

CORPORATE COUNSEL NEWS

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Virginia State Bar Corporate Counsel Section

<http://www.vsb.org/sections/cc/index.htm>

Don't Blame the Messenger: Establishing Accounting Complaint Procedures

By Margaret N. Rosenfeld

When Sherron Watkins of Enron came forward to blow the whistle on the company's questionable accounting practices, she did not have the protection of a federal fraud anti-retaliation law and Enron wasn't required to have internal accounting complaint procedures for her to follow. That has all changed with the passage of the Sarbanes-Oxley Act of 2002, which provides protection to employees of public companies who report actual or potential violations of federal fraud laws, Securities and Exchange Commission ("SEC") rules or regulations, or any other federal law relating to fraud against shareholders. Section 806 of the Act shields a whistle-blowing employee from retaliation such as termination, demotion, suspension, harassment or discrimination and provides

civil remedies for violations. Although the Act's provisions only apply to public companies, private companies may also want to consider complying with the provisions.

In tandem with Section 806, Section 301 of the Act directed the SEC to require the national securities exchanges (e.g. NYSE) and the national securities associations (i.e. Nasdaq) to require the audit committee of a listed company to establish procedures for the receipt, retention and treatment of complaints relating to all accounting, internal accounting controls, or auditing matters of a company, including procedures for the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters. The SEC has not mandated specific complaint procedures, recognizing that the

procedures for a very large company may not work for a small company, although it is possible that the NYSE or Nasdaq may mandate more specific procedures when the rules are finalized. Listed companies must have complaint procedures in place by the earlier of (1) their first annual meeting after January 15, 2004, or (2) October 31, 2004. This article provides some suggestions for you to consider in developing your company's complaint procedures.

Make a Strong Policy Statement Against Retaliation

Complaint procedures should begin with a policy statement from the company that promotes its commitment to open discussion of its business practices and its

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The Virginia State Bar Corporate Council Section will be sponsoring a CLE program entitled "An Update on the Do Not Call Act," at the VSB Annual Meeting on Friday, June 18, 2004 from 11:00 am to 1:00 pm. A panel of state and federal lawyers will provide an overview of the Act, the Federal Communications Commission and Federal Trade Commission rules implementing the Act, and the recent constitutional challenges filed in several federal courts.

The discussion will focus on how lawyers are advising their clients on compliance with the Act, how the Act or other legislation effects unsolicited faxes and emails, and provide an overview of the exemptions. Finally, the panel will discuss similar Virginia legislation and the line between state and federal regulations. ❖

VSB Annual Meeting 2004

By Jennifer Leigh
McClellan,
Verizon Corporation

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View from the Chair

by J. Philip Hart, Chair, Cornerstone Realty Group

As the 2003-2004 chair of the Virginia State Bar's Corporate Counsel Section, I am pleased to report that we are off to a good start this year. In September the Board of Governors completed our plan for the year, and since then we have been busy implementing the plan.

The Section is undertaking several new programs and projects. In October, we sponsored a CLE program with Squire, Sanders & Dempsey on the topic of "Ethics Issues for Corporate Counsel." In December, we sponsored another CLE in Northern Virginia at which speakers from Holland & Knight and Chubb Insurance Company spoke about potential legal liability of in-house attorneys

and insurance products available to afford some protection. We are also taking a fresh look at our section website with a goal of making "second generation" improvements to the website. If you haven't already done so, take a look at the website at <http://www.vsb.org/sections/cc/index.html> and let us how you think it could be made more useful to you.

This year the Corporate Counsel Section will also be continuing a number of activities that have been staples of the Section for years. We will hold our law school writing competition again in the spring, and we are re-doubling our efforts to increase participation. We will continue to

publish our Section newsletter, and we will sponsor annual luncheons for our members in May in Northern Virginia, Richmond, Hampton Roads and Roanoke. We will also sponsor a CLE program at the Virginia State Bar's annual meeting in Virginia Beach next June. The topic will be the "Do Not Call" law, which we are all discovering has wide implications for businesses and non-profits.

