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Special SEC Briefing: Dodd-Frank Whistleblower Rules and Procedures

NWC | NATIONAL WHISTLEBLOWERS CENTER

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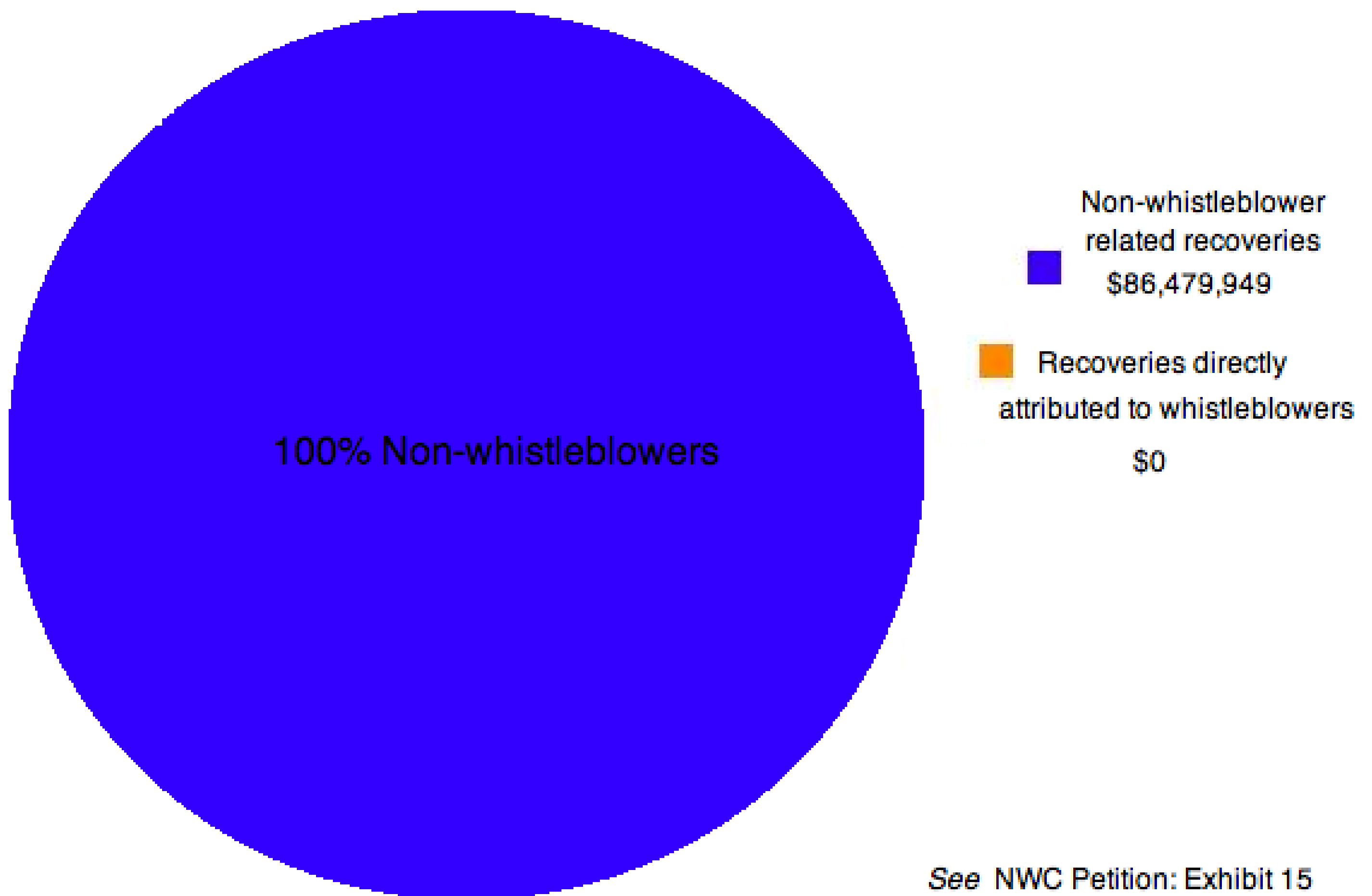
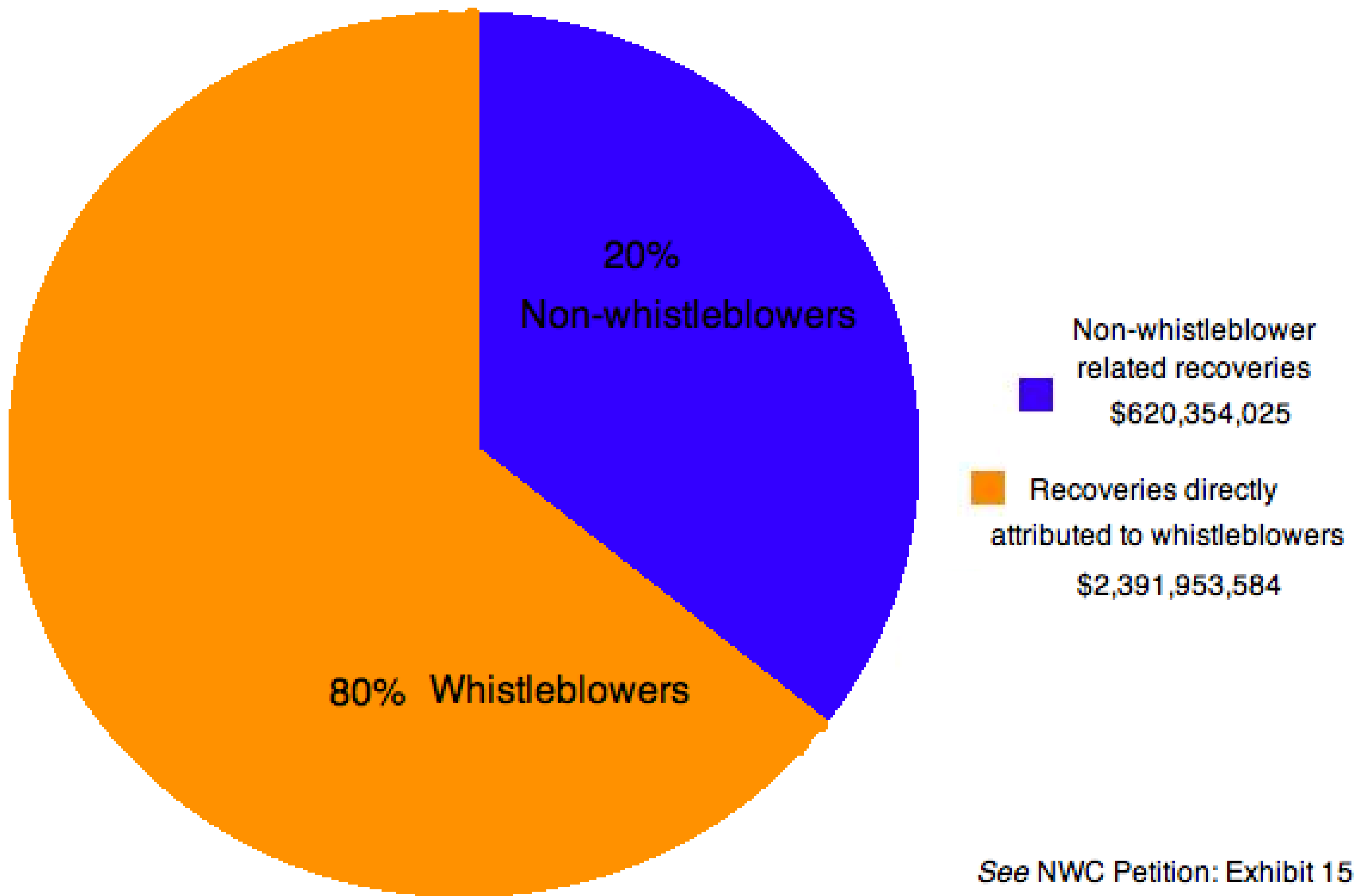
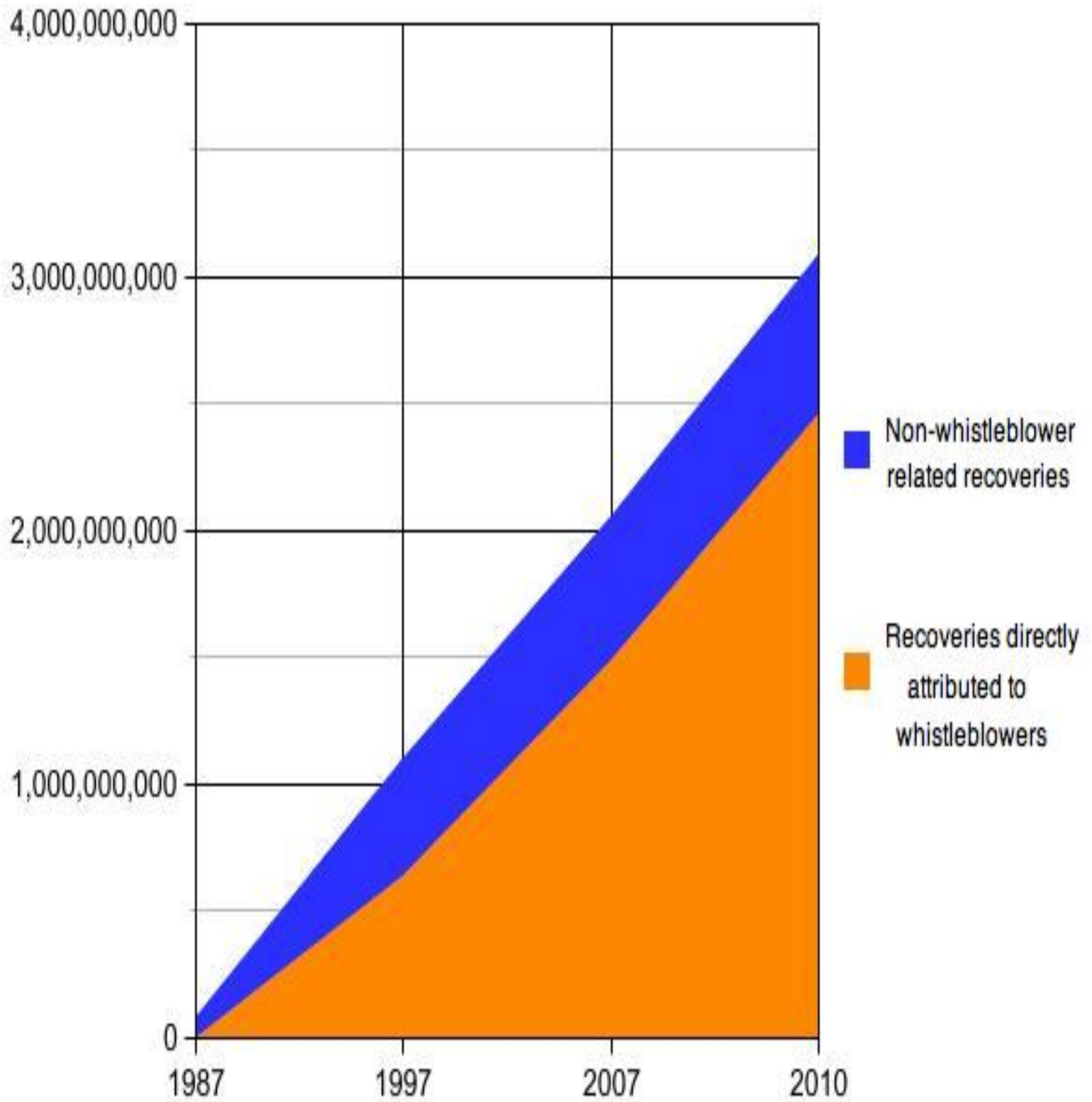
Part I: The False Claims Act Is the Most Successful Model for Improving the Disclosure of Fraud

