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Successful Defense in the Age of the Whistleblower

In 1863, following reports of unscrupulous merchants selling diseased mules to the Union Army, Congress passed the False Claims Act to deter the submission of fraudulent claims for payment to the government. Under the Act's *qui tam* provisions, private citizens for the first time could institute actions on behalf of the government to recover damages and were entitled to retain a portion of the recovery. Whistleblower claims have been a part of the American legal landscape ever since.

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Provisions for whistleblower bounties and protection can now be found in statutes involving such diverse areas as federal contracting, taxation, and environmental protection. Whistleblower activity has been key in increasing enforcement of the federal Foreign Corrupt Practices Act, 15 U.S.C. §§ 78dd-1, *et seq.* In the securities field, Congress wrote whistleblower protections into the 2002 Sarbanes-Oxley law, 18 U.S.C. § 1514A, and last year included a provision in the Dodd-Frank Act that requires the SEC to reward whistleblowers with at least 10 percent, and as much as 30 percent, of the government's recovery in whistleblower-initiated cases. 15 U.S.C. § 78u-5(b)(1). Like many states, California has enacted its own "whistleblower protection" statute, Cal. Gov. Code §§ 8547-8547.12, and state False Claims Act. Cal. Gov. Code §§ 12650, *et seq.*

According to several estimates, the federal government has recovered more than $25 billion under the False Claims Act since the statute was strengthened in 1986. SEC officials have stated that they expect the number of whistleblower claims to explode, and plaintiffs' firms are increasingly promoting their experience in representing whistleblowers.

Business litigators can play a critical role in helping companies deal with whistleblower issues. At the outset, they can assist in developing strong compliance policies and procedures to minimize the occurrence of claims and to increase the chances that any complaints will be dealt with internally. Even the best policies, however, will not eliminate whistleblower cases, so counsel will also need to develop effective strategies to defend them.

An Ounce of Prevention

The effort to defeat a whistleblower claim should begin long before a claim arises. Design or revision of the client's compliance policies and procedures is the most cost-effective approach. Not only will a strong compliance program help reduce the incidence of conduct that could lead to whistleblower activity, but it will also benefit the defense of any claims that are made.

As will be explained below, it is very advantageous for a company to be able to investigate claims internally, before it faces a government inquiry. An effective compliance program works in two ways to increase the likelihood that a whistleblower claim can be investigated internally. First, an employee who is convinced that her complaint will be investigated thoroughly and fairly is more likely to raise her concerns internally. Second, even if the whistleblower goes outside the company, a resource-constrained agency may permit the company to investigate the allegations if the company can convince the agency that it will conduct a credible investigation. The SEC, for example, has made it clear that it is more likely to permit companies with well-developed compliance programs and credible

plans to investigate to perform their own investigations of whistleblower claims, so long as they report their findings back to the agency.

A rigorous compliance program is also beneficial when a whistleblower complaint proceeds to trial. The existence of well-established internal procedures may form a sound basis for challenging the whistleblower's motivations. Why, for example, did she bypass a time-tested, confidential hotline and go straight to the government? Was she motivated by money or personal animus?

The Benefits of Internal Investigation

If an employee believes misconduct has occurred, it is difficult if not impossible to prevent her from reporting it to the government. The SEC's new whistleblower rules, for example, forbid companies to use confidentiality agreements or similar devices to keep employees from "reporting out," although in certain circumstances compliance personnel or in-house counsel may be required to report internally first. 17 C.F.R. §§ 240.21F-4(b)(4)(iii)(B). In addition, the provisions for a percentage recovery for whistleblowers, either in a False Claims Act *qui tam* action or the SEC's whistleblower rules, provide a powerful monetary incentive for employees to take their concerns outside the company instead of relying on internal processes.

Even so, companies should encourage employees to report internally. The benefits to the company of conducting its own investigation are hard to overstate. If the employee reports out and a government agency contacts the company concerning a whistleblower claim, counsel should make every effort to engage agency personnel early on and to convince them that the company should be permitted to perform its own investigation.

Think of the vast differences between responding to a government investigation and conducting one on your own. The government investigation is out of your control; you probably don't know what information the government has been provided or the scope of its investigation; you don't control the timing of the proceedings or the possibility that the government will try to contact former employees without your knowledge; and there is always the possibility that in the course of the inquiry, the investigators may uncover (or think they have uncovered) new areas of concern. By contrast, an internal investigation is one that is ultimately under the control of the board or a board committee, its progress and probable costs can be tracked, and it has a foreseeable end date.

Even when a whistleblower complaint remains internal and the company has not yet decided whether to report the allegations to the government, any internal investigation should be thorough, impartial, and well documented. The investigative body and the attorneys it retains must be conflict-free. Counsel should plan for the possibility that the company will present the results of the investigation to several key audiences, including the board, independent auditors, the government, or even a plaintiff in future litigation. Therefore, process matters greatly, and counsel must be prepared to explain their choices at every step of the way. Were all of the potentially critical witnesses interviewed? Were relevant documents collected and reviewed? What search terms were used in the review of electronic data? Counsel should review investigative protocols in advance with those who will be briefed at the end of the investigation. Otherwise, the results of the investigation may be open to attack, or critical steps may have to be repeated later.