Thank you for being a member of the section. The Board of Governors is always glad to hear from our Section members, and you may call me directly at 804-643-1761.❖

Squire Sanders — Corporate Counsel Section CLE

On October 29, 2003, the Corporate Counsel Section co-sponsored a continuing legal education program with the law firm of Squire, Sanders & Dempsey L.L.P. Held at the Squire Sanders' Tysons Corner office, the CLE, titled "Ethics Update for the Corporate Counsel" focused on the new attorney ethical obligations under Sarbanes-Oxley and SEC Rules, the new Virginia registration rule governing in-house corporate counsel, and recent developments in the rules governing attorney ex parte communication with current & former corporate employees. There was no fee for attendees and the program was open to all members of the Corporate Counsel Section and in-house and outside counsel from the Washington D.C. metropolitan area.

Robert Webb, a partner with Squires Sanders with extensive experience providing counsel to businesses and handling

business and financial transactions, presented a discussion of Sarbanes-Oxley, the new SEC Rules, and the new attorney reporting requirements. He also discussed the new SEC Rules "Standards of Professional Conduct for Attorneys," the "up the ladder reporting" requirement, and explored possible disclosure obligations to SEC, the noisy withdrawal option, the role of the "Chief Legal Officer," the strengths and weaknesses of a "Qualified Legal Compliance Committee" (QLCC), and other related topics.

David Ross Rosenfeld, a member of the Corporate Counsel Section's Board of Governors, and a frequent speaker and prolific writer on the subject of attorney ethics and professional responsibility, spoke on the Virginia's new corporate counsel rule, ex parte communications with current and former corporate employees, and lawyer discipline in Virginia. ❖

Mark Your Calendars

February 15, 2004 – Submission deadline for entries for the Annual Corporate Counsel Law Student Writing Competition

February 17, 2004 – George Mason University Law School Career Program sponsored by the Corporate Counsel Section

May 20, 2004 – 10th Annual Corporate Counsel Luncheon, Northern Virginia, Norfolk, and Richmond

June 18, 2004 – State Bar Annual Bar Meeting, Corporate Counsel program "Do Not Call!"

NOTE – In previous years, CLE attendance forms were available on tables outside the meeting rooms. However, this year, to ensure compliance with the Bar's policy that only paid registrants at the Annual Meetings receive CLE credit for attendance at seminars and workshops, CLE forms will be included in the packets that are given to paid attendees at the time of registration.

In-Source Your Contracts

By Eileen Morgan Johnson, General Counsel, National Wildlife Federation

Some in-house departments out-source their work when they have too much to handle in-house. You can save money on outside counsel bills by "in-sourcing" contracts to other staff in your company. Your clients are able to take on more of the responsibility for contracts than you might think.

When working with your clients, you need to understand their expectations in terms of your level of involvement in contract negotiation and drafting. Are you training them to handle the contract process from soup to nuts without any legal oversight? Or are you preparing them to do an initial draft and negotiation with the fine tuning to be provided by you?

You need to know your client's level of expertise with contracts. Do they understand contract terminology? Do they know their business and the industry standards? Do they have experience with things that have worked or not worked before? Do they have a history with the other party? You are in the strongest position as a team when your clients know their business and what needs to be accomplished and you can help them figure out the best way to get there.

Once you are familiar with a client's particular business and level of expertise, you may be able to turn over contract negotiation and some (if not all) of the drafting to the client. Your client will understand the contract better if they are the one responsible for negotiating and drafting it. You can work with your client to identify what role you need to play in reviewing the contract and identifying areas not covered in their draft before it is signed.

Not all of our clients are able to negotiate or draft their contracts. You need to assess each client and their ability to handle contract drafting and negotiation before turning that responsibility over to them. Your level of involvement in the contract development process will depend upon the client's contract experience and the value of the contract.

