

# Whistleblowers:

## The Human Factor in Ensuring Compliance

**W**hile employee tips have been shown to be an effective tool in preventing and correcting corporate misconduct, many feel ambivalence about whistleblowing is rooted in distaste for tattletales and snitches. This article analyzes the crucial role that whistleblowers play in ensuring compliance, and addresses their reluctance to come forward, as well as the reluctance of authorities to give proper credit to whistleblower reports. The article also gives practical guidance on overcoming obstacles to realizing the potential business-saving benefits of whistleblower reports.

Thirty years ago, a retired FBI agent named Ralph Childs was building a second career as a security consultant. One of his clients was experiencing a serious inventory shrink problem. Childs was convinced that other employees knew who was stealing. The challenge was to overcome the pressures to keep silent. He set up a toll-free telephone number, available 24 hours a day so employees could call, anonymously if they wanted, to tell what they knew. In those early days, the number was routed to Childs' house after hours, and he went to bed with a pencil and pad on his nightstand. So the employee hotline industry was born.



By Marian E **X**all

## The Limits of Technology

Compliance technology has come a long way since then, from video cameras to biometric recognition access systems; from accounting software that red-flags suspicious transactions, to programs that claim to prevent them altogether. And yet it is still the human factor that is most effective in combating misconduct in the workplace. Just as human ingenuity finds ways to circumvent the rules by engineering loopholes in even the most sophisticated mechanisms for ensuring compliance, so human integrity is the best defense of those rules. The challenge remains finding ways to enable that human factor in the service of compliance programs.

Every two years, the Association of Certified Fraud Examiners (ACFE) publishes a survey regarding occupational fraud and abuse.<sup>1</sup> Tips consistently outrank all other means of detecting misconduct in the workplace. Here is the ACFE's most recent *Report to the Nation*:

### Initial Detection of Occupational Frauds

Tip .....	46.2%
By Accident .....	20.0%
Internal Audit.....	25.4%
Internal Controls.....	23.2%
External Audit.....	9.1%
Notified By Police.....	3.2%

The majority (57.7 percent) of tips that uncover fraud come from employees, and about 30 percent of tips come from other outside sources such as customers and vendors. Another 8.9 percent are anonymous. This means that internal tips are nearly three times as likely to lead to the detection of fraud as an external audit.

The Sarbanes-Oxley Act of 2002<sup>2</sup> gave a significant nod to the human factor by including stringent anti-whistleblower-retaliation provisions, as well as requiring that the board's audit committee establish and maintain channels for employees to report financial irregularities. Remember that the financial scandal at Enron, a major motive behind the passage of Sarbanes-Oxley, was exposed by a whistleblower, Sherron Watkins. However, Sarbanes-Oxley is a sweeping piece of legislation, affecting almost every aspect of corporate accountability. In the furor to meet the various deadlines that the Act imposed, many corporations adopted a "check-the-box" mentality to compliance. The focus of effort and dollars was on Section 404's mandate of adequate internal financial controls. The search was on for a "software fix" for Section 404 compliance.



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## Building an Ethical Culture

With the passage of time, the realization has grown that achieving technical Sarbanes-Oxley compliance does not meet the spirit of the law. As demonstrated by agendas at conferences and seminars, and the content of business periodicals including *ACC Docket*, the emphasis is now on building "an ethical culture" throughout the organization. What does this mean? Clearly, it involves maintaining an ongoing communications campaign about business ethics that not only educates as to appropriate conduct, but also makes clear what employees are expected to do when inappropriate conduct occurs. It means setting the tone from the top, with the board as well as senior management on down not only modeling ethical behavior, but also knowing how to respond appropriately to employees when they speak up about their concerns.

Nurturing employee-whistleblowers as essential and valued partners in ensuring corporate compliance is an aspect of creating and maintaining an ethical culture that deserves to be specifically addressed. However, there is a reticence about discussing the role of whistleblowers in compliance planning. This reluctance has deep roots in our language. *Roget's Thesaurus* lists "whistleblower" with "blabbermouth, busybody, fink, nark, rat" and "snitch" as pseudonyms for "tattletale." Understanding these negative associations with the "w" word is a crucial first step to overcoming them, and thus unleashing the potential of the human factor in detecting and preventing non-compliance.