US Civil Fraud Recovery Statistics Under FCA 1987




US Civil Fraud Recovery Statistics
Under FCA 2010
20%
Non-whistleblowers
80% Whistleblowers
Non-whistleblower
related recoveries
$620,354,025
Recoveries directly
attributed to whistleblowers
$2,391,953,584
See NWC Petition: Exhibit 15



See NWC Petition: Exhibit 15
Bench Mark
4,000,000,000
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0
1987
1997
2007
2010
Non-whistleblower related recoveries
Recoveries directly attributed to whistleblowers

"I have based [the False Claims Act] on the old fashion idea of holding out on temptation and 'setting a rogue to catch a rogue', which is the safest and most expeditious way of bringing rogues to justice."

Senator Howard,

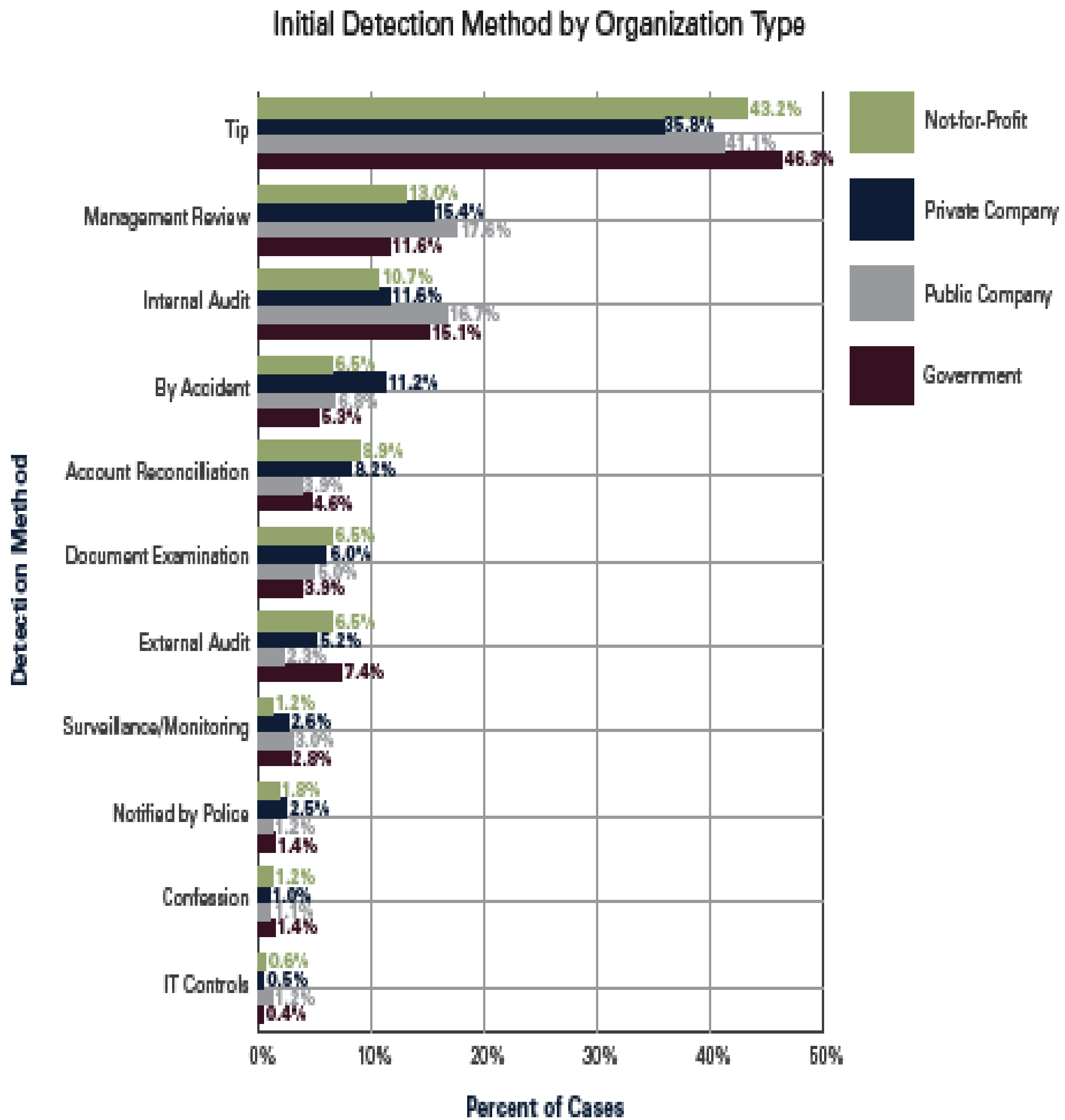
Congressional Globe, March 1863

"Incorporate best practices obtained from DOJ and the IRS into the SEC bounty program with respect to bounty applications, analysis of whistleblower information, tracking of whistleblower complaints, recordkeeping practices, and continual assessment of the whistleblower program."

SEC Inspector General,
OIG Report, March 2010

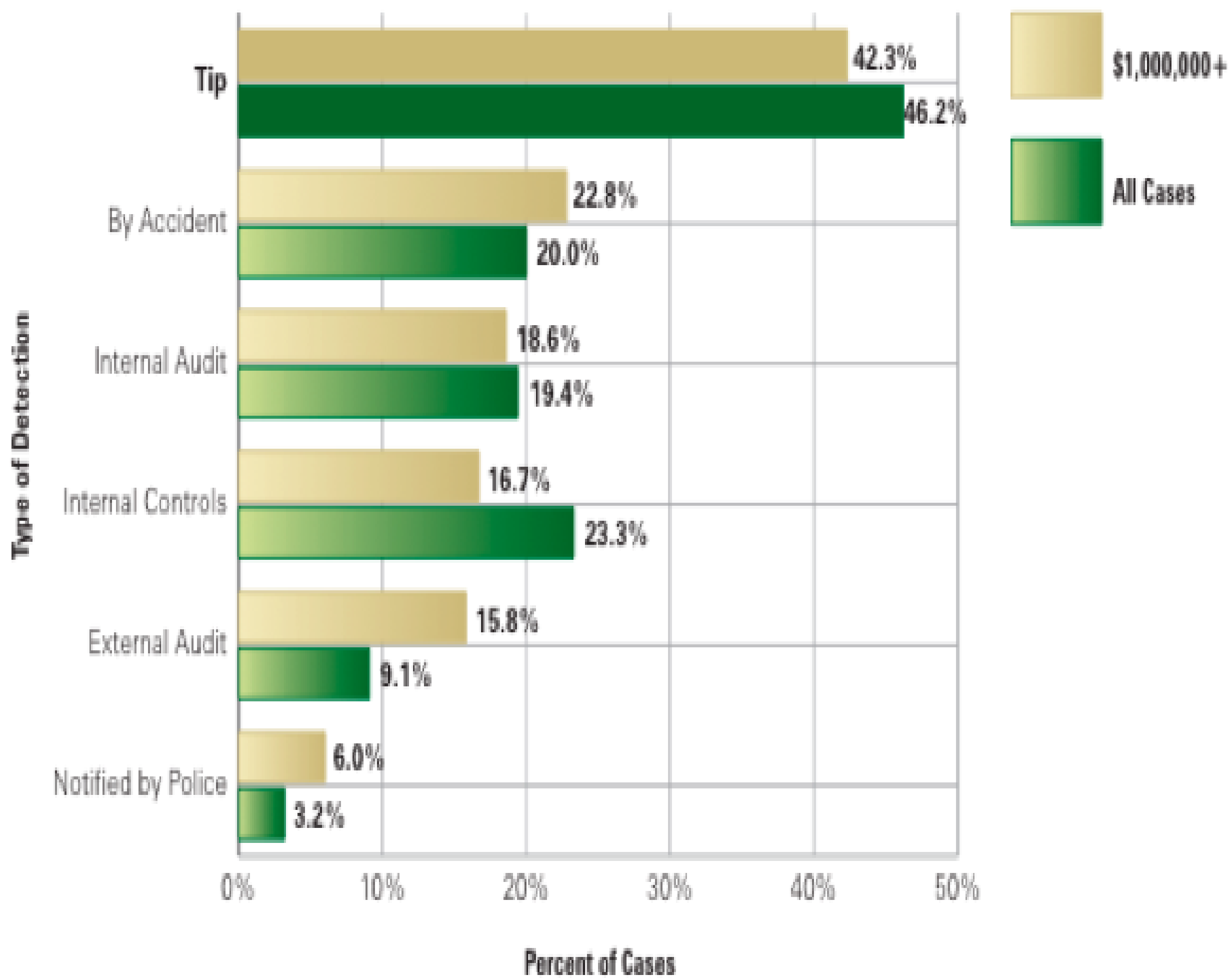
Part II: Why *Qui Tam* Works: Employee Disclosures Are the Most Effective Means to Detect Fraud

