The Business Case for Whistleblowers

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Overview

I. Whistleblower Law 101
   • Key Features of Federal, State & Local False Claims Acts
   • SEC/CFTC/IRS & DOT Whistleblower programs
   • International WB Programs

II. Case Study
   • Jes Staley/Barclay’s CEO

III. An Ounce of Prevention: Advice for Avoiding Whistleblower lawsuits
What do I mean by Whistleblower under US WB programs?

• Not Edward Snowden or Chelsea (Bradley) Manning

• U.S. Government or US Regulatory Interests (SEC/CFTC/IRS/DOT) undermined.
  
  – Inside information re: fraud v. U.S.
    
    • Defrauding DOD, Medicare, US customs
    • Violating US securities laws/harming shareholders of publicly traded companies
Whistleblowing Works
Whistleblowing Works

• Government’s primary tool for prosecuting fraud
  • Well-placed insider vs. Government audits from the outside – road map to the fraud
Whistleblowing Works – Let’s Look at the Numbers

• FALSE CLAIMS ACT
  – Government recovered more than $2.9B in 2016 from whistleblower lawsuits
    • Whistleblowers received $519M in rewards in 2016
  – 1986 – 2015: over $47B recovered
Whistleblowing Works – By the Numbers

• SEC WB Program (Dodd-Frank)
  – Game changer
  – 7 years in, Program is in Full Stride
SEC WB Program

• Program Overall (2010 to 2017)
  – Wrongdoers ordered to pay $975M in sanctions
  – 49 WBs ~$250M in awards

• 2017 Report to Congress
  – Paid $50M in awards to 12 tipsters

• 2018 Poised to be Biggest Year yet
  – $221M in future WB payments are “probable”
  – vs. $10.8M reserve in 2017
LARGEST AWARDS TO DATE

• FEB 2018: **Edward Siedle** – JP Morgan failure to disclose it was directing wealthy clients to investments benefiting JPM
  – $78M award ($48 SEC/$30M CFTC)

• MARCH 19, 2018: Merrill Lynch paid $415M misuse of customer funds
  – $83M award ($50M to 2 WB; $33M to 3rd)
SEC Active in Protecting WBs

- Imposing Fines on Companies who seek to chill WB / impede reporting to SEC
- “NO PERSON MAY TAKE ANY ACTION TO IMPEDE AN INDIVIDUAL FROM COMMUNICATING DIRECTLY WITH THE COMMISSION STAFF ABOUT A POSSIBLE SECURITIES LAW VIOLATION, INCLUDING ENFORCING OR THREATENING TO ENFORCE, A CONFIDENTIALITY AGREEMENT ... WITH RESPECT TO SUCH COMMUNICATIONS.” 17 CFR 240.21F-17.
SEC Active in Protecting WBs

• SEC has fined 9 companies for interfering w/ WB ability to communicate w/ SEC
  – 2017: $500,000 fine on Homestreet severance agmt requiring EE waive rt to WB award
Don’t Impede EE ability to report to SEC

- Enforcement Actions Based on Actions Taken to Impede Reporting
  - In the Matter of Homestreet, Inc. and Darrell Van Amen, File No. 3-17801 (January 19, 2017)
  - In the Matter of Blackrock, Inc., File No. 3-17786 (January 17, 2017)
  - In the Matter of SandRidge Energy, Inc., File No. 3-17739 (December 20, 2016)
  - In the Matter of NeuStar, Inc., File No. 3-17736 (December 19, 2016)
  - In the Matter of Anheuser-Busch InBev SA/NV, File No. 3-17586 (September 28, 2016)
  - In the Matter of Health Net, Inc., File No. 3-17396 (August 16, 2016)
  - In the Matter of BlueLinx Holdings Inc., File No. 3-17371 (August 10, 2016)
  - In the Matter of Merrill Lynch, Pierce, Fenner & Smith Incorporated and Merrill Lynch Professional Clearing Corp., File No. 3-17312 (June 23, 2016)
  - In the Matter of KBR, Inc., File No. 3-16466 (April 1, 2015)
Whistleblowing Works –
Improved Outcomes in Gov’t Enforcement
Fraudsters Fare Worse When Whistles Blow

