



**Wednesday, October 22**  
**11:00 am-12:30 pm**

## **903 How to Survive a SOX Whistleblower Complaint**

**Roscoe C. Howard Jr.**

*Partner*

Troutman Sanders LLP

**Tanya Axenson Macallair**

*Counsel for Human Resources*

Constellation Energy Group

**Dean A. Manson**

*Senior Vice President, General Counsel, and Secretary*

Hughes Communications, Inc.

## Faculty Biographies

### **Roscoe C. Howard Jr.**

Roscoe Howard, Jr., is a partner at Troutman Sanders, LLP in Germantown, Maryland.

He is the former United States Attorney for the District of Columbia, has prosecuted or directed civil and criminal litigation for most major federal agencies, including the Securities Exchange Commission (SEC), Department of Homeland Security, Department of Treasury, Environmental Protection Agency (EPA), and Department of Labor. Over his thirty-year career, Mr. Howard has tried over 100 cases as a federal prosecutor and has handled matters for the Department of Justice (DOJ) and two independent counsels in both federal court, and the District of Columbia Superior Court. Mr. Howard's vast experience as a prosecutor gives him specific knowledge of the federal government's strategies and tactics, providing valuable insights and advice for clients. He has directed internal investigations and provided advice to corporate boards of directors, audit committees, and company executives.

Mr. Howard is a member of the board of directors, Canada-US Fulbright Program; a member of the board of directors, Roger Williams University School of Law; and a member of the editorial board of the National Law Journal.

He earned his JD from the University of Virginia School of Law, his AB from Brown University, and attended Culver Military Academy, Culver, Indiana.

### **Tanya Axenson Macallair**


Tanya Axenson Macallair is human resources counsel for Constellation Energy Group in Baltimore, Maryland.

Prior to joining Constellation, Ms. Macallair was an associate in the labor and employment group at Gibson, Dunn & Crutcher in Washington, DC.

Ms. Macallair is a graduate of Harvard Law School and Cornell University.

### **Dean A. Manson**


Senior Vice President, General Counsel, and Secretary  
Hughes Communications, Inc.



## Sarbanes-Oxley Act "SOX"

Provides Whistleblower Protection for Employees of Publicly-Traded Companies

- those that sell stock



## Purpose of SOX

- To clean up corporate fraud after problems in companies like Enron, Arthur Anderson, Tyco, Global Crossing & World Com
- Corporate managers must create tight controls over financial reporting, evaluate their effectiveness regularly, and have outside auditors do the same

ACC Association of Corporate Counsel

### What Does SOX Mean ...

Every business must have:

- Internal controls
- Every control needs a written set of procedures; and
- There must be a sampling of actual business operations against the controls

ACC Association of Corporate Counsel

### Protected Activity

- provide information
- cause information to be provided
- or otherwise assist in an investigation

regarding any conduct which the employee reasonably believes constitutes . . .

ACC Association of Corporate Counsel

### Whistleblower Protection

Makes it illegal to discriminate against an employee for providing information, or assisting in an investigation, regarding what the employee "reasonably believes" to be a violation of an SEC rule;

federal mail, wire, and bank fraud laws; or any provision of federal law relating to fraud against shareholders

ACC Association of Corporate Counsel

### Prohibited Activity Subject to Reporting

- a securities violation
- or violation of any provision of Federal law relating to fraud against shareholders
  - Securities fraud is attempting to obtain by false representations or promises any money or property in connection with the purchase or sale of securities (stock)
  - To make any untrue statement of a material fact or to omit a material fact from required reports



### Prohibited Activity Subject to Reporting

- mail, wire, or bank fraud
  - Federal law prohibits using mail, wire or bank systems to commit fraud
  - “Wire” encompasses transmission by telephone, telegram, facsimile, television, and email in interstate commerce
  - Fraud is any scheme to obtain money or property by false representations or promises



### What is a Reasonable Belief?

#### **Objective/Subjective Reasonable Belief**

*A belief that an activity was illegal may be reasonable even when subsequent investigation proves a complainant was entirely wrong.*

*The accuracy or falsity of the allegations is immaterial; the plain language of the regulations only requires an objectively reasonable belief that shareholders were being defrauded.*



### Protected Activity

- Relationship to Public Financial Reporting
  - financial statements/required SEC filings
  - not include violations of internal policy
- Materiality
  - having real consequences on corporate finances
- Reporting Within Normal Job Duties
  - split of authority on whether reporting activities in the normal course of job duties is SOX-protected



### SOX Case Law

- SOX protects “all good faith and reasonable reporting of fraud” even where the plaintiff’s complaint is not directly related to securities or accounting fraud. *Collins v. Beazer Homes, USA, Inc.*, 334 F. Supp. 2d 1365 (N.D. Ga. 2004)
- Most cases under SOX involve the termination of the whistleblower; however, one court has held that a loss of job responsibilities “was a sufficient change in employment conditions within the meaning of the Act.” *Willis v. Vie Financial Group, Inc.*, 2004 U.S. Dist. LEXIS 15753 (E. Pa. 2004)

ACC Association of Corporate Counsel

### Penalties for Violations

Individuals:

- Up to 20 years in jail
- Up to a \$5 million fine
- SEC can also bar anyone it determines “demonstrates unfitness” from serving as an officer or director of a public company

ACC Association of Corporate Counsel

### SOX Whistleblower?

The law does not “provide whistleblower protection for all employees complaints about how a public company spends its money and pays it bills.”