WHO DETECTS FRAUD?



[1]

[1] Source: Association of Certified Fraud Examiners, 2010 Global Fraud Study (page 19)



[6]The sum of percentages in this chart exceeds 100 percent because in some cases respondents identified more than one detection method.

"While tips have consistently been the most common way to detect fraud, the impact of tips is, if anything, understated by the fact that so many organizations fail to implement fraud reporting systems."

Association of Certified Fraud Examiners
– Global Fraud Study, 2010

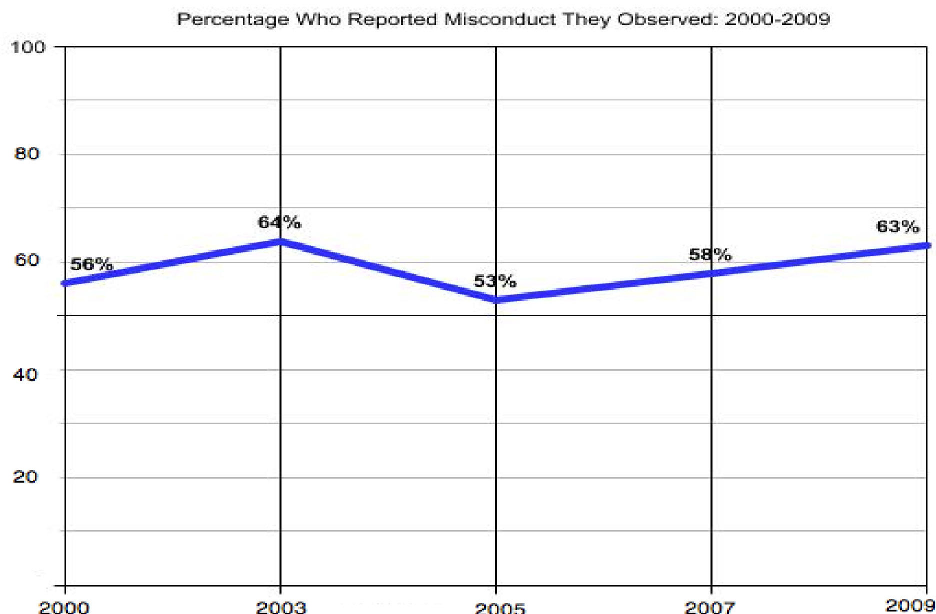
Part III:

Employees Are Reluctant to Report Fraud

Employee Reporting Behaviors

The Ethics Resource Center ("ERC") studied employee reporting behavior trends between 2000 and 2009. *See* ERC, "Blowing the Whistle on Workplace Misconduct," NWC Petition: Exhibit 15. [2]