## Bypassing Internal Channels

On a superficial level, the factor that distinguishes the whistleblower as snitch from the whistleblower as saint is to whom "the whistle" is blown.

Employees who call the media or government enforcement agencies such as the Security Exchange Commission's hotline present a nightmare scenario for companies. Immediately, the company is thrown on the defensive, and the chances of objectively investigating and correcting the alleged misconduct are seriously diminished. Why do whistleblowers bypass internal channels and go outside the company to complain? There are various reasons for this behavior, and not all of them can be neutralized. However, to the extent they can be analyzed and addressed, the company may be able to save itself from embarrassment and expense at least, if not from out-and-out disaster.

## No Effective Internal Channel

Long before the passage of Sarbanes-Oxley, the establishment of an effective channel for employees to voice

their concerns to management has been recognized as a key component of corporate compliance programs. The *Federal Sentencing Guidelines*, issued in 1991, listed the creation and publicizing of a reporting system whereby employees and other agents could report criminal conduct within the organization without fear of retribution as one of the seven requirements for an effective compliance program. Adherence to these requirements allows an organization and its executives to avoid or minimize criminal penalties for corporate misconduct. The guidelines were reviewed and updated in 2004, and the reporting system requirement was strengthened with a recommendation that such systems include mechanisms that allow for anonymity or confidentiality.

However, to be effective an internal reporting channel must be used. If reports are required to be made through the chain of command, the system is unlikely to be effective because employees will not report misconduct to the very people who may be responsible for it. Similarly, channeling reports to human resources is usually ineffective because HR may be perceived as not having a strong voice with senior management. The best practice is to have several alternative channels available, including, if a publicly-held company, the opportunity to report to a board member directly. If the company has a chief ethics officer, or similar position, then clearly one reporting route should be to that person. However, even that route should be one of several offered.

Many companies pride themselves on their “open door” policy. This pride is usually misplaced. If the company was once small enough for top management to deal with employee complaints, it has probably long outgrown that possibility. More likely, the CEO’s door was never really “open” to employee complaints. Better to abandon the open door fiction, and work at promoting a real openness that involves several alternative channels of communication.

### **Fear of Retaliation**

Fear of retribution is still the number one deterrent keeping employees with concerns about corporate misconduct from coming forward. Sarbanes-Oxley was not the first legislation to provide penalties or a civil right of action to employees who lost their job because they spoke up about illegal conduct. Federal statutes including the Occupational Health and Safety Act (OSHA), the Americans with Disabilities Act (ADA), the Age Discrimination in Employment Act (ADEA), and Title VII all contain anti-retaliation provisions. Yet in spite of this panoply of protection, retaliation claims are on the increase. The Equal Employment Opportunity Commission (EEOC) reports that in 2007, over 32 percent of the charges received cited retaliation, up from 22 percent in 1997, making retaliation

the second most frequent claim after race discrimination. Some estimates suggest that over 50 percent of whistleblowers experience retaliation.

Furthermore, the definition of what constitutes retaliation is expanding beyond the ultimate act of loss of employment. In *Burlington Northern and Santa Fe Railroad Co. v. Sheila White*,<sup>5</sup> the US Supreme Court enlarged the standard for what is actionable retaliation in a sex discrimination case to include acts that are “materially adverse” to a reasonable employee, including transfers or suspensions that do not result in any loss of pay, benefits, or privileges. Wise companies will adopt a broad definition of retaliation in their ethics policies.

Litigation statistics and definitions crafted in the courtroom take a while to sift down to the everyday workplace, where a manager may perceive an employee’s use of an ethics reporting system that by-passes her as disloyal, and may rate down the employee’s performance because of it. One of the most important elements of compliance training is making sure managers really understand what “no

## **Four Reasons Why Employees Don’t Speak Up and How to Overcome Them**

### **Fear of Retaliation**

To make a “no retaliation” policy stick, managers have to understand that they put their careers at stake, as well as expose the company to liability, if they retaliate or allow retaliation to occur.

### **Belief That Nothing Will Be Done**

Appointing a chief ethics officer with real power to investigate and correct misconduct is a first step to building credibility. Always follow up with a whistleblower to explain the results of the investigation and remedial steps taken. Over time, employees will know the company takes complaints seriously.