– Study from earlier this year – *Journal of Accounting Research*
  • Examined data on 658 federal investigations of financial misrepresentation from 1978 to 2012

– When WB involved in Government Enforcement (SEC/DOJ), companies are more likely:
  • To be hit with financial penalties (8.5% increased likelihood)
  • Pay far higher penalties
    – (average: $8.7M vs. $30.7M)
    – (total penalties: $22.8M v. $69.4M)
  • Increased likelihood of criminal sanctions
  • Longer prison sentences (22.5 mos v. 41.9 mos)
DETAILS OF US WB LAWS
The Laws

A. False Claims Act (FCA)
   - Federal, State and Local FCAs

B. IRS Whistleblower Program

C. SEC/CFTC Whistleblower Programs

D. DOT/NHTSA Auto Safety WB Program

E. Other Whistleblower Laws
Federal False Claims Act

Filing Process/Procedure (31 U.S.C. § 3730(b)(2)-(5)).

1. Complaint and written disclosure is filed with the government.
   • Under Seal

2. Upon expiration of seal, the government either proceeds with the case or declines.
   • If the government proceeds, the action is conducted by the government.
   • If the government declines, the whistleblower has the right to continue the action on his/her own.
FALSE CLAIMS ACT –
granddaddy of WB laws

✓ Federal False Claims Act (FCA)
  – Medicare fraud
  – Defense fraud

✓ State False Claims Acts
  – Medicaid fraud & infrastructure fraud

✓ City & Country FCAs
State Whistleblower Laws

• Generally
  ✓ 29 states and DC have FCAs that are generally modeled on the federal FCA.

• New Hampshire (formerly Montana)
  ✓ Some states limit claims to those brought by state citizens or against companies with a strong presence in state.

• Cities & Counties
  ✓ Some cities & counties (Chicago, New York) have separate False Claims Acts.
30 States with False Claims Act & Qui Tam Provisions

- California
- Colorado
- Connecticut
- Delaware
- District of Columbia
- Florida
- Georgia
- Hawaii
- Illinois
- Indiana
- Iowa
- Louisiana
- Maryland
- Massachusetts
- Michigan
- Minnesota
- Montana
- Nevada
- New Hampshire
- New Jersey
- New Mexico
- New York
- North Carolina
- Oklahoma
- Rhode Island
- Tennessee
- Texas
- Vermont
- Virginia
- Washington
2 States with False Claims Acts with WB Rewards Only, No *Qui Tam* Provision

- Arkansas
- Missouri
6 Cities and 2 Counties with False Claims Acts

- Bay Harbor Islands, FL
- Broward County, FL
- City of Hallandale Beach, FL
- Miami-Dade County, FL
- Chicago, IL
- New York City, NY
- Allegheny, PA
- Philadelphia, PA
IRS Whistleblower Program

A. Tax fraud must exceed $2 million, with limits (for individuals) based on annual income.
   - Practical limitations.

B. Fraud not required, merely evasion

C. The IRS itself has jurisdiction over the claim through its Whistleblower Office, therefore, there is no court filing.

D. Statute of limitations, generally 3 years.
SEC Whistleblower Program

Filing/Process/Procedure:

– Whistleblowers provide information to the SEC through its Whistleblower Office.

– If the SEC recovers sanctions over $1 million, it posts a Notice of Covered Action (NoCA) on its website.
  • Whistleblower then has 90 days to apply for an award.
  • Application is reviewed by the SEC and Final Order is issued granting or denying an award.

– Whistleblower cannot continue the claim privately if the SEC declines to initiate an enforcement action.