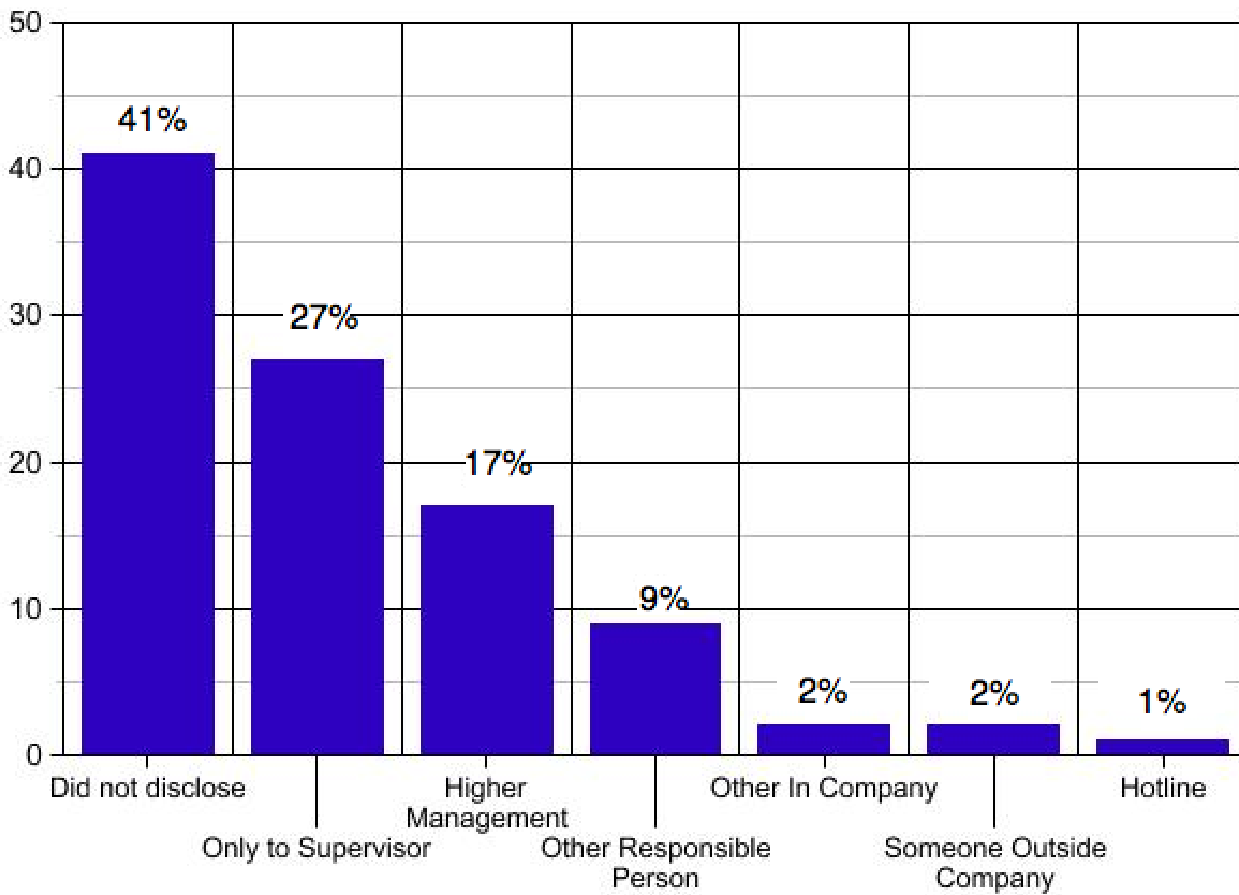
As set forth in the following chart, approximately 40% of employees who witness fraud or misconduct do not report this misconduct to *anyone*. The percentage of employees who report has somewhat fluctuated over the ten year period surveyed by ERC and averages 41% of employees not reporting misconduct to anyone. The numbers reported have remained relatively constant, even after the enactment section 301 of Sarbanes-Oxley Act. Moreover, there is no decline in numbers based on the existence of the False Claims Act and the enactment of the IRS whistleblower law for tax fraud in 2006.



*Based directly on the 2010 ERC Whistleblowing Report, *See* Exhibit 15

[2] The ERC was founded in 1922 and describes itself as "America's oldest nonprofit organization devoted to the advancement of highly ethical standards and practices in public and private institutions". According to its website, ERC is predominantly sponsored by the regulated community including corporations such as BP, Raytheon, Dow, Lockheed, Martain, and Lilly. It also receives support from the Ethics and Compliance Officer Association.

Little or No Progress in Voluntary Corporate Efforts to Increase Reporting



*Based directly on the 2010 ERC Whistleblowing Report, See NWC Petition: Exhibit 15

"One of the critical challenges facing both [Enforcement and Compliance] officers and government enforcement officials is convincing employees to step forward when misconduct occurs."

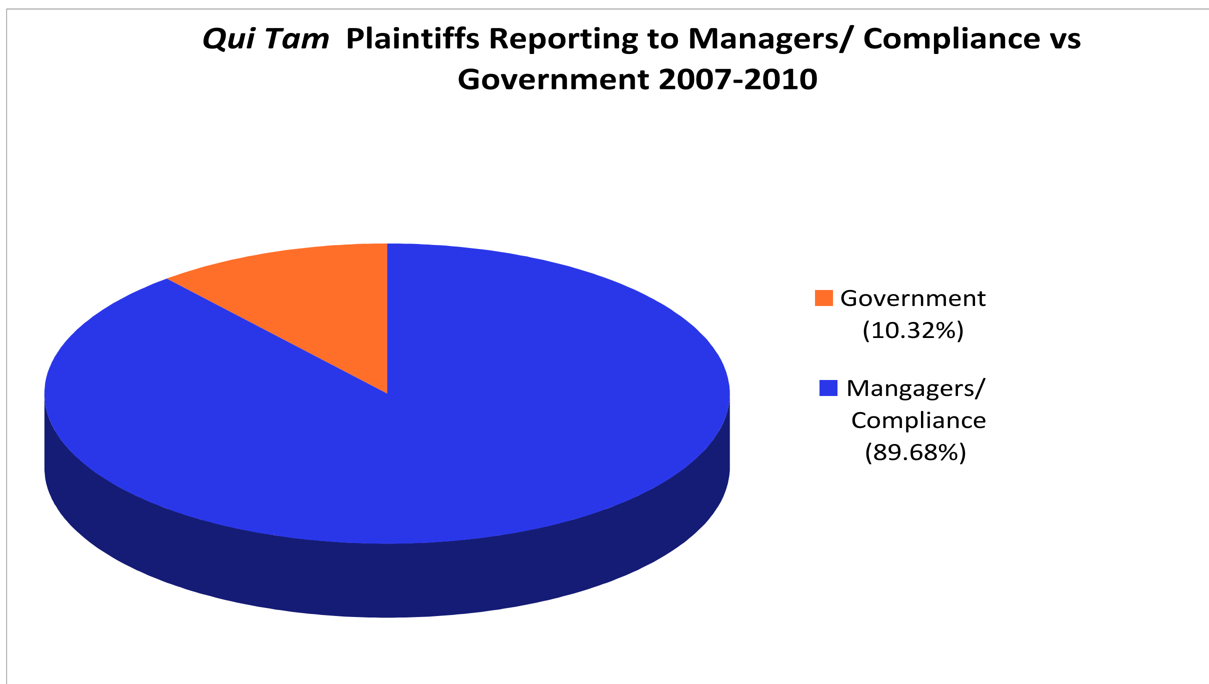
Ethics Resource Center Report,
December 2010

