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To: **The Secretary**
Ontario Securities Commission
Email: comments@osc.gov.on.ca

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Re: **Comments on the - OSC Staff Consultation Paper 15-401: Proposed Framework for an OSC Whistleblower Program**

Introduction:

Thank you for the opportunity to comment as I strongly support the OSC moving ahead with a whistleblower reward and protection program in Canada.

I have been an Internal Auditor for over 20+ years with large publicly traded companies and in my opinion Internal Auditors are often in the best position within companies to identify and report on serious fraud and non compliance issues. However, Internal Auditors are employees of the company and are often manipulated and coerced to conceal and not report sensitive issues concerning serious non compliance and fraud. In these situations, Internal Auditors need legal protection to come forward and report issues directly to regulatory authorities.

For example, I have personally reported on several cases of non compliance with securities regulations and Management Fraud activity over the years as an Internal Auditor. Sadly, in the majority of cases, audit findings concerning fraud & corruption have not been addressed effectively by internal compliance systems and have been concealed and not disclosed to external auditors and securities regulators.

The common approach used by Management is to conceal issues from attention by manipulating the internal audit process to revise down or eliminate the findings in the

reports or to deliberately conceal the findings from being reported by using various tactics including; directing scope changes in the audits away from the sensitive areas, not approving audits of sensitive areas to begin with, deleting sensitive findings from completed audit reports or simply cancelling audits before reports can be issued.

When Management manipulates the Internal Audit process to conceal findings, the internal auditor quickly finds themselves in a difficult ethical dilemma and potentially career ending situation. If the auditor succumbs to pressure and agrees to conceal the audit findings from attention they become complicit & culpable in the unethical behaviour themselves, which contravenes audit standards and professional obligations.

If the Auditor elects to stand up and comply with audit standards and ethical policies and refuses to conceal the audit findings – they are simply terminated without cause and notice at the company's discretion. In order to receive employment severance compensation they are made to sign confidentiality release agreements which prohibit them from disclosing the findings to outside parties, including securities regulators. Terminating the auditor without cause is an effective method to silence them and to prevent disclosure.

If the Auditor refuses to sign the severance agreement due to the confidentiality provisions they are forced to take the company to court claiming wrongful dismissal which is an expensive and lengthy legal process - which most individual auditors are not in a position to pursue. Job references are withheld and auditors will likely suffer career reputation damage making the job search process more difficult. Internal Auditing is a relatively small job market and word of scandal or controversy travels fast within the Internal Audit community impairing a successful job search.

Internal Auditors are a unique source of high quality and specific information concerning non compliance and fraudulent activity. However, the current system does not provide adequate protection for internal auditors to come forward and to report information without fear of reprisal and termination. In more serious situations, auditors may also fear that their personal security may be at risk in cases where audit findings involve companies owned by organized crime and fraudulent billing schemes such as in the construction industry.

Robert Patterson

My Specific Comments and Responses to Questions:

Individuals with compliance roles and those who acquire information as a result of an internal process for reporting misconduct

We propose to exclude from eligibility the Chief Compliance Officer (CCO) (or equivalent position) and officers and directors who learn of misconduct as a result of an entity's internal processes for dealing with potential violations of securities laws.

However, not all those who learn of possible misconduct through an internal reporting process or investigation would be ineligible. For example, compliance department staff who are aware of the misconduct and observe a failure by the CCO to address it, would be able to provide information to the OSC and be considered for an award, provided all other eligibility criteria are satisfied.

I agree with this suggestion above that compliance dept staff should be eligible for awards provided that they can demonstrate that they have tried to report issues properly through their internal reporting protocols.

However, in some situations, auditors may be prevented from reporting on sensitive issues and if they can demonstrate that they were directed to not report issues – they should still qualify for rewards if they come forward.

Internal reporting

We recognize that robust internal compliance programs play a key role in protecting the integrity of the capital markets and we encourage individuals to report to their compliance personnel as a first step. We do not propose to require individuals to report conduct internally prior to providing information to the OSC. However, we would encourage individuals to do so. See further discussion in section 10.

