

Expanded Whistleblower Protections: The Steps Companies Should Take
Receive, Respect, Respond
by Steven H. Cohen, Cohen Law Group, Chicago
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Largely due to the Sarbanes-Oxley Act of 2002 (“SOX”), public companies have developed internal compliance programs to report securities, bank or wire fraud, and other fraud affecting shareholders. As a result, we have seen the beginning of corporate compliance transparency. The Dodd-Frank Act, passed in July 2010, presents yet a new channel for disclosing such fraud, by encouraging corporate whistleblowers to inform the SEC of alleged securities fraud violations that would otherwise not be reported by companies.

The Dodd-Frank whistleblower incentives should compel companies to do more than merely improve their internal compliance programs. Companies should take practical steps to (1) really listen to internal employee concerns; (2) respect the credibility of the employee’s information; and (3) genuinely respond to the employee’s concerns. By maintaining an employee’s loyalty during the internal process, companies will decrease their risk that the employee will go outside of the workplace to report fraud as a whistleblower.

Dodd-Frank Act Practicalities

In amending SOX, the Dodd-Frank Act rewards whistleblowers who provide the SEC with original, independent information of corporate fraud that leads to a recovery of \$1 million or more. The SEC can award the whistleblower up to 30 percent of the assessed sanctions. Dodd-Frank also expands the SOX anti-retaliation provisions.

SEC final rule-making, due in April 2011, will demonstrate how the SEC will implement the Dodd-Frank Act. Proposed rules give a hint to the limits and scope of the corporate whistleblower’s incentive to report corporate fraud. According to an SEC proposed rule, the whistleblower’s information must “significantly contribut[e] to the success of the action.” The whistleblower’s award may be denied if the information was obtained through an attorney-client privileged communication.

Finally, the whistleblower must first internally report the alleged fraud or securities law violation.

How the implementing regulations affect Dodd-Frank will likely be the subject of much litigation in the next decade. For example, notwithstanding the bar to an award based on information obtained through attorney-client privileged communication, an internal whistleblower reporting a Madoff-sized fraud may recover a sizeable award given the crime-fraud exception to the attorney-client privilege.

Practically, however, in most instances whistleblower-initiated cases will drive much of SEC enforcement actions in years to come. As health care providers learned during the last decade of Medicare and Medicaid anti-fraud enforcement activity based on the False Claims Act, employees with access to substantial evidence of fraud are well-positioned to enhance government investigations and to receive large awards for their contributions.

Our experience representing such employees in the False Claims Act context shows that these potential whistleblowers tend to be hardworking employees who start out loyal to their employer. They take the bold step of becoming a whistleblower because their principled concerns about what is going on in the workplace go unheeded within the corporate infrastructure. They also tend to see compliance issues starkly and adhere to a strong belief in corporate integrity. They blow the whistle because of their concern that others in the company are being dishonest and harming the company to which they have devoted their professional career. If the company ignores their concerns, or worse, retaliates against them for raising such concerns, they feel their own sense of loyalty has been betrayed and their own dedication to their company has been undermined. As Shakespeare observed, "Heaven has no rage like love to hatred turned, Nor hell a fury like a woman (or man) scorned."

Many whistleblowers have told their counsel that they only wanted to be heard, and responded to; hence the practical steps to "receive, respect, respond."

Receive

All compliance programs nowadays include an “open door” policy. More than that is needed. Top managers should initiate regular conversations with employees and ask about how programs are working, and whether the employees are concerned about how programs are working. Do not ask, “Do you think we are involved in any fraud or SEC violations?”

A proactive approach is not just reflected in how these interviews are done, but also who does them. Unfortunately, in many corporations, both the Human Resources and Legal Departments are seen as second-class citizens—those who don’t get how the business really works and are only there to say “no.” It’s better if executives or top managers take the lead on establishing a compliance culture.

Respect

When a manager hears from an employee something that even suggests a red flag, start digging. Take the employee’s concerns seriously. Interview that employee and others on a number of separate occasions. This will help assess the quality and veracity of the information.

Do not immediately go on the defensive. As indicated, isolating the kind of employee who is likely to be a successful whistleblower will have the opposite of the desired affect. In no way, shape or form, should the employee be punished or reprimanded—or even discouraged. Keeping the employee in the fold will show him or her that his or her loyalty to the company is, as it should be, rewarded.

Respond

Once there has been a thorough investigation, let the employee know what was, or was not, found. If there is no substance to the complaint, explain why. Consider putting such an explanation in writing—to be shared later if necessary with both the SEC and the employee’s counsel if s/he does become a whistleblower.

If an SEC violation is uncovered, correct it and promptly self-disclose to the SEC. And, reward the employee for using the internal, rather than the external, complaint procedures.

In sum, whistleblowers want to be heard and taken seriously. If all companies did that, we wouldn’t have any clients.