Part IV:

Qui Tam Laws Have No Negative Impact on Corporate Compliance Programs

Impact of *Qui Tam* Laws on Internal Reporting

The existence of a *qui tam* whistleblower reward program has no impact on the willingness of employees to internally report potential violations of law, or to work with their employer to resolve compliance issues. Our statistical study of *qui tam* cases decided in the past four years demonstrates that approximately 90% of all employees who would eventually file a *qui tam* lawsuit initially attempted to resolve their disputes internally.



**See* Exhibit 2

These statistical findings are consistent with other reviews. For example, in its May 13, 2010 issue, the New England Journal of Medicine published a "Special Report" examining the behaviors of *qui tam* whistleblowers who won large False Claims Act judgments against the pharmaceutical industry. *See* Exhibit 2, Special Report. This report also found that "nearly all" of the whistleblowers "first tried to fix matters internally by talking to their superiors, filing an internal complaint or both." In fact, 18 of the 22 individuals in the control group initially attempted to report their concerns internally. The four individuals who reported their concerns to the government were not employees of the defendant companies (i.e. they

were "outsiders" who "came across" the frauds in the course of their business), and therefore had no "internal" avenues through which to voice their concerns. It would thus be fair to say that every *qui tam* whistleblower who had the opportunity to report internally in fact did so.

Moreover, many of the cases in the NWC's study where employees reported directly to the government involved very special circumstances. For example, in one case, the initial report to the government was testimony before a Grand Jury. It clearly would have been inappropriate for that employee to discuss confidential Grand Jury testimony with his or her employer.

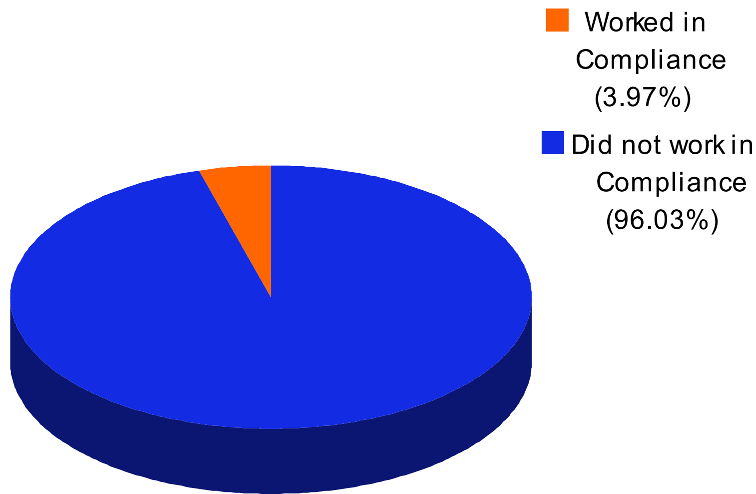
The Journal's conclusion that "nearly all" of the whistleblowers try to report their concerns internally is entirely consistent with the larger study conducted by the NWC and stands squarely contrary to the baseless concerns raised by industry that "greedy" employees will avoid internal compliance programs in pursuit of "pie in the sky" rewards. The truth is that the overwhelming majority of employees who eventually file *qui tam* cases first raise their concerns within the internal corporate process.

The *qui tam* reward provision of the False Claims Act has existed for more than 20 years and has resulted in numerous large and well-publicized rewards to whistleblowers. However, contrary to the assertions by corporate commenters, the existence of this strong and well-known *qui tam* rewards law has had *no effect whatsoever* on whether a whistleblower first brings his concerns to a supervisor or internal compliance program. There is no basis to believe that the substantively identical *qui tam* provisions in the Dodd-Frank law will in any way discourage internal reporting.