Since one of the factors for eligibility is that information must not already be known to the OSC, a potential whistleblower may be concerned that reporting to compliance personnel instead of directly to the OSC may result in the whistleblower not meeting the eligibility criteria for the program if someone else reports directly to the OSC during the period of time the matter is being investigated by the organization. If the whistleblower subsequently reports the matter to the OSC due to a failure by the organization to

respond to the matter, the information would already be known to the OSC. However, in these circumstances we would consider the timing of the initial internal reporting to determine who provided the information first. In certain circumstances, it may be possible for more than one individual to qualify as a whistleblower.

Under the SEC's Whistleblower Program, if an individual reports a matter internally and then submits the information to the SEC within 120 days, the date that the person submitted the information internally is the date that the SEC will consider in determining whistleblower eligibility. The intent is to promote individuals reporting internally while still maintaining their eligibility for a whistleblower award

5. Should the Chief Compliance Officer or equivalent position be ineligible for a whistleblower award?

No, I feel the Chief Compliance officer or equivalent position – should still be eligible for a reward in certain circumstances.

However, I feel the requirements to receive rewards for persons at these job levels should be more stringent and specific for them to qualify. For example, if a CCO (VP of Audit, etc) reported to the Audit committee and nothing was done to address the issue that should qualify. Or if the CCO was fired before they could report to the audit committee that might also qualify them.

Generally, though I agree that persons at the CCO level are compensated for the risks of those positions and are expected to report as part of their job responsibilities. So the burden of proof should be higher.

6. Do you agree that individuals should not be required to report misconduct to their organizations' internal compliance programs in order to be eligible for a whistleblower award?

Yes – in certain situations the internal compliance reporting programs may be corrupt or not reliable. I know of one such situation where an auditor reported a sensitive fraud issue to the official internal ethics hotline. The issue and their identity was disclosed to

the CEO by the hotline staff and the auditor was fired and escorted out of the building within an hour of the issues being reported to the CEO.

Under some circumstances individuals should be free to directly report issues to regulatory authorities.

8. Whistleblower Protection

To encourage whistleblowers to come forward and report possible securities law violations, we would seek to have measures put in place to protect whistleblowers from retaliation by their employers. We intend to pursue discussions with the Ontario government to consider the addition of three provisions to the *Securities Act* that would provide a meaningful deterrent against retaliation by employers.

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The three provisions are:

1. A provision making it a violation of securities law to retaliate against a whistleblower thereby permitting Staff to prosecute the employer through a proceeding under s.127;

2. A provision giving a whistleblower a civil right of action against an employer who violates the anti-retaliation provision; and

3. A provision to render contractual provisions designed to silence a whistleblower unenforceable.

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As described in greater detail below, recommendations for these provisions were drawn from consideration of the SEC and ASIC whistleblower regimes, as well as, anti-retaliation provisions found in other Canadian statutes. We believe that having anti-retaliation measures in place is a key element necessary to support an effective Whistleblower Program.

8.1 Prohibition against Retaliation

To encourage whistleblowers to provide the Commission with high-quality information while addressing fears of retaliation, we are considering the inclusion of a prohibition against retaliation in the *Securities Act*. Similar prohibitions exist in a number of Ontario statutes, including labour and employment-related statutes{5} and statutes implementing other regulatory regimes.{6} In those statutes unrelated to labour and employment, protections are provided for employees who report information or provide documents in good faith, make disclosures in the context of an investigation or give evidence in a proceeding, or who otherwise "seek the enforcement of the act".Similar prohibitions against retaliation or reprisals exist in public sector whistleblower legislation, implemented federally and in many provinces.{7}

The *Criminal Code* makes it an offence for an employer to retaliate against an employee who provides information about offences being committed to individuals involved in the enforcement of federal or provincial law.{8} An element of the Competition Bureau's Whistleblower Program is a provision of the *Competition Act* that prohibits employers from taking retaliatory action against employees who report employer misconduct or refuse to engage in illegal acts.{9}

The provisions implementing the whistleblower programs of both the SEC and ASIC also prohibit retaliation against whistleblowers. The *Securities Exchange Act* makes it a violation of the Act to "discharge, demote, suspend, threaten, harass...or in any other manner discriminate against, a whistleblower in the terms and conditions of employment" because the whistleblower provided information to the SEC, assisted in an investigation or testified against the employer or made disclosures required under *Sarbanes-Oxley*.{10} In Australia, the *Corporations Act* makes it a criminal offence to victimize a whistleblower for making a protected disclosure.{11}

8.2 Enforcement of the Retaliation Prohibition

We envision two avenues for enforcing the prohibition against retaliation in the *Securities Act*:

1. Enforcement by Staff in a s.127 proceeding; and

2. Enforcement by the whistleblower through a statutory civil right of action.

Under existing Ontario statutes containing prohibitions on retaliating against whistleblowers, victims have the right to file a complaint with the Ontario Labour Relations Board (the OLRB). We think deterrence against retaliation would be greater if the anti-retaliation prohibitions included in the *Securities Act* were enforced by Enforcement Staff who investigated the misconduct uncovered as a result of the whistleblower's disclosure.

