

## When a Whistleblower Is Wrong—Time for a Proactive Defense

### *Bloomberg Law*

By: John Carney & Alexandra Karambelas

January 6, 2022

<https://news.bloomberglaw.com/us-law-week/when-a-whistleblower-is-wrong-time-for-a-proactive-defense>

The number of SEC whistleblower complaints and award amounts set records in 2021. BakerHostetler’s John Carney and Alexandra Karambelas acknowledge the growth, but say some whistleblower complaints are baseless and made in bad faith. They offer companies a plan for resolving these claims before they cost companies, time, money, and their reputation.

The Securities and Exchange Commission’s chief of [the Office of the Whistleblower paid out](#) over half a billion dollars in whistleblower awards in 2021—more than any other federal agency. This compelling financial incentive resulted in more than 12,200 whistleblower tips in 2021, nearly doubling the previous year’s number, but it also resulted in numerous baseless and even bad faith tips.

Indeed, a week after announcing that the SEC’s whistleblower program had paid out record-breaking awards, the commission [announced](#) that it had banned two individuals from the program, each of whom had filed hundreds of frivolous claims and award applications.

The problem of bad faith whistleblowers is not limited to the SEC. According to the Occupational Safety and Health Administration’s whistleblower [statistics](#), in 2020, nearly three-quarters of the whistleblower reports submitted to OSHA were either dismissed or withdrawn.

It is laudable that the SEC has taken some limited proactive steps to curb bad faith tipsters, but many public companies and senior officers still find themselves under investigation for events that never happened or were fundamentally misunderstood. Each baseless complaint can result in large costs in terms of both time and money, even when the claim is ultimately dismissed.

With this in mind, it is critical that companies take prompt, proactive steps to protect the company and its officers. Below are four proactive steps to plan for resolving a baseless matter before time, money, and reputation are lost.

### **Four-Point Plan**

#### **Communicate with Regulators**

Even in bad faith cases, companies should be up front with regulators as quickly as possible if the matter has been, or is likely to be, reported to the SEC. The company should let the enforcement staff know that it will come to them with as much information as possible.

When the complaint already has been reported internally, companies can come to regulators with the results of an internal investigation to try to keep them from getting invested in a meritless case.

## **Explain the Logical Inconsistency, Impossibility**

It's not uncommon for unfounded whistleblower complaints to come from an employee who's merely mistaken about something they genuinely believed to be a violation.

For example, an employee might believe they have a valid whistleblower claim because they see that loss reserves in one region or division are inadequate. However, while loss reserves in one region were too low, a surplus existed in another region, and, collectively, on the balance sheet, the loss reserves were properly stated. Even though there's no wrongdoing here, resolving this kind of meritless complaint can be a long and expensive process if not dealt with quickly.

Once a claim is made to the SEC, company counsel should explain to the enforcement staff why the employee didn't have visibility on the issue they're claiming to report or why the supposed violation is impossible or illogical. Providing this information to the agency early on will help ensure SEC staff feel confident that they are getting a complete picture of the situation, and may avoid an even longer and more expensive process.

## **Show the Bad Faith**

When companies suspect the supposed whistleblower is making a malicious or frivolous claim out of bad faith, it's important to give regulators evidence of bias. To that end, it's essential to document any employee misconduct. Showing that a supposed whistleblower with a documented history of misconduct was terminated for cause prior to the report will go a long way to showing the employee's reason to fabricate a complaint.

It's equally important to avoid taking any retaliatory action against a whistleblower (currently employed or separated), even if the company believes the person is acting in bad faith. The best defense to a bad-faith reporter, as well as false claims of retaliation, is clear, contemporaneous documentation of the employee's performance issues, which may suggest reasons to lie.

Similarly, all communications with the reporter should be memorialized in writing as soon as they occur. Providing regulators with contemporaneous, documentary evidence showing that the employee is not making a good faith report is job one.

## **Act Quickly**

For each of these steps, it is critical to act quickly in order to avoid regulators becoming invested in a meritless complaint.

Regulators have a duty to investigate and follow up on tips, but they are as susceptible as anyone to the sunk-cost fallacy. Once investigators have already devoted significant time and resources to a claim, they could be more likely to dig in their heels and sink more resources into the complaint.

Therefore, companies and executives should consult with attorneys well versed in this area as soon as they become aware of a whistleblower report so they can respond to the claim swiftly and effectively.

The number of SEC whistleblower reports, along with the associated financial incentives for reporting, have increased nearly every year since the program's inception in 2011, and are expected to continue to rise in 2022. Whistleblower awards range from 10-30% of the money collected when the monetary sanctions imposed on companies exceed \$1 million, and these awards have increased as the number of reports and the amount of sanctions have increased each year.

Having systems in place to encourage internal reporting can help prevent these types of claims from going forward in the first place.

Baseless and malicious complaints will continue to impact companies and executives, seeking legal advice as soon as a complaint is received and adopting these proactive strategies can dramatically limit the potential impact of a meritless claim.

*This column does not necessarily reflect the opinion of The Bureau of National Affairs, Inc. or its owners.*

[Write for Us: Author Guidelines](#)

#### **Author Information**

*[John Carney](#) serves as BakerHostetler's SEC defense team co-leader and specializes in whistleblower matters. He is a former DOJ securities fraud chief, assistant U.S. attorney, SEC senior counsel, and certified public accountant at a Big Four accounting firm.*

*Alexandra Karambelas is a first year associate (admission pending) in BakerHostetler's New York office.*