– Statue of limitations generally 2 years / 5 years.
CFTC Whistleblower Program

• Largely mirrors the SEC Whistleblower Program.
DOT/NHTSA Whistleblower Program

• WB = EEs of car manufacturers, car part suppliers or car dealerships
• Motor Vehicle Safety Whistleblower Act, 49 U.S.C. § 30172
  – Largely mirrors the SEC Whistleblower Program.
• Violations of safety regulation
1st Whistleblowers under DOT Program

• 2 former employees of Takata
  – Mark Lillie & Anonymous WB
  – Received $1.13M to settle their claims for WB rewards

Other Whistleblower Programs

• Ocean Dumping/Pollution
  – APPS (Act to Prevent Pollution from Ships)

• Wildlife protection
INTERNATIONAL WHISTLEBLOWER LAWS
Ontario Securities Commission

• WB statute largely identical to US SEC WB program

• Securities fraud in Ontario
  – Companies traded on TSX Toronto Stock Exchange
Africa & Asia

- Namibia
- South Korea
On The Horizon

• Australia – legislation expected in July 2018 expanding WB protections
• U.K. – support for Office of the Whistleblower in UK Government
  • House of Lords
    – Lord Cromwell (CB)
    – Baroness Kramer (LD)
    – Lord Touhig (Lab)
Key Features of Whistleblowing Statutes

• Whistleblower Identity Protection
  ✓ Cases filed Under Seal
  ✓ WB identity initially protected but usually revealed at end of case

• Incentivized Integrity
  ✓ Financial Reward

• Protections Against Retaliation
A Uniquely American Phenomenon

Other Countries

- Reactive
  - Whistleblower protections against retaliation

U.S. Whistleblower Laws

- Reactive
  - Whistleblower protections against retaliation

- Proactive
  - Report
  - Ability to assist
  - Pursue Independently
  - Share
Identity Protection / Anonymity

A. FCA

✓ Case remains under seal for a minimum of 60 days, and often years.

✓ At end of case, whistleblower identity is almost always revealed.

✓ Practical considerations.

B. State Law

✓ Ex: NY State – Whistleblower remains anonymous if case is dismissed
Identity Protection / Anonymity

A. SEC

✓ Most robust
✓ Anonymity largely ensured throughout
  ✓ Can be anonymous even to the SEC
    ✓ Mr./Ms. XYZ
Reward (FCA)

- Percentage of whistleblower reward ranges from 15% to 30% of amount recovered by Government for federal programs (can be higher in some states).
  - Government intervenes = 15% - 25%
  - Government does **not** intervene = 25% - 30%
- Size of award depends on nature of whistleblower’s contribution to recovery.
- Grounds for reducing the reward percentage
  - WB’s info is based primarily on public disclosures = Not more than 10%
  - WB planned and initiated the fraud = Share may be reduced or eliminated
  - Convicted of a crime arising from the fraud = Dismissed from the case & recover nothing
Protection Against Retaliation: FCA’s anti-retaliation provision

FCA prohibits retaliatory acts taken against a WB or potential WB.

✓ “Any employee, contractor, or agent shall be entitled to all relief necessary to make that employee, contractor, or agent whole, if that employee, contractor, or agent is discharged, demoted, suspended, threatened, harassed, or in any other manner discriminated against in the terms and conditions of employment because of lawful acts done by the employee, contractor, agent or associated others in furtherance of an action under this section or other efforts to stop 1 or more violations of this subchapter.” 31 U.S.C. §3730(h).

FCA covers retaliation not just against WBs who have filed a *qui tam* action but also against “other efforts” to stop fraud, presumably other types of internal and external reporting of fraud.

Remedies includes double back pay, special damages and attorney’s fees and costs.
Protection Against Retaliation:  
State False Claims Laws, SEC & DOT

- Many States also have anti-retaliation provisions
- SEC has anti-retaliation provisions
- SOX – Sarbanes Oxley protections (arising out of Enron scandal)
- DOT WB program – OSHA protections
ANATOMY OF WB-INITIATED FALSE CLAIMS ACT CASES
False Claims Act Liability

The False Claims Act prohibits:

a) knowingly presenting, or causing someone else to present, a false or fraudulent claim;

b) knowingly making, using, or causing to be made or used, a false record or statement material to a false or fraudulent claim; and

c) knowingly concealing or knowingly and improperly avoiding or decreasing an obligation to pay or transmit money or property to the Government.

31 U.S.C. § 3729(a)(1)(A), (B), (G).
Elements of FCA Liability

• Claim
  ✓ False or Fraudulent
  ✓ Material to Government’s purchase decision
  ✓ Made Knowingly
Claim

Any request or demand for money or property: presented to an officer, employee or agent of the Government; or to be spent or used on Government’s behalf or to advance Government interest and any portion of funds requested is provided or reimbursed by government.

31 U.S.C. § 3729(b)(2)
False or Fraudulent

- Not limited to express false statements
- Includes misrepresentations by omission
Materiality

• Natural tendency to influence, or be capable of influencing, the payment or receipt of money or property

31 U.S.C. § 3729(b)(4)

“Immaterial,” even if intentional, breaches not covered

✓ the wrong shade of paint;
✓ providing something which is better than what was required
Knowingly

- Actual knowledge
- Reckless disregard
- Deliberate indifference
- Specific intent not required

31 U.S.C. § 3729(b)(1)

- Mistakes and mere negligence not covered
- “Government knowledge” is not a defense to liability. Could be relevant to Defendant’s scienter.
Treble Damages & Penalties

Violations of the FCA subject violators to liability for:

- Up to 3x value of false claims submitted to the government (or payments evaded).
- Penalties ($10,781.40 and $21,562.80 per false claim) available.
MECHANICS OF WB-INITIATED FALSE CLAIMS ACT CASES
Who Can Be a Whistleblower?

• Archetypal WB = insider – current or former employee of the defendant
• Do not have to have clean hands.
  ✓ “It takes a rogue to catch a rogue.”
  ✓ Ok if whistleblower participated in the fraud; however, planner or initiator may receive reduced reward; and person convicted of crime arising from violation is not entitled to reward. 31 U.S.C. §3730(d)(3)
• Do not need to be U.S. citizen or resident.
Whistleblower Trends

- Competitors/Companies as WB
- Joint WBs – two or more WBs joining together to bring the case as co-WBs
- More international whistleblowers
Competitors/Companies as WB

• ROLE REVERSAL. Big Pharma usually target of WB suits, not the WB

• Sanofi-Aventis
  – August 2017: awarded $38.7 million of $465 million False Claims Act settlement w/ Mylan for knowingly misclassifying EpiPen as a generic drug to avoid paying Medicaid rebates

• Sanofi has been target of many successful WB lawsuits
Whistleblowers Without Borders: International Application of U.S. Whistleblower Laws

- Need Not be U.S. citizen or resident to be a WB under American WB laws
- Fraud must have U.S. nexus – Need not occur in the U.S.
International Whistleblowers

• Dinesh Thakur
  ✓ Naturalized U.S. Citizen of Indian origin
  ✓ 2003 – 2005: worked outside Delhi for Ranbaxy Laboratories, largest generic drug manufacturer in India
    ➢ Director & Global Head, Research Information & Portfolio Management
  ✓ Filed Whistleblower lawsuit under U.S. False Claims Act exposing Ranbaxy’s systemic product-testing failures and violations of good manufacturing practices
  ✓ U.S. Nexus: Ranbaxy drugs are sold in the U.S.
  ✓ Ranbaxy paid $500M settlement in 2013
    ➢ Thakur received $48.6M WB reward
Increase in International Whistleblowers
Filing Tips under SEC WB Program

London/UK: presence of financial services industry – securities fraud

- LIBOR rate rigging
- FX rate manipulation
Increase in International Whistleblowers
Filing Tips under SEC WB Program

Foreign Corrupt Practices Act (FCPA) violations

– Walmart (coming soon)
  • Reserved $283M for FCPA settlement w/ DOJ/SEC
    – $24M bribes Mexico to open stores
    – Also Brazil, China & India

– VimpelCom
  • $795M Global Settlement to win biz in Uzbekistan
    – $100M bribe to daughter of President
## Countries w/ Most SEC WBs (outside US)

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Who Can Be Sued?

