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VIA EMAIL

Committee Secretary
Parliamentary Joint Committee on Corporation and Financial Services
PO Box 6100
Parliament House
Canberra ACT 2600

Re: *Joint Parliamentary Inquiry on Whistleblower Protections in the Corporate, Public, and Not-For-Profit Sectors*

Dear Committee Secretary:

We welcome the opportunity to submit our recommendations to the Joint Parliamentary Committee on Corporations and Financial Services regarding the Committee's inquiry into whistleblower protections in Australia's corporate, public, and not-for-profit sectors. We are United States attorneys at Constantine Cannon LLP, who primarily represent whistleblowers under the federal False Claims Act (FCA), the numerous equivalent state acts, and the whistleblower program of the United States Securities and Exchange Commission (SEC) created by the Dodd-Frank Act. We have limited our response to a single Term of Reference: *compensation arrangements in whistleblower legislation across different jurisdictions, including the bounty systems used in the United States of America*. For the reasons set forth below, we strongly believe Australia should implement a system of financial incentives for whistleblowing akin to the US system. Our recommendation is based on our substantial experience representing whistleblowers under the US statutes that financially incentivize whistleblowing -- primarily the FCA and the Dodd-Frank Act -- and the deep understanding we have gained of what motivates whistleblowers and of the significant risks they take and harm they face in reporting wrongdoing.

The False Claims Act

The FCA is by far the most widely used vehicle through which whistleblowers report financial frauds against the US government. It was originally enacted in 1863 during the United States Civil War to combat the fraudulent sale of substandard supplies to the Union Army such as rancid food and defective weapons. Recognizing the embattled government's limited resources and ability to detect and prosecute these frauds on its own, the law reached back to thirteenth-century England to revive the concept of *qui tam*, derived from the Latin phrase, "he who pursues this action on our Lord the King's behalf as well as his own." The *qui tam*

provisions of the FCA allow private citizens to bring suit on the government's behalf to recover government funds lost to fraud. The FCA encourages *qui tam* suits by rewarding these private citizens, known as relators, with fifteen to thirty percent of any government recovery obtained through the relator's suit.

Despite its lofty aspiration and early promise, the FCA was largely ignored in the century following the Civil War and then substantially weakened in the 1940s, when the US Congress sharply restricted the amount relators could recover from successful *qui tam* suits. The government's apparent loss of interest in the statute -- and in the concept of incenting whistleblowing -- was reversed in the 1980s, in the face of widespread reports of outrageous abuses by government contractors, including bills for $400 hammers, $1,000 bolts, and $7,000 coffeepots.

In response to these and other pervasive and continuing frauds against the federal fisc, Congress substantially amended the Act in 1986 -- and, again, in 2009 and 2010 -- to enhance the US government's ability to recover losses sustained as a result of fraud. Congress intended that the amendments encourage individuals with knowledge of fraud to disclose the information without fear of reprisals or government inaction, and to encourage private attorneys to commit legal resources to prosecuting fraud on the government's behalf. The most significant amendments included the imposition of triple damages on wrongdoers, an increase in the whistleblower reward ceiling to thirty percent, and the addition of significant anti-retaliation protections for whistleblowers.

By the mid-1990s, hundreds of millions of government dollars were recovered under the FCA every year, with tens of millions in rewards going to whistleblowers. By 2000, annual recoveries extended into the billions as the law's reach expanded beyond defense contractors to fraud in other industries, including healthcare and banking. The past eight years have seen an even greater increase in FCA enforcement. Total government recoveries since 2009 have topped $31.3 billion, and account for roughly sixty percent of all recoveries since the 1986 amendments to the Act.[1] In 2016 alone, the government recovered more than $4.7 billion, with nearly $3 billion originating from *qui tam* suits brought by whistleblowers.[2] There were more than 702 such whistleblower lawsuits filed last year, and roughly $519 million doled out in whistleblower rewards in the same period.[3]

Financial incentives are clearly a driving force behind the FCA's demonstrated success in combating fraud against the US government. Indeed, the United States Department of Justice (DOJ), Congress, and Supreme Court have repeatedly emphasized this fact. Frequent DOJ press releases laud the statute's incentive structure and trumpet whistleblowers' role in helping the

[1] https://www.justice.gov/opa/pr/justice-department-recovers-over-47-billion-false-claims-act-cases-fiscal-year-2016
[2] *Id.*
[3] *Id.*

government fight fraud. Congress and the Supreme Court have likewise highlighted the important role whistleblowers and whistleblower rewards have played in strengthening the Act. *See, e.g., Graham Cty. Soil & Water Dist. v. U.S. ex rel. Wilson*, 559 U.S. 280 (2010) ("We do not doubt that Congress passed the 1986 amendments . . . 'to strengthen the Government's hand in fighting fraud claims' and 'to encourage more private enforcement suits.'"); H.R. Rep. No. 660, 99th Cong., 2d Sess. 22 (1986) ("[T]he purpose of the 1986 amendments was to repeal overly-restrictive court interpretations of the qui tam statute [and to encourage] private individuals who are aware of fraud . . . to bring such information forward.").

The Dodd-Frank Act and the SEC Whistleblower Program

In July 2010, in response to the 2008 financial crisis, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act, known colloquially as "Dodd-Frank." One of the most important components of this broad overhaul of the US financial regulatory system was the enactment of the SEC Whistleblower Program, through which those with knowledge of securities laws violations are financially incented to share this information with the SEC. Like the FCA, the Dodd-Frank Act provides a whistleblower reward of up to thirty percent of any government recovery. In passing this legislation and overhauling an SEC whistleblower program that had previously lacked financial incentives -- and by all accounts had not been successful -- the US Congress recognized the critical role a bounty system plays in encouraging whistleblowers to come forward.

Since the passage of Dodd-Frank, whistleblower tips have flooded into the SEC, and recoveries and awards have been substantial. From the beginning of the SEC whistleblower program through the end of 2016, information and assistance provided by the thirty-four whistleblowers who received awards led to $584 million in financial sanctions against wrongdoers, including $346 million in disgorgement of ill-gotten gains and interest.[4] In 2016 alone, awards exceeded $57 million -- more than all award amounts issued in previous years combined.[5] All indications suggest the number of awards will continue to grow in coming years.

The SEC made clear in its most recent annual report on the whistleblower program that financially incenting whistleblowers is of paramount importance to the program's success: "We believe that the continued payment of significant awards, like those made this past year, will continue to incentivize company insiders, market participants, and others with knowledge of potential securities law violations to come forward and report their information to the agency."[6] The SEC further credits its whistleblower program as having "bolstered the agency's

[4] https://www.sec.gov/whistleblower/reportspubs/annual-reports/owb-annual-report-2016.pdf
[5] *Id.*
[6] *Id.*

enforcement efforts and aided harmed investors." By all accounts, the program has been a huge success.[7]

Just and Necessary Compensation

Aside from this clear empirical evidence that the US whistleblower reward system works, there is also a simple policy rationale for the use of financial incentives. They are just and necessary because they compensate whistleblowers for what will almost certainly be a tiresome and unpleasant ordeal. No question, laws protecting whistleblowers have vastly improved in recent years. But the risk of retaliation or some form of estrangement, alienation, or even blacklisting remains very real. We know this firsthand from our clients, and studies continually underscore the point. A 2013 National Business Ethics Survey conducted by nonprofit Ethics Resource Center (ERC) and published in 2015, reports that "[m]ore than one in five workers (21 percent) who reported misconduct said they suffered from retribution as a result . . . . Asked why they kept quiet about misconduct, more than one-third (34 percent) of those who declined to report said they feared payback from senior leadership. Thirty percent worried about retaliation from a supervisor, and 24 percent said their co-workers might react against them."[8] Financial incentives thus not only encourage whistleblowing, but also provide some measure of just recompense for the significant hardships so many whistleblowers suffer for standing up and speaking out.

Financial incentives also allow whistleblowers to more easily partner with qualified counsel to represent them through the legal process. The various whistleblower laws, particularly the FCA, are long and complex, with innumerable requirements and restrictions on the type of fraud or misconduct that is covered and the way the complaint must be presented to the government. Only through the promise of a sizeable reward will most whistleblowers be able to afford counsel or entice them to take up their representation. The involvement of counsel not only is of major importance to the whistleblower. It is critical for weeding out claims or complaints unworthy of the government's involvement, and for packaging those that are worthy with the legal arguments and evidence that makes the most efficient use of the government's limited resources.

Arguments Against Incentives Are Easily Defeated

Two principal arguments are typically made against whistleblower rewards. One, that rewards lead to frivolous filings and therefore waste government resources. And two, that encouraging whistleblowers to bring information to the government will discourage internal reporting and undermine internal ethics and compliance programs. Neither argument has held up in the US experience.

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[7] *Id.*
[8] https://www.ethics.org/ecihome/research/nbes/nbes-reports/nbes-2013

First, no evidence from any US agency supports the assertion that whistleblower rewards have led to frivolous filings. And given the involvement of counsel with most whistleblower claims, and the threat of court sanctions that accompany any frivolous filing under the FCA, it is unlikely there would be. In any event, the relevant question is not whether financial incentives result in a greater number of ultimately unsuccessful whistleblower complaints (even if some of them are in fact frivolous). It is whether the incentives have resulted in a greater number of meritorious whistleblower complaints, leading to a greater number of successful enforcement actions. As discussed above, under the FCA and through the SEC whistleblower program, successful enforcements have clearly increased.

Second, the concern that government incentives interfere with internal compliance programs is equally unfounded. This was one of the major arguments the business community made in unsuccessfully attempting to defeat the inclusion of a whistleblower rewards provision under Dodd-Frank. The truth is there is no evidence that financial rewards drive whistleblowers directly to the government at the expense of reporting internally to their employers. In fact, studies show just the opposite: in most cases, individuals who blew the whistle to the government only did so after attempting to work out issues internally. One study, also conducted by the ERC, found that only a tiny fraction of whistleblowers -- a mere 3 percent -- go directly to the government to report fraud or misconduct. Instead, they first work within their company to expose, and attempt to remedy, the wrong. Only after they attempt to work it out internally, do they then take their concerns to the government.

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Our own experience representing whistleblowers counsels that financial incentives are just and necessary compensation to individuals who often risk a great deal to report wrongdoing to the government. Likewise, the broad success of the US whistleblower regime demonstrates the key role such incentives play in not only recovering government funds lost to fraud and corruption, but also in encouraging strong internal compliance efforts and deterring further wrongdoing. Based on our experience -- and on the broader US experience -- we urge Australia to adopt compensation arrangements similar to those present in US whistleblower legislation as it moves toward improving and expanding its whistleblower regime.

Best regards,

Gordon Schnell
Rosie Dawn Griffin