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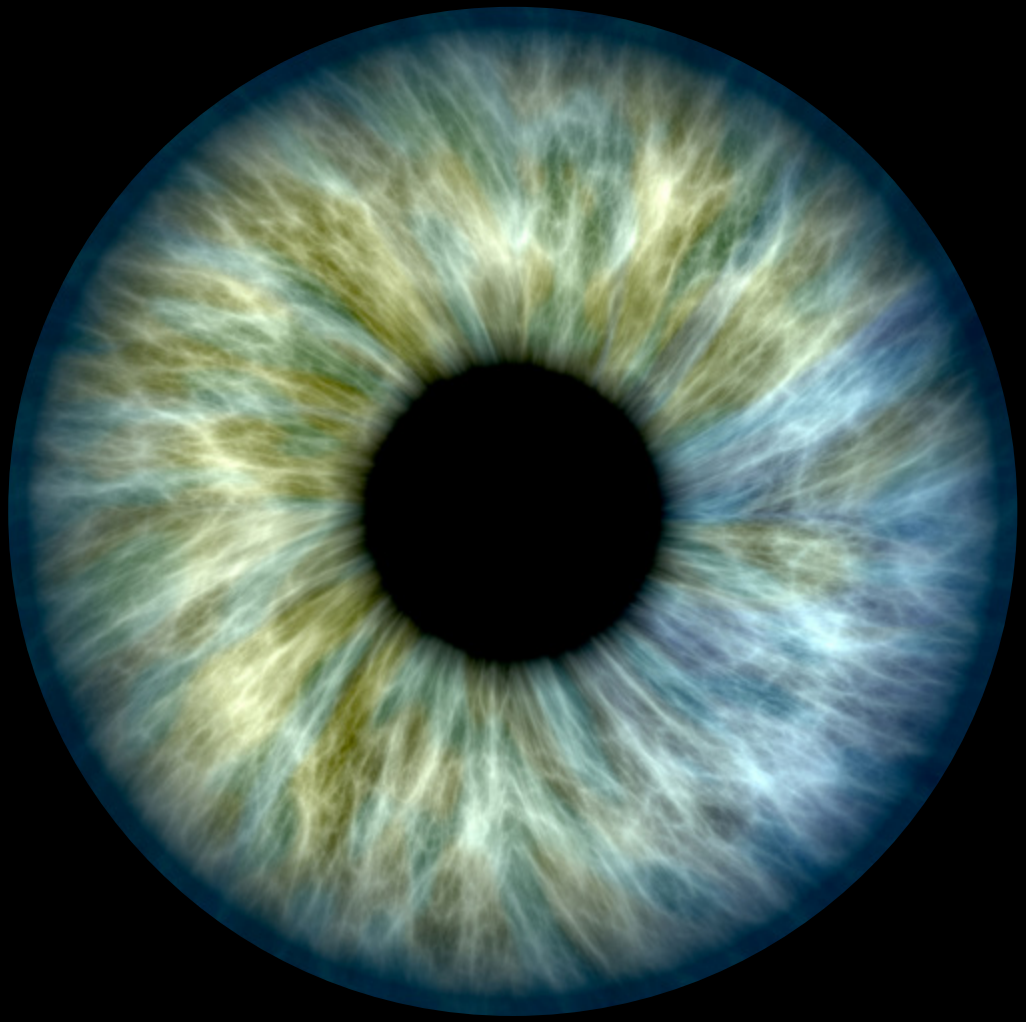
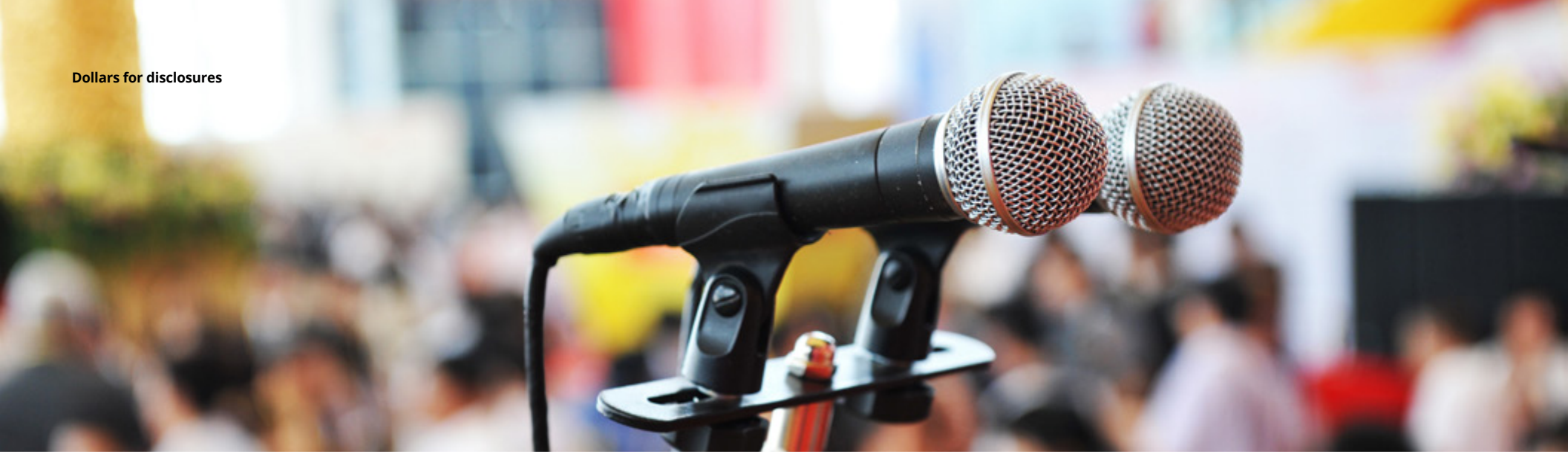