### **Fear That Identity Will Be Revealed**

Complete confidentiality can never be guaranteed because an effective investigation may require the disclosure of facts that reveal the whistleblower’s identity. However, disclosure must only be on a “need to know” basis.

### **Not Wanting to Make Waves or Get Others Into Trouble**

A comprehensive ethics communications campaign should stress that early detection and correction of misconduct helps the company—and its honest employees—succeed.

## In the pressure to meet deadlines or budget, managers may brush off an employee who is at all tentative about voicing his or her complaint.

retaliation” means. The most effective training is participatory, using “real life” vignettes that allow the managers to explore how employees perceive even unintended slights and coolness as retaliation for speaking up.

### Complaints Ignored

One of the more surprising statistics uncovered in a 2006 benchmarking survey published by CSO Executive Council and The Network, Inc.,<sup>4</sup> is that over 28 percent of whistleblowers who used a third party hotline had already reported the misconduct to management within their company, presumably with little or no result.

Another crucial element of compliance training for managers is teaching them how to respond to employees who come forward with concerns. All too often, managers fail to take the time to listen carefully to their employees. In the pressure to meet deadlines or budget, managers may brush off an employee who is at all tentative about voicing his or her complaint. “I’ll bear that in mind,” or “Why don’t you talk to so-and-so?” are *not* adequate responses to employee concerns. At a minimum, training should include active listening techniques, and a model script for a conversation with a whistleblower. Although managers should be dissuaded from “going it alone” in questioning the whistleblower—the decision of who should conduct the investigation and how is a subject for another article—certain key information must be communicated in the initial interview, such as an undertaking to treat the complaint confidentially, a commitment that someone will get back in touch, and sincere thanks for coming forward.

### Cultural Obstacles to Encouraging Whistleblowing: The European Experience

Turning from the employee’s reluctance to come forward to management’s reluctance to credit or act upon a whistleblower report, a look at the European attitude to whistleblowing may be instructive.

The European Union has sought to regulate ethics hotlines under the EU’s Privacy Directive which mandates that each EU member pass legislation protecting personal

data privacy, and establish an agency to enforce the law. France’s data privacy protection agency, the Commission Nationale de l’Informatique et des Libertés (CNIL) was the first to see whistleblower reports as a threat to personal privacy when it denied authorization to McDonald’s hotline. Of particular concern to the CNIL was the possibility of making anonymous reports. The CNIL subsequently issued guidelines for hotlines. Companies who comply with these guidelines benefit from a streamlined authorization process. In summary, the guidelines require:

- The scope of the hotline should be restricted to accounting, auditing, banking, and anti-corruption.
- Anonymous calls should be discouraged.
- A dedicated unit to gather and investigate calls.
- The individual accused in the report must be informed as soon as the evidence has been secured.

Other EU countries have followed France’s lead in restricting hotlines, especially where they encourage anonymous reports. The EU itself has weighed in with an Opinion from its Article 29 Working Party echoing the CNIL concerns. The CNIL and the EU Working Party acknowledge up front that their distrust of whistleblowing has historical roots. During and immediately after World War II, those who bought favors from the Nazi occupiers by informing on the Resistance, Jews, and others were reviled as informers. Similarly, in those EU members that were previously Communist states informers, were a dreaded tool used to track down non-conformers.

The United States and the United Kingdom, which did not share this experience, have a more accepting attitude toward whistleblower reports. However, US companies, even those without European operations, can learn some les-

## HR Best Practices for Preventing Retaliation

- Respond to all whistleblower reports with a prompt, thorough and impartial investigation, regardless of whether the source is a “problem” employee.
- Make sure all employees understand the standard of performance expected, and the consequences of failing to meet the standard (notice).
- Make sure employees have a meaningful opportunity to meet the performance standard by providing the necessary training, tools and counseling (opportunity).
- Document! Document! Document! Rather than “building a file” once the termination decision has been made, keep a concise, factual record of the employee’s performance or conduct, including notice and opportunity.

sons from the EU approach. While the risk of malicious or deliberately false reports is small, it must be recognized. The career and reputation of someone wrongly accused is on the line. The protection of the rights of all concerned depends on a prompt, thorough and objective investigation, including an early interview with the person named as a wrongdoer.