Sometimes we forget that our job is not to draft the best contract ever but to serve the needs of our client. Given the right tools and time, we could all draft brilliant, airtight, model contracts. But is that what our clients need? It is often difficult for attorneys to let go, but sometimes the sheer lack of resources forces you to do this. Maybe your client would not word the information in the contract the same way you would, but that is probably okay. Did they get their point across? Is it clear and unambiguous? Would someone not familiar with the negotiations understand what is meant? If you can answer yes to those questions, then while it may not be perfect, it is just fine. Not every contract needs to be great. Sometimes good will do just as well as perfect.

Most companies that allow people other than attorneys to negotiate or draft contracts employ one or more of these training methods:

- Classes or seminars taught by members of the law department covering the basics of contract law or focusing on specific subjects such as negotiations.
- Outside programs at training centers or community colleges where an employee takes a one to two day class and learns the basic elements of contract law, negotiating and drafting.
- Form contracts distributed by a company's intranet, employee manual or other means.
- Checklists to assist staff in making sure they cover all of the required elements in reviewing contracts.
- Informal training or mentoring when an attorney works with a non-attorney on a contract.

You provide informal contract training each time you explain to a client the pros and cons of a particular contract provision. When giving contract advice, you should explain why you are recommending a particular course of action. The why is very important. They will not learn why choice A is better than choice B unless you provide that background information to them. That is part

of the learning process your clients go through as they start to negotiate contracts.

You can help your client by asking questions to clarify their intent. Are they entering into a new contract, trying to modify an existing one, or anxious to terminate an unsatisfactory vendor in favor of a new one? Once you know what the problem is, ask them some simple questions. What are they trying to accomplish? What is the end goal? Sometimes clients get caught up in jargon and it's not clear what their goal is. Once you know the problem(s) and the goal(s), you can help them solve the problem and meet the goal. As you help them ask the right questions, you are informally training them to analyze their contractual problems.

Once you know the client's goals, you can help draft a checklist that he or she can use with the existing contract and all future contracts. A checklist will help the client analyze any contracts received from vendors and it will help you in working with the client to draft or review contracts. By using a checklist, you can identify what terms might be missing in a contract and compare the proposed language, if any, against your standard contract terms. This will help you both to achieve a simple but complete contract that addresses your client's business needs and your legal needs.

One of our senior staff member with whom I have worked on contracts for many years recently gave me this advice on working with clients: "Don't underestimate how naïve we can be about things that can go wrong." You may turn over some or all of the negotiation or drafting responsibilities, but it is still up to you to spot the potential problems and use your legal knowledge to solve them. ❖

Ms. Johnson is General Counsel, National Wildlife Federation located in Reston, Virginia and a member of the Board of Governors of the Virginia State Bar Corporate Counsel Section.

Don't Blame the Messenger *(continued from page 1)*

stance against retaliatory action for certain whistle-blowing activities. A sample policy statement follows:

The Company encourages its employees to report [to the Company's compliance officer][as specified in this policy] any concerns they may have about accounting, internal accounting controls, or auditing matters of the Company. The Company will investigate promptly any questionable accounting or auditing matters brought to its attention by an employee. No employee shall be subject to discipline or retaliatory action by the Company or any of its employees or agents as a result of submitting a report or participating in an investigation under this policy.

The complaint procedures then should describe the scope of the matters covered by the procedures.

Decide How to Delegate Responsibility for the Complaint Procedures

The audit committee of a listed company will have the ultimate responsibility in adopting and overseeing the complaint procedures, but it would be impossible for a company's audit committee to handle the day-to-day administration of the complaint procedures. Therefore, companies should consider appointing a compliance officer who is responsible for administering the complaint procedures. The compliance officer would be responsible for receiving, retaining and investigating any complaint reports and providing a report at each meeting of the audit committee. A company may consider appointing its general counsel or another in-house attorney as the compliance officer in order to preserve any attorney-client privilege that may be available. If a company does not have any in-house

lawyers, it may be appropriate to designate an executive officer (i.e. the CFO) as the compliance officer.