Retaliation could be the subject of a s.127 proceeding brought by Staff. In 2014, the SEC settled its first enforcement action involving the anti-retaliation provisions under 21F(h)(i) of the *Securities Exchange Act*. The settlement related to an action against Paradigm Capital Management Inc. which involved an investigation into trading without the appropriate client disclosure and consent, as well as retaliation against the employee who reported the misconduct to the SEC.{12}

We expect that Staff could pursue allegations of securities law violations and retaliation in a single proceeding in the same manner. If such allegations were proven in a s.127 proceeding, the Commission could order, among other things, that the employer and/or individuals review and amend workplace policies and practices, be reprimanded, resign positions held as directors or officers and that the retaliation be the subject of an additional penalty of up to $1 million.

Another key element of the anti-retaliation measures implemented by ASIC and the SEC is the ability of the whistleblower to bring a civil action against an employer. Just as other statutory rights of action in the *Securities Act* enhance deterrence of other types of violations of the *Act*, so too would a statutory right of action for whistleblowers deter retaliation. A provision enabling a private right of action in the *Securities Act* and providing for remedies similar to those available under the *Securities and Exchange Act*{13} (which include reinstatement, two times the amount of back pay owed and

costs), would also give the whistleblower access to broader remedies than those available to complainants before the OLRB, whose powers are limited to reinstatement and reimbursement for lost wages, but do not include punitive damages.{14}

Bringing an effective civil action against the employer is likely the most practical solution for an employee who is retaliated against and fired as most people will not be able to function back at their old jobs and companies after being fired.

8.3 To Whom Should the Retaliation-Protections Apply?

Anti-retaliation protections should be available to both individuals who report possible violations of the *Securities Act* "up the ladder" through their employer's internal compliance reporting system and individuals who report directly to the OSC. Whether a whistleblower who reports internally rather than to the SEC is entitled to the anti-retaliation protections in the *Securities Exchange Act* is a live issue in the United States.

Some federal district courts have taken an expansive view, finding that one need not report to the SEC in order to be entitled to whistleblower protections.{15} One Circuit Court of Appeal issued a ruling that would narrow the scope of the protections to only those who make a disclosure to the SEC.{16} The SEC has since attempted to clarify that the expansive view should be taken and that anti-retaliation protections should be available to those who report internally as well as to the SEC.{17}

In Canada, the Supreme Court of Canada has held that the retaliation prohibition in s.425.1 of the *Criminal Code* only applies where whistleblower information is given to a law enforcement body, but does not apply where information is communicated up the chain of command.{18} To provide the strongest protection to whistleblowers under the *Securities Act*, we would recommend that the prohibition against retaliation encompass whistleblowers who report wrongdoing to the OSC as well as through internal reporting procedures.

I strongly agree that protection against retaliation should be extended to persons who report internally in addition to persons who report directly to the OSC. Often persons who report internally are then retaliated against and fired – after termination access to information is restricted and people may not have the ability to report directly to the OSC.

8.4 Rendering Unenforceable Whistleblower Silencing Provisions

An issue related to retaliation is any measure implemented by an employer that is designed to silence whistleblowers from reporting wrongdoing to securities regulators. These measures may take the form of confidentiality agreements, separation agreements and employment agreements, containing confidentiality clauses or disparagement clauses that condition certain incentives on not reporting activities to regulators. The SEC launched an investigation into such practices at a firm in March of 2014 after information came to light from a whistleblower from one of the nation's largest government contractors. The SEC sought and obtained the disclosure of hundreds of employee agreements following claims that "employees seeking to report fraud had to sign confidentiality statements barring them from disclosing the allegations to anyone, including federal prosecutors and investigators".{19}

In May of 2014, Sean McKessy, Chief of the Office of the Whistleblower of the SEC warned in-house counsel against preparing agreements containing these provisions without providing exceptions for regulