

- ▶ Dodd-Frank whistleblower incentives may foster an adversarial culture
- ▶ An organizational ombudsman may be a more effective alternative
- ▶ Ombudsman an informal channel that provides complete anonymity
- ▶ Establishing the office shows that company values honesty and candor

By Jonathan McBride and Stephen Norman

Time for an ombudsman?

The whistleblower provisions included in the Dodd-Frank Wall Street Reform and Consumer Protection Act legislation present a unique challenge to corporate executives and directors committed to improved governance and creating cultures of trust and ethical conduct within their organization.

The rules are designed to entice whistleblowers to report on possible violations or questionable conduct by offering significant financial rewards if the information leads to a fine and/or settlement with the SEC or Department of Justice.

In its current form, whistleblowers are entitled to a percentage of the final settlement or action amount – potentially a very large sum indeed. But Congress's good intentions in allowing the SEC to create an environment that encourages whistleblowers to come forward may have serious unintended consequences and may not achieve the desired result.

The unintended consequence of greatest concern is that the whistleblower protection provisions in Dodd-Frank may foster an adversarial relationship between employees and employers. With the offer of a substantial 'bounty' for reporting questionable conduct to the SEC, employees become strongly tempted to consider blowing the whistle as a first resort, sidestepping internal channels and thus minimizing the opportunity for the company to investigate and promptly rectify the issue.

The SEC, in its proposed regulation to implement

the Dodd-Frank legislation, recognizes this problem and provides enhanced financial incentives for individuals who first go to the company's internal compliance function with an issue that might ultimately be the subject of whistleblowing. The risk, however, is that such defensive measures will detract from the more fundamental need to create a safe place for individuals to take their concerns within their organization.



The last resort?

Ideally, whistleblowing should be used only after an individual has exhausted the internal corporate channels of communication. The US Sentencing Guidelines, SOX, the NYSE and NASDAQ OMX already mandate formal mechanisms where employees can expose malfeasance without fear of retaliation or retribution.

Corporations have responded with the widespread adoption or creation of ethics offices, compliance offices, hotlines and other formal channels through which employees can raise concerns. And yet, however attractive they may be, these formal programs often require the employee to reveal him or herself to management. As a result, they are not always effective because the workforce may be fearful of using them.

One possible solution could be the creation of an independent ombudsman to deal with whistleblowing situations. Because an office of ombudsman provides anonymity, its presence may be one of the most powerful

governance tools corporate directors and management have at their disposal today. An organizational ombudsman's office is an informal, independent, neutral and confidential resource. It is neither an advocate for the employees, nor for the company – it is an advocate for fair process.

By establishing an office of ombudsman, a corporation opens the door for employees to speak about potentially serious issues they might otherwise be reluctant to reveal to superiors within the company due to uncertainty or fears of retaliation or ostracism.

Also, the fact that a corporation takes the initiative to establish a function that is safe and confidential conveys a positive impression about how that organization's leadership thinks about its employees. It communicates in a credible way that management welcomes information about potential problems and that it wants its employees to surface and resolve problems in a manner that is non-threatening to the employee.

The presence of an organizational ombudsman conveys several useful messages about the company that establishes such an office:

- ▶ As a matter of policy, the corporation wants to foster trust, candor and accountability. This is a channel staffed by skilled professionals where the employee, as a matter of first resort, can go to be heard and to be coached in the options for effective action.
- ▶ The company acknowledges employees' hesitancy to raise certain issues with formal channels such as their direct supervisor or the human resources department, ethics or compliance office, general counsel, hotline or audit committee, because when they go down this route they have put the organization 'on notice'. As a consequence, the company will have to undertake a formal investigation and any prospect of maintaining employee confidentiality is greatly diminished.
- ▶ Because the ombudsman is an informal channel, it is not a 'location of notice'. This means that if an employee raises a particularly contentious issue, the organization will not know he or she has done so. Thus the employee is safe to assess whether and/or how to escalate the issue, and what the implications are of choosing a particular course of action. It is

safe and confidential; no one will know that the employee has visited with the ombudsman.

The bottom line

Establishing an office of ombudsman creates a safe place for employees to sort out their concerns and evaluate their options. It creates a supplementary channel for employees who fear the negative experience of 'ratting out' their organization. In this constructive context, where employees can participate in creating a work culture that fosters candor, trust and accountability, whistleblowing becomes a last resort, seldom needed.

In addition, because an organizational ombudsman makes periodic reports to the audit committee or the board on emerging issues of concern (with no attribution, to safeguard those who have come to the ombudsman), the board has an early warning system that can surface and resolve problems before they become costly, and can identify areas of potential weakness in the corporation. It's a win-win for everyone.

An office of ombudsman more than pays for itself. Assessments conducted by John Zinsser of Pacifica Human Communications, a leading expert on ombudsman program performance metrics, show that for every \$1 invested in the ombudsman function, between \$14 and \$23 of value is ultimately returned to the organization. This is a big win for the bottom line.

However well intentioned, the Dodd-Frank Act, with its monetary inducements to reward whistleblowers, fails to promote one of the most effective in-house ways of identifying and resolving instances of corporate malfeasance. Establishing an office of ombudsman is a proven means of enabling corporate leaders to address the continuous challenge of exposing potential malfeasance – before it becomes a threat to the corporate brand. CS

Establishing an ombudsman's office creates a safe place for employees to sort out their concerns

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