Establish Multiple Channels for the Receipt of Complaints

Companies will need to determine how complaints will be received. The SEC is concerned that audit committees are dependent upon management for their information about business practices and believes management often may not have the incentives to self-report all questionable practices to the audit committee. All complaints should ultimately reach the audit committee level for consideration. Therefore, a company may want to design its complaint procedures to provide employees with multiple channels for reporting complaints to encourage open and effective communication to the audit committee. An employee should be encouraged to raise concerns with his or her immediate supervisor in the first instance. The supervisor then would inform the compliance officer of the complaint report. When this is not possible, for example, where the supervisor's conduct is being complained of, the complaint procedures should allow the employee to make a complaint report directly with the compliance officer. If the employee is uncomfortable reporting his or her complaint to the designated compliance officer, the company may want to consider designating a member of the audit committee to receive complaints. These reporting channels also can be used to allow an employee to report any retaliatory action he or she believes has been taken because of a complaint report he or she made.

Companies also are required to provide confidential and anonymous methods for the submission of concerns. Companies may want to consider providing one of more of the following:

- A locked drop box where employees can leave written complaint reports

- A secure intranet site where employees can send and receive anonymous emails
- A telephone voicemail hotline that does not record caller-identification information

If an employee submits a hand-written complaint, upon its receipt, the complaint report should be typed and the typed version should be used for the investigation of the complaint report to ensure that the employee is not identified by his or her handwriting. When an anonymous report involves an employee who is uncomfortable reporting in person to the compliance officer, the company should evaluate whether its complaint procedures should require the compliance officer to first receive such anonymous complaints or should require such anonymous complaints to be directly escalated to the audit committee or an audit committee designee.

Create a Specific Plan of Investigation for Each Complaint

Once a complaint is received, there should be established procedures for the investigation and resolution of the complaint report. A supervisor who receives a complaint report should not commence an investigation of the complaint report, but should give the report to the compliance officer or the audit committee designee if the complaint report involves the compliance officer. A specific plan of investigation should be tailored for each complaint by the compliance officer or the audit committee designee, as the case may be, rather than forcing the investigation of a complaint to conform to detailed standard investigation procedures. Certain review safeguards should be included in each plan, such as a request that the person lodging the complaint be interviewed (if not anonymous), that reasonable efforts be made to keep the name of the individual lodging the complaint as confidential as possible (to limit

chance of retaliation later) and that a written report of the investigation be prepared. In addition, a specific plan of investigation may include engaging independent advisors such as an accountant or legal counsel or may require a special meeting of the audit committee. A company may want to consider requiring that the compliance officer or the audit committee designee, as the case may be, provide the audit committee with a formal, written report about the complaint and the status of the investigation at each audit committee meeting. The compliance officer or the audit committee designee, as the case may be, should keep written records of all communications and reports concerning the complaint and the audit committee minutes should reflect the discussion of any complaints.

Create an Atmosphere That Does Not Tolerate Retaliation

A company's code of ethics should include a clear prohibition against any reprisal or retaliation, such as the statement included in the sample policy statement above. In order to monitor whether the complaining employee is being subjected to reprisals or retaliation, the compliance officer, an audit committee designee, or a specially designated member of a company's human resources staff, as the case may be, may from time to time contact the employee

to determine whether any changes in the employee's work situation has occurred as a result of his or her complaint report. Examples of reprisal or retaliation are:

- Denial of adequate staff to perform duties
- Frequent staff changes
- Frequent and undesirable office changes
- Refusal to assign meaningful work
- Unwarranted and unsubstantiated letters of reprimand or unsatisfactory performance evaluations
- Demotion
- Reductions in compensation
- Denial of promotion
- Suspension
- Dismissal
- Supervisor or superior encouraging co-workers to behave in a hostile manner toward the employee

A company's human resources staff should be kept up-to-date on the developments in this area and may need to become involved in investigations or in follow-up with the person lodging complaints.