# Dollars for disclosures

The OSC's Office of the Whistleblower raises the stakes for internal reporting and investigations



## Introduction

On July 14, 2016, the Ontario Securities Commission (OSC) followed in the footsteps of the US Securities and Exchange Commission (SEC) and launched the Office of the Whistleblower, a program that provides paid compensation of up to $5 million to individuals who provide original information about violations of Ontario's securities laws that lead to enforcement penalties of at least $1 million. Coupled with new laws aimed at bolstering whistleblower protection,[1] the OSC has created renewed incentive for individuals with relevant knowledge to come forward.

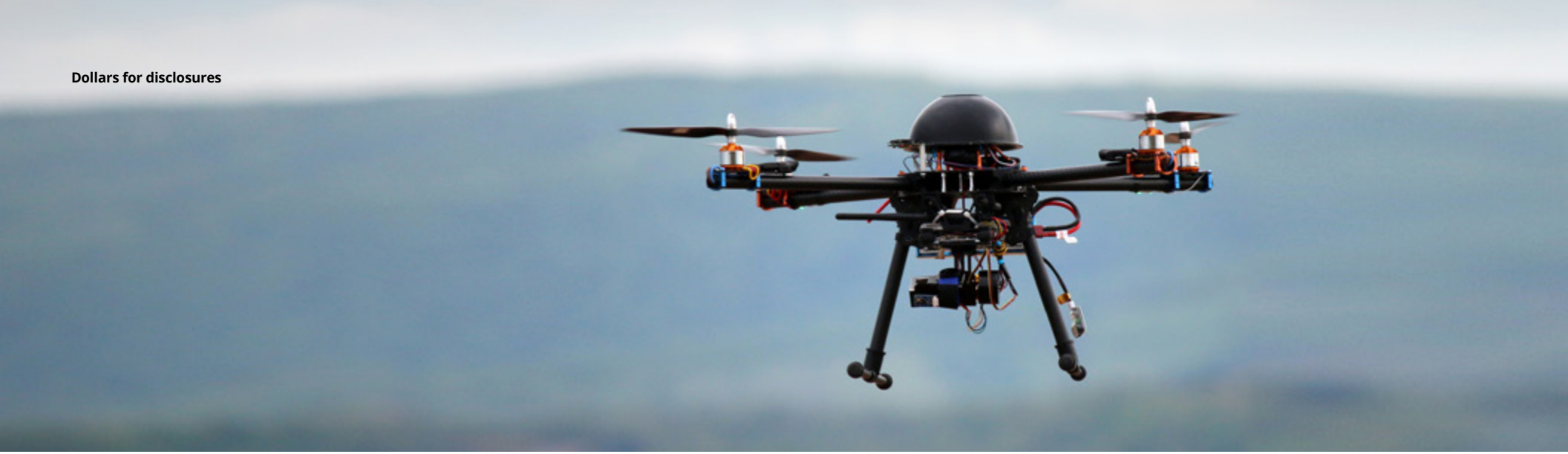
For publicly listed companies, securities issuers and dealers (i.e., affected organizations), the impact could be far reaching. For starters, the program is widely available – to current and former employees, suppliers and customers, among others. As a result, the OSC may know more about an organization's operating issues than many individuals at the organization itself.

While the OSC encourages individuals to report information internally, they may also report information directly to the OSC, completely bypassing whistleblowing avenues inside the organization. Additionally, internal documents supporting any allegations may be shared with regulators without the organization's knowledge.

While the intention is clearly to foster a more transparent environment for disclosure and regulation, situations may arise where the organization at the source of an allegation is the last to know, and is playing catch up to a regulatory investigation. How can affected organizations avoid being left in the dark? Consider taking the following protective steps:

- Conduct a critical evaluation of the existing internal control framework to ensure that adequate policies, processes, and procedures are in place and operating effectively, including a confidential reporting program.
- Develop a protocol for investigation of issues raised internally or by regulators.

1. Securities Act, Part XXI.2, Protection from Reprisals



## Evaluation of internal control framework

An entity's first line of defense against violations of securities law is a robust internal control and compliance framework. Key attributes of a well-designed control framework include:

- Adequate tone from the top clearly articulating a "culture of compliance"
- Sufficient oversight and resources
- Policies, processes, and controls to prevent and detect irregularities
- Periodic assessment of the specific risks facing the organization
- Education and training for employees and business partners
- Adequate incentives and disciplinary measures
- Sufficient due diligence procedures, including employees and business partners
- A confidential reporting system
- Periodic testing and review

Past enforcement activity has shown that even where no wrongdoing is identified, the OSC may still impose fines for failure to maintain proper standards for internal controls and supervision[2]. Additionally, the OSC expects that market participants will investigate any breakdown in internal controls, take corrective action, and implement new systems[3]. A failure to correct an internal control problem identified to senior management or the board may also exclude an entity from qualifying under the OSC's Credit for Cooperation program[4].

Integral to an effective internal control environment are proper channels for individuals to share relevant information, on a confidential basis if desired. A confidential reporting program is imperative to a healthy control environment, and one of the most effective tools available to an organization to assess the extent to which its policies and procedures have been implemented.

Key considerations for an organization's confidential reporting program include:

- Is it inclusive? Is it open to employees, suppliers, customers, and others with relevant information?
- Is it accessible? Can individuals reach an outlet at any time, from anywhere in the world? Has access been tested?
- Is it multi-medium? Are concerns raised through a hotline, email, social media, or an anonymous hand-delivered letter all dealt with in the same way?
- Do people know about it? Is information about the confidential reporting program widely available and likely to be seen by all stakeholders?
- Is information actioned? Is there an individual with appropriate authority responsible for reviewing allegations and developing an appropriate investigative response?

2. Numerous Settlement Agreements between staff of the Commission and mutual fund dealers, including Quadrus Investment Services.
3. OSC Staff Notice 15-702 Revised Credit for Cooperation Program 1.1.1, item 8
4. OSC Staff Notice 15-702 Revised Credit for Cooperation Program 1.1.1, item 12(i)

## Investigative protocol

The OSC's Credit for Cooperation program articulates the commission's view that market participants are expected to fully investigate any matters where an employee, officer, or director may have acted contrary to securities law[5]. Yet there is no requirement for whistleblowers to report information internally before contacting the OSC, and OSC staff do not, as a matter of course, publicly disclose the existence of, or details about, an investigation. Where information is reported internally, whistleblowers can remain eligible for an award provided they report the same information to the OSC within 120 days of making an internal report.

It is therefore critical that affected organizations react quickly when allegations are raised – whether internally, or through disclosure of a regulatory investigation already underway. Developing a response plan with a regulator at your door may result in hasty or unsupported decisions that can impact the scope of an investigation and potential enforcement action.

Affected organizations should develop a protocol for conducting an investigation following receipt of insider information. Such a protocol should, at a minimum:

- Be clearly documented, outlining roles and responsibilities, with consideration of how those roles might change if specific individuals are implicated. Consider if the actual operation of the business may be hindered by an investigation, and develop a business continuity plan to minimize disruption.
- Establish a steering committee with ultimate oversight for investigative activities. In many instances this responsibility will rest with the Board of Directors, who may form a special committee. Oversight should rest with a group of individuals with an appropriate mix of experience and skills. Finance, Human Resources and Technology, for instance, should each have different perspectives and responsibilities in an investigation.
- Identify factors suggesting that outside expertise is required, including legal counsel, forensic accountants, or other advisors. Important decisions need to be made up front, particularly with respect to dealings with whistleblowers themselves and the preservation of electronic evidence. Retaining outside experts early will ensure the organization has a well-rounded perspective based on practical experience.
- Outline a communications strategy, with some guidance on what can be shared, by whom, and when, both internally and externally. The reputational fallout from a poorly managed communications strategy can be more devastating than any resulting fines or penalties.

5. OSC Staff Notice 15-702 Revised Credit for Cooperation Program 1.1.1, item 9

## Conclusion

While the OSC's new whistleblowing program has received some criticism, affected organizations should also see this as an opportunity to prioritize internal control and compliance efforts. Profiteering informants will inevitably emerge, but the calibre of information that would likely attract a material payout under the program should be even more valuable to an organization than it is to the OSC. If individuals have information worth sharing, organizations should ensure that they are comfortable and capable of sharing it internally, where the situation can be better controlled.

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## By the numbers: The US experience

The SEC experience in the US may provide some insight into how the OSC's Office of the Whistleblower program may unfold north of the border:

- 2 - # of cases denied due to willful false claims being made between July 18, 2012 and July 19, 2016
- 2 to 4 years – the average lifecycle of an SEC investigation into a whistleblower complaint
- 9 – average annual percentage increase in the volume of tips reported throughout 2013 to 2015
- 18 - Percentage of complaints related to "Corporate Disclosures and Financials," the single largest category of complaint outside of "Other" (24%)
- 50 - percentage of successful complaints raised by current and former employees in 2015
- 80 - percentage of current and former employees that issued complaints and reported internally
- 95 – Number of countries outside of the US from which tips originated in 2015. The UK provided the most tips, followed by Canada

*– 2015 Annual Report To Congress on the Dodd-Frank Whistblower Program*

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