. 775 (1998); Burlington Indus., Inc. v. Ellerth, 524 U.S. 742 (1998). While the company may be able to avoid liability, a decision maker, who most likely is indemnified by the employer, will not.

C. Pitfalls For Employees

The Sarbanes-Oxley Act is not without pitfalls for employees and the lawyers representing them.

The short statute of limitations in the Act creates a difficulty for employees. The statute of limitations for a civil whistleblower action is ninety (90) days from the date the alleged violation occurred. 18 U.S.C. §1514A(b)(2)(D). In today’s environment, where whistleblowers are prominently in the news, ninety days is enough time for an employee to decide to see a lawyer, meet with a lawyer, and file a complaint. Historically, however, discharged employees have been hard pressed to meet even longer statute of limitations. Only time will tell whether the statute of limitations under the Act is appropriate or far too short.

The administrative procedure in the Act presents another difficulty for employees. Unless the DOL fails to issue a decision within one hundred eighty (180) days of the employee’s complaint, an employee is not entitled to pursue their claim in federal district court. 18 U.S.C. § 1514A(b)(1)(B). The standard administrative process culminates with a trial on the merits in front of an ALJ. See Section I.A.3.d., supra. Given the choice between a jury trial and a bench trial, most lawyers representing employees would choose the former. Here, employees have no choice. In the event that the ALJ rules against the employee, the standard of review on appeal is abuse of discretion and unsupported by substantial evidence. 5 U.S.C. § 706 (setting standard of review); 49 U.S.C. 42121(b)(4) (providing that appellate review shall conform to the standards of 5 U.S.C. § 705); 18 U.S.C. 1514A(b) (providing that an action under the Act will
be governed by the procedures set forth in 49 U.S.C. 42121(b)).

Another concern is the potential interpretation by the Courts. Specifically, employees will have to guard against State Courts interpreting the Act similar to The Public Sector Whistleblower Statute, Tex. Gov’t Code Ann. §554.001, et seq. (1994). The Texas Supreme Court has issued several opinions favorable to employers under this statute, but this should not be considered controlling authority for a federal statute. Moreover, Sarbanes-Oxley is clearly designed to provide more protection to employees than the Texas Whistleblower Statute. Also, I believe the Courts will apply a McDonnell Douglas burden shifting approach to the Act and that approach has at least proved moderately workable in the Title VII content and there is no reason why it should not apply similarly to the Sarbanes-Oxley Act. One important distinction from Title VII jurisprudence, however, is that Sarbanes-Oxley specifically provides that for an employer to escape liability despite evidence sufficient to raise an inference of retaliation, an employer must provide clear and convincing proof the it would have taken the same action against the employee even if the employee had not engaged in conduct protected by Sarbanes-Oxley. Since this is a rather stringent burden on the employer, this language should be emphasized in every claim under the Act, if nothing else other than to emphasize Congress’ intent to provide broad protection for the employee.

D. Conclusion

The Sarbanes-Oxley Act is a good starting place for a comprehensive attempt to reform the way in which corporate whistleblowers are protected. Its potentially broad coverage will afford employees of publicly traded companies with significant protection that has been lacking in the past.

IV. FINAL WORD

Unfortunately, when employers hear a reference to the Sarbanes-Oxley Act, they may incorrectly think “corporate fraud problem,” “publicly-traded company problem,” or “CEO problem.” Hopefully, this paper has reiterated the need to think of the Act at least in part as “an employment problem,” “every company’s problem,” and, potentially, “your problem.”