ACC Association of Corporate Counsel

### Penalties for Violations


Corporations:

- Up to \$25 million fine

ACC Association of Corporate Counsel

### SOX Whistleblower?


Employee complains about indoor air quality.

 *Not a SOX whistleblower because the law was “enacted to address the specific problem of fraud in the realm of publicly traded companies and not the resolution of air quality issues, even if there is a possibility that poor air quality might ultimately result in financial loss.”*

ACC Association of Corporate Counsel

### SOX Whistleblower?


Employee complains about the collection of markdown allowances from vendors and the accounting for the value of inventory.

 *SOX whistleblower, even though employee had no accounting background and no knowledge of the company's accounting practices, because company had treated the complaints as reasonable enough to have warranted internal investigation—company “understood the nature of employee's allegations.”*

ACC Association of Corporate Counsel

### SOX Whistleblower?


HR employee complains about a fraudulent insurance scheme when supervisor adds ineligible individuals to company-provided health insurance as dependents and that supervisor provided a fake social security card for an employee in order to satisfy the I-9 requirements of the immigration law.

 *SOX whistleblower because the law clearly protects an employee against retaliation based upon that employee's reporting of mail fraud or wire fraud regardless of whether that fraud involves a shareholder of the company.*

ACC Association of Corporate Counsel

### SOX Whistleblower?

Employee complains that significant numbers of its batteries were defective.

 *Not a SOX whistleblower because the complaint “does not address any kind of fraud or any transactions relating to securities” nor did it allege “intentional deceit that resulted in a fraud against shareholders or investors.”*

ACC Association of Corporate Counsel

### Not just an HR issue...

- Company must investigate alleged securities violations
- Multiple government agencies
- Multiple legal issues



### § 307 Special Rules for Lawyers

- Required to report credible, material evidence of violations
- Report to Chief Legal Counsel or Chief Executive Officer
- Once reported, attorney and CEO/CLC must decide to fully investigate allegations
- If the attorney believes the company has not appropriately responded, he/she must report the evidence to the Audit Committee of the Board of Directors or the Board of Directors



### OSHA's Role in SOX

- Complaints are filed with OSHA via the Secretary of Labor
- OSHA conducts investigation, including meeting with employer and determining whether or not there is cause to believe that there was a SOX act violation



### Working With OSHA

- SOX complaints are handled by OSHA investigators
- Need to work with OSHA on complex issues of financial fraud – a possibly new area
- Evolving area of law regarding covered entities, scope of protected activity, etc.



### Burden of Proof Under § 806 of SOX

Plaintiff's *prima facie* case of discrimination must show by a preponderance of the evidence that:

- (1) the employee engaged in protected activity;
- (2) the employer knew of the protected activity;
- (3) the employee suffered an unfavorable personnel action; and
- (4) circumstances exist to suggest that the protected activity was a contributing factor to the unfavorable action. *Collins v. Beazer Homes, USA, Inc.*, 334 F. Supp. 2d 1365, 1375 (N.D. Ga. 2004)



### Administrative Procedures

- Complaint filed with the Secretary of Labor within 90 days of discrimination
- Secretary then notifies the person named in the complaint
- Employer has 20 days after the complaint is filed to meet with OSHA representatives and give evidence in its favor



### Administrative Procedures

- Secretary of Labor must issue a final decision within 180 days
- If the Secretary fails to do this, the claimant may bring an action at a law or equity for *de novo* review in the appropriate U.S. District Court



### Administrative Procedures


- If OSHA believes the employer may have violated the SOX act, OSHA informs the named person
- That person then has 10 business days to give written evidence in response to the allegations, meet with investigators, and present arguments why preliminary relief is not warranted




### Methods of Handling Complaints

- Anonymously, but this may inhibit ability to investigate
- Company's Corporate Compliance Policy
- Use of internal audit, external auditors, local lawyers
- Note that failure to report a violation may subject you to discipline, including termination




 **Conducting An Investigation**

- Does the company have established procedures?
- If not, need to discuss and establish procedures with Company's directors

 **Conducting An Investigation**


First Concern:

- In-house, or
- Outsource to Independent Agency
- What will in-house counsel's involvement be? How does this affect privilege?

 **Conducting An Investigation**

18 U.S.C. § 1519 – Data preservation:

- Companies can face severe fines as well as other penalties for destroying, altering, concealing, or falsifying documents
- Imperative that the Company implement a preservation policy to retain data immediately

 **Conducting An Investigation**

An Effective Investigation:

- Gathers and preserves relevant evidence
- Conducts interviews with staff and management
- Compile results of investigation in neutral, logical manner



### Conducting An Investigation

#### An Effective Investigation Continued:

- Subject results of investigation to competent evaluation
- Protects confidentiality of sources and preserves results
- Ensures whistleblower is not retaliated against
- Produces fair and informed results and takes corrective action where necessary



### Protecting the Company's Information

- Documents (position statement and exhibits) filed with the DOL may be subject to inspection under FOIA
- In order to protect privacy and sensitive information, redact any sensitive or confidential information (SSN#, trade secrets, etc.)
- Consider filing a protective order



### Writing A Position Statement

- Be truthful
- Be complete
- Be transparent
- Be compelling



### Instituting/Updating Compliance Program

#### Based on the results of the investigation:

- Update policies and procedures
- Implement remedial measures
- Educate and train employees
- Inform employees about resources available to aid them