When a company first implements the policy statement and complaint procedures or revises existing procedures, the company may consider holding educational meetings for its employees to discuss the policy statement and complaint procedures. In addition,

a company may consider holding an annual training session for its supervisors to explain the complaint procedures, the responsibilities of the supervisors and the non-retaliation policy. In addition, whenever a new supervisor is promoted or hired by a company, such new supervisor should have an individualized training session.

Get Started Now and Don't Forget to Review the Procedures Annually

Although the SEC has not specified the particular complaint procedures that companies must adopt, it is likely that a practice consensus will develop over the next year as to the content of the complaint procedures. The compliance officer of a company should consider reviewing the complaint procedures on an annual basis, evaluating the effectiveness of the procedures, as well as comparing the procedures to the procedures of other public companies (where available), and preparing a report to the audit committee with his or her recommendations for any changes or additions to the complaint procedures. ❖

© 2003 Ms. Rosenfeld is an attorney with the law firm of Smith, Anderson, Blount, Dorsett, Mitchell & Jernigan, L.L.P., 2500 Wachovia Capitol Center, Raleigh, North Carolina 27601.

Help Needed! - Swearing In of In-House Corporate Counsel

by David Ross Rosenfeld

Under the Virginia Supreme Court's revision to Rule 1A:5, by July 1, 2004, all in-house attorneys working in Virginia who are not full-fledged members of the Virginia State Bar must become licensed by the Bar by July 1, 2004. The new rule creates two categories: certification and registration. However, those attorneys opting for certification must be sworn in

before the Supreme Court of Virginia in Richmond and will need a sponsor to appear on their behalf.

Presently, dates assigned by the Court for swearing in ceremonies are April 12 - 16, 2004, June 7 - 11, 2004, and Sept. 13 - 17, 2004. These ceremonies usually take place at the beginning of each Court session and last from approximately 8:30 a.m. to 9:30 a.m.

We anticipate there will be a need for local attorneys to sponsor in-house attorneys during these swearing in ceremonies. If you would be willing to help, please send your name, telephone number and e-mail address to Dolly Shaffner, Virginia State Bar, 707 E. Main St., Ste. 1500, Richmond, VA 23219 or e-mail her at Shaffner©,vsb or call Dolly at 804-775-0514. ❖

Same Old, Same Old: Virginia's Amendment to Rule 1.13

by David Ross Rosenfeld

While congressional pundits and corporate watchdogs throughout the country clamor to impose greater responsibility on attorneys for the ethical conduct of corporate management, Virginia's revision of Rule 1.13 of the Rules of Professional Conduct demonstrates little movement in this direction.

Prior to January 2004, Virginia's Rule 1.13 followed and was identical to the Rule 1.13 of the American Bar Association's Model Rules of Professional Conduct. That rule provided that when corporate counsel obtained information that a person within the organization was violating, or intended to violate the law in a way that would likely "result in substantial injury to the organization," that attorney, while being required to "proceed as is reasonably necessary in the best interests of the organization," was simply limited in options to "asking reconsideration of the matter," requesting "a separate legal opinion," or "reporting up the ladder" within a corporation. And, as a final option, if all of these steps failed, the attorney could just resign.

Reflecting the waive of public opinion and the various pressures underlying Sarbanes-Oxley, in August, 2003, the American Bar Association adopted a significant revision to ABA Model Rule 1.13. Trumping the limitations and restrictions imposed by Rule 1.6 on the attorney communication of confidential client information, the ABA amended Model Rule 1.13 to permit but does not require corporate counsel to communicate as necessary with persons outside of the organization where corporate management either insists on or fails to timely address action that is clearly a violation of law that the lawyer believes is reasonably

certain to result in substantial injury to the organization.