In conducting an investigation, the company needs to be particularly careful to preserve the attorney-client privilege and attorney work product. Communications between investigating counsel and a government agency are likely to be considered nonprivileged, and counsel should be careful when providing written documents, reports, or analyses to the government. Even a promise by the government not to claim that a privilege has been waived may not be sufficient to shield the disclosures from a third-party subpoena. Fortunately, most government attorneys understand this issue and are willing to work constructively with companies and their counsel to minimize potential privilege waivers.

Dealing With a Government Investigation

Assume, however, that a company learns of a whistleblower claim only when it is contacted by a government agency, and the agency refuses to suspend its investigation while the company conducts its own inquiry. Even in this situation, counsel should be proactive and should not simply wait to respond to the government's requests or subpoenas. Mounting an aggressive defense requires counsel to learn as much as possible about the identity of the whistleblower and the nature of her complaint, and to plan avenues of response and attack at the earliest stages.

At the same time, defense counsel should attempt to engage government attorneys in a constructive manner throughout the process. It may or may not be possible to obtain helpful information directly; False Claims Act cases are kept under seal for months or years, and whistleblower statutes typically require the government to maintain the confidentiality of the informant's identity. Even so, establishing a relationship of trust and credibility with the agency may open up avenues of discussion that will be helpful in shaping the direction of the inquiry, or at least in helping the defense understand where the government may be going.

It will certainly be helpful to the company to know the whistleblower's identity as soon as it can—not solely for the purpose of impeaching her credibility, but also for the purpose of assessing the seriousness of her allegations of misconduct, and the identities and credibility of potential fact witnesses. If the whistleblower is a discharged employee or one with a history of performance or disciplinary problems, those facts will be important to know. Counsel may decide to bring these facts to the attention

of the investigating authority at the earliest possible time. Similarly, it will be helpful to know if the whistleblower's accusations relate to other employees with known performance issues.

However, the company should not be so single-minded about learning the identity of the whistleblower that it loses sight of the importance of assessing the alleged conduct that is under investigation. Even if the government will not postpone its inquiry while the company conducts an internal investigation, the company should get out in front of the issue to the greatest extent possible, looking for documents before the government requires them to be turned over, locating and interviewing witnesses before they are subpoenaed, and developing evidence that will support a defense narrative—the kind of evidence that the government has no incentive to develop and often overlooks. Even if it turns out that misconduct has occurred, demonstrating that the conduct was isolated or aberrational, or developing mitigating evidence, is vitally important.

Staying abreast of—or even ahead of—the government enables the company to develop an effective defense long before the matter proceeds to a formal accusation or trial. The earlier the company can credibly suggest to the government that there may be problems with the accusations, or provide an alternative explanation for the events at issue, the better its chances of derailing or limiting an investigation before it acquires a bureaucratic momentum that may make it difficult to stop. At a time when the company wishes to discuss settlement of the potential charges, or to argue for termination of the investigation without any action being taken, it will be necessary for the company to be able to articulate a factually supported narrative explaining the events that are under scrutiny. The company needs to be able to explain why the conduct under examination was not improper, or why it did not have serious consequences, or why the government's theory is based on an unreliable informant or dubious information. It is not possible to present these arguments forcefully unless they have been thoroughly developed and tested.

Discovery and Trial Strategies

In some cases, the only way to acquire certain knowledge of the whistleblower's identity will be to refuse to settle with the government at the investigative stage, resulting in the filing of a complaint and a possible trial. Although doing so will result in negative publicity, the disadvantage may not be as great as it first appears, because settling with the government before formal charges are filed will almost certainly result in a government press release and attendant publicity. The SEC, for example, requires settling parties to agree that they will not deny that the charges have a basis in fact. 17 C.F.R. § 202.5(e).

Once the matter proceeds beyond the investigative stage to a formal complaint, the tools available to the defense expand considerably. For one thing, the company can now discover the whistleblower's identity through formal discovery. Once this information has been secured, subsequent discovery requests should call for all interview notes, testimony transcripts, and investigative reports concerning the informant and any information she and other witnesses provided to the government. Third-party subpoenas may help to unearth critical evidence that might not have been possible to obtain during the investigative stage. In civil cases, the deposition of the informant will be a critical event. The defense should be prepared to make the whistleblower a central focus of the case, and the company should consider using all available, lawful means to investigate the whistleblower, her background, and any motivation she may have to stretch or distort the truth.

The defense should be careful not to overplay its hand with the whistleblower, however, particularly if she is sympathetic or credible, or if her allegations have a solid factual basis. Whether the defense unleashes an all-out attack on the whistleblower's credibility or merely suggests that she is somehow misguided or misinformed will depend on a careful strategic calculation, but neither possibility should be entirely ruled out as the case is being prepared for trial.

In addition, the defendant company must not ignore the accusations themselves, particularly if they appear to have merit. Where the accusations focus on questionable policies or practices as opposed to alleged rogue employees, it is important to address institutional problems without awaiting a jury verdict. If the company also had a strong culture of compliance prior to the alleged misconduct, it will be important to develop those facts, both to increase the fact-finder's sympathy for the entity and to reduce the likelihood of a finding that misconduct resulted from a pervasive culture of unethical behavior.

Business litigators play a critical role in helping companies deal with a predicted surge in whistleblower complaints. They should help companies focus attention on existing policies in order to create a workplace environment that reduces accusations of misconduct. When a complaint is made, they can assist in conducting a prompt and thorough investigation. If the case ultimately proceeds to trial, they will maximize the client's chances of success by constructing a defense long before the accusation becomes public.

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