- BOTH those who submitted the false claim to the Government AND
- Those who caused another person/entity to submit the false claim to the Government.

Examples:

- Medical device manufacturers who pay kickbacks to get doctors to order their device(s) cause those doctors to submit false claims.
- Part C: vendor hired by a Medicare Advantage Plan to review its members’ patient charts for diagnoses that risk adjust who causes MA Plan to submit false and unsupported diagnoses to CMS to increase the Plan’s capitation payment.
Process for Filing a WB Lawsuit

- Case must be filed under seal for at least 60 days.
  - Seal is routinely extended.
  - Average time a case is under seal is ~ 2 years.
- Purpose of the Seal: allow Government to investigate WB’s allegations without Defendant knowing
- Only the Government receives a copy of the WB complaint;
- Complaint is not publicly available/docket is sealed.
- Defendant is NOT served with the complaint.
Expiration of the Seal

Upon expiration of seal, the government either proceeds with the case or declines.

✓ If the government proceeds, the action is conducted by the government.
✓ If the government declines, the whistleblower has the right to continue the action on his/her own.
Significance of Government Intervention vs. Declination

- Likelihood of success increases exponentially when Government intervenes in WB case.
  - Government intervention in 15-20% of cases
  - Average recovery is ~$800,000 to the Government

- Where Government declines to join a WB case, its likelihood of success is often drastically reduced.
  - Historically, this had resulted in fewer WBs proceeding with case after Government declination (as is their right)
  - New Trend:
    - As # of WB cases increases, Government doesn’t have resources to join all meritorious WB cases and is sometimes declining even though believes case has merit
    - More whistleblowers moving forward with such cases
    - Largest recovery in declined case $450M (2015)
Average Lifespan of a Whistleblower Case

- Cases take a long time to resolve (typically between 3 and 7 years; many exceed 10 years)
  - Depends on complexity of the fraud
  - Scope of fraud (nationwide/spanning many years/multiple defendants/government declined often take longer)
Common Types of Healthcare Fraud

✓ Upcoding Diagnoses to increase Risk Adjustment Scores (Part C)
✓ Stark & Anti-Kickback Statute Violations
✓ Billing for Upcoded Medical Services
✓ Unbundling Services to Increase Reimbursement
✓ Best Price & Medicaid Rebate Fraud
✓ Billing for Medical Services that were not Performed
CASE STUDY: JES STALEY, CEO BARCLAYS
Crisis Management

• 3 attempts to unmask WB
  – Involved Barclays security staff, USPS postal inspector
• Resignations of key EEs involved
• Jes Staley still in place as CEO
• FCA poised to take action
Advice for Avoiding Whistleblower Lawsuits

• Vast majority of whistleblowers do **not** set out to be whistleblowers
  ✓ Most raise concerns internally (often repeatedly) & expect employer will fix them
  ✓ Only resort to whistleblowing when rebuffed by employer

• Heed what whistleblowers are saying
  ✓ Ensure Robust Compliance Program/internal whistleblower reporting procedure
  ✓ Investigate WB’s concerns
  ✓ Don’t blame the messenger / retaliate

• Change the Way you Think and Talk About Whistleblowers
  ✓ Canary in the coal mine
    ➢ Vital to health of organization
  ✓ Not snitch, tattle tale, rat
    ➢ disloyal
Advice for Avoiding Whistleblower Lawsuits

• Don’t take the easy way out. Releases in Severance Agreements are not a magic bullet.
  ✓ Whether U.S. courts will enforce a release of FCA claims within an employment or severance agreement:
    ➢ Generally, if the release is signed before the whistleblower files the complaint, then the release is unenforceable.
    ➢ If the release is signed after the complaint is filed, some courts have enforced the release.
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