Resisting similar change to Virginia's Rule 1.13, the Virginia Standing Committee on Legal Ethics declined to follow the ABA's lead. Virginia's Rule 1.6, the reasoned, clearly a) permits disclosure of client confidences where the attorney had information which "clearly establishes" the client's fraud on a third party during the course of, and related to representation. Rule 1.6 also mandates attorney disclosure of client confidences where the client i) has perpetrated a fraud on a tribunal during the course of, and related to representation, or ii) admits an intent to commit a crime in the future. Therefore, the Committee concluded, revising Rule 1.13 was unnecessary and recommend against any significant change to Rule 1.13.

The amendment to Rule 1.13 adopted by the Virginia Supreme Court and effective January 1, 2004, involved only a single technical change to subparagraph (b)(1), which was not intended to be substantive, but merely stylistic. Thus, when confronted with corporate management misconduct, although alternative courses of action may exist in other rules, the guidance provided to Virginia corporate attorneys by Virginia's Rule 1.13 remain traditional. ❖

Mr. Rosenfeld is a solo practitioner in Alexandria, Virginia providing ethics counsel to attorneys and corporate counsel. He is a member of the Corporate Counsel Section Board of Governors and editor of the Corporate Counsel Section Newsletter.

Editorial Policy

CORPORATE COUNSEL NEWS is published by the Virginia State Bar Corporate Counsel Section and is intended to provide information relating to law practice and management for the education and benefit of in-house counsel and others with similar interests. Statements or expressions of opinion or comments appearing herein are those of the editors, authors and contributors and should not be deemed as endorsed by the Corporate Counsel Section or the Virginia State Bar.

CORPORATE COUNSEL NEWS welcomes articles of interest to fellow members of the Corporate Counsel Section for publication in future editions.

Newsletter Editor

David Ross Rosenfeld

Rosenfeld@drrpc.com

(703-548-2600)

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CORPORATE COUNSEL SECTION

Corporate Counsel Section Board of Governors 2002-2003

J. Philip Hart

Chair

Cornerstone Realty Group
Richmond
(804) 643-1761
Fax: 782-9302
p.hart@termail.com

Lorrie J. Kleine

Immediate Past Chair

Norfolk Southern Corporation
Norfolk
(757) 629-2893
Fax: 629-2607
ljkleine@nscorp.com

Edward Henry Beck

Exxon Mobil Corporation
Fairfax

(703) 846-5877
Fax: (262) 313-9452
edward.h.beck@exxonmobil.com

Jennifer L. McClellan

Verizon Corporation
Richmond

(804) 772-1512
Fax: 772-2143
jennifer.l.mcclellan@verizon.com

Eileen M. Johnson

Vice Chair

National Wildlife Federation
Reston
(703) 438-6453
Fax: 438-6433
johnsone@nwf.org

David R. Rosenfeld

Newsletter Editor

David Ross Rosenfeld, P.C.
Alexandria
(703) 548-2600
Fax: 549-8664
rosenfeld@drpc.com

Douglas D. Callaway

Wachovia Securities (WF2216)
Richmond

(804) 787-6826
Fax: 344-6599
ddcallaway@wachoviasec.com

Scott E. Snyder

Chantilly
(703) 818-6930

Fax: 818-6931
scott.e.snyder@travelers.com

Darragh J. Davis

Secretary

Vista Information Technologies
Herndon
(703) 561-4149
Fax: 561-4332
darragh.davis@vistait.com

Greg E. Summy

Norfolk Southern Corporation

Norfolk
(757) 533-4890
Fax: 533-4872
greg.summy@nscorp.com

Edythe C. Katz

Severna Park, MD
(410) 975-9114

Fax: (301) 361-2510
edythe.katz@espire.net

Dolly Shaffner

VSB Liaison

Virginia State Bar
Richmond

(804) 775-0514
Fax: 775-0501
shaffner@vsb.org

Kathleen M. Kronau

Shenandoah Life Insurance Co.
Roanoke

(540) 985-4226 Fax: 857-5916
kathleen.kronau@shenlife.com

CORPORATE COUNSEL NEWS

Virginia State Bar

Eighth & Main Building
707 E. Main Street, Suite 1500
Richmond, VA 23219-2803

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