Part V:

Qui Tam Laws Have No Negative Impact on the Conduct of Compliance Related Employees

Participation of Compliance Employees in *Qui Tam* Reward Cases



**See* NWC Petition: Exhibit 2

The existence of large *qui tam* rewards did not cause compliance employees to abandon their obligations and secretly file FCA cases and seek large rewards:

- 3.97% of Plaintiff Employees worked in compliance
- Only 1 Plaintiff Employee contacted a Government Agency without first raising the concern within the corporation

The fact that compliance officials could learn of frauds, and file *qui tam* lawsuits to obtain significant monetary rewards had no impact on the reporting processes of employees working in compliance departments. Only 3.97% of *qui tam* relators worked in compliance programs. There was no spike in the number of compliance-associated employees filing *qui tam* cases and there is no reasonable basis to believe that permitting employees who work on compliance to file *qui tam* suits will in any way undermine internal compliance reporting.

Of those compliance-relators, only *one case* concerned an employee who reported his concerns directly to the government, without first trying to resolve the issues internally.

This one case is clearly an exception. In that case, *Kuhn v. Laporte County Comprehensive Mental Health Council*, the Department of Health and Human Services Inspector General was conducting an audit of the company's Medicaid billing. During the audit, the whistleblower learned that the company's internal "audit team" was altering documents to cover-up "numerous discrepancies," including a "forged" signatures and so-called "corrections" to "billing codes." The employee reported this misconduct directly to the United States Attorney's Office. The disclosures to the government were *not* provided as part of a *qui tam* lawsuit. Instead, the employee believed that these disclosures would help "protect" the employer from "federal prosecution" based on the voluntary disclosures.

Indeed, this case highlights exactly why it is important to permit compliance employees to report directly to the government. When the compliance department itself is engaged in misconduct, where else could this whistleblower have gone?

Part VI:

The Sarbanes-Oxley Act Prohibits the SEC from Adopting Rules that Require Internal Reporting

The Sarbanes-Oxley Act Prohibits the SEC from Adopting Rules that Require Internal Reporting

"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 not more then 10 years, or both."

18 U.S.C. § 1513(e)

Federal Law creates a near absolute protection for employees who contact any federal law enforcement agency regarding the violation of any federal law. Section 1107 of the Sarbanes-Oxley Act, codified as 18 U.S.C. § 1513 (e) *criminalizes* any attempt to interfere with the right of any person to contact the SEC concerning any violation of law. The section sets forth an overriding public policy, implicit or explicit in every federal whistleblower law, that employees can *always* choose to report concerns directly to law enforcement, regardless of any other program, private contract, rule or regulation. This provision was explicitly included in the Dodd-Frank Act's anti-retaliation provision, section 21F(h)(1)A)(iii) and in other provisions of law.

Part VII:
Conclusions and Recommendations to SEC

Conclusion # 1: The existence of a strong *qui tam* reward program will have no impact on internal employee reporting activities.

Conclusion # 2: The evidence does not support employer concerns that Dodd-Frank will interfere with existing compliance programs.

Conclusion # 3: The systemic problems with corporate internal compliance programs are not related to *qui tam* law rewards and exist regardless of whether employees file whistleblower complaints with the government.

Conclusion # 4: The SEC must ensure, through a formal rule, that reports to internal compliance programs are fully protected. The decades-long history of regulated companies opposing such protections in judicial proceedings must be ended. The definition of protected disclosures should conform to the standards recommended by the Association of Certified Fraud Examiners.

Conclusion # 5: The recommendations of the SEC's Inspector General should be fully implemented in a manner consistent with the requirement that the Dodd-Frank reward provisions be "user-friendly".

Conclusion # 6: Any action by an employer that in any way limits an employee's right or incentive to contact the SEC, regardless of whether or not the employee first utilized a compliance program, is highly illegal and constitutes an obstruction of justice.

Conclusion # 7: The exclusion of employees who work for foreign state-owned industries or government agencies must be modified or eliminated.

Conclusion # 8: All whistleblower rewards must comply with the 10 – 30% range mandated by the statute.

About the National Whistleblowers Center

The National Whistleblowers Center (NWC) is an advocacy organization with a more than 20 year history of protecting the rights of individuals to speak out about wrongdoing in the workplace without fear of retaliation. Since 1988, the NWC has supported whistleblowers in the courts and before Congress, achieving victories for environmental protection, nuclear safety, government ethics and corporate accountability. The NWC also sponsors several educational and assistance programs, including an online resource center on whistleblower rights, a speakers bureau of national experts and former whistleblowers, and a national attorney referral service run by the NWC's sister group the National Whistleblower Legal Defense and Education Fund (NWLDEF). The National Whistleblowers Center is a non-partisan, non-profit organization based in Washington, DC.

This report was prepared under the direction of Stephen M. Kohn, Executive Director of the National Whistleblowers Center. The National Whistleblowers Center would like to recognize the contributions of Director of Advocacy and Development Lindsey M. Williams and Staff Attorney Erik D. Snyder for his legal research, analysis, and editorial contributions to this Report. In addition, the National Whistleblowers Center would like to thank Law Clerks Zach Chapman, Greg Dobbels, Katie Mee, Andrew Palmer and David Simon for their assistance in reviewing the False Claims Act cases. Finally, the National Whistleblowers Center would like to thank legal interns Marshall Chriswell and Shane Swords for their work on preparing this presentation.