Particular care should be taken with anonymous reports. The hotline intake interview may be the only chance to obtain crucial information which enables a meaningful investigation. This is why any hotline program should provide skilled interviewers available 24/7 to probe for all the facts. Although Sarbanes-Oxley requires the whistleblower reporting system to allow anonymous calls, they need not be encouraged. The hotline interviewer by stressing that the caller's identity will be kept confidential, especially from anyone named in the call, may be able to persuade the caller to forego anonymity, thus permitting feedback and follow-up critical to an effective investigation.

### The Problem Employee


Some executives may remain suspicious that employees will manufacture whistleblower complaints in order to ward off discipline, termination for poor performance, or their own misconduct by gaining the protection of the legal prohibition on retaliation. Again, these cases are probably a small minority, and should not lead you to abandon or neglect a whistleblower reporting system.

The best defense against the self-serving whistleblower is clearly communicated and consistently enforced human resources policies. The three key words here are: notice, opportunity, and documentation. If a problem employee has notice of what the standard for performance is, an opportunity to meet the standard, and if notice, opportunity, and the employee's performance have been appropriately documented, the employee can be held accountable, up to and including termination, without fear that management action will be found to be retaliatory. Of course, any complaint made by a problem employee must be treated as seriously as any other, but that is a separate matter from the employee's questionable workplace behavior or performance.

Managers who remain unconvinced can take comfort from the track record established for retaliation claims brought under the Sarbanes-Oxley Act. Statistics show that employers prevail most of the time in these cases. Almost none make it past the administrative level.

### From Snitch to Saint

It takes time and consistent communication and enforcement of an ethics program and human resources best practices to change the reticence of both employees and managers towards whistleblowing. The obstacles that dissuade employees from speaking up need to be acknowledged

and addressed, while at the same time working thoughtfully through the reasons why executives may be reluctant to recognize whistleblowers, if not as saints, at least as the foot soldiers of an effective compliance program 

Have a comment on this article? Email [editorinchief@acc.com](mailto:editorinchief@acc.com).

#### NOTES

- 1 2008 Report to the Nation, Association of Certified Fraud Examiners, [www.acfe.com/resources/publications.asp?copy=rttn](http://www.acfe.com/resources/publications.asp?copy=rttn)
- 2 Corporate and Criminal Fraud Accountability Act of 2002, 18 U.S.C. § 1514A.
- 3 548 U.S. \_\_\_\_\_, 2006 LEXIS 4895 (2006).
- 4 [www.reportline.net/news/pressreleases/tmw\\_pr\\_111506bench.asp](http://www.reportline.net/news/pressreleases/tmw_pr_111506bench.asp)

## ACC Extras on ... Whistleblowers

### ACC Docket

*Sarbanes-Oxley Whistleblowers: Avoiding the Nightmare Scenario* (2006). Sarbanes-Oxley's whistleblower provisions have caused more than their fair share of hair-tearing by in-house counsel seeking to implement those mandates. But the whistleblower provisions of SOX also represent an opportunity to use whistleblowers as a valuable internal early warning system for illegal conduct and other wrongdoing. [www.acc.com/resource/v7106](http://www.acc.com/resource/v7106)

### InfoPAKs<sup>SM</sup>

*Sarbanes-Oxley Primer for the Small Law Department* (2005). This primer provides a broad overview of several provisions of Sarbanes-Oxley. It is intended to offer a brief introduction into SOX topics to non-securities law practitioners practicing as in-house counsel, and perhaps to provide a quick, summary level "brush-up" for securities practitioners. To aid readers in their understanding of the covered topics, it includes practice tips and several forms and reference materials in the samples and forms section at the end. [www.acc.com/resource/v6362](http://www.acc.com/resource/v6362)

### Sample Forms and Policies

- *Sample Whistleblower Policy* (2007). Excerpted from Program 807 at ACC's 2007 Annual Meeting. [www.acc.com/resource/v9190](http://www.acc.com/resource/v9190)
- *Whistleblower Policy*. [www.acc.com/resource/v84](http://www.acc.com/resource/v84)

ACC has more material on this subject in our Virtual Library<sup>SM</sup>. To create your personalized search, visit [www.acc.com](http://www.acc.com), click on the "Research" pull-down menu button, then select Virtual Library. Type in your keywords and search to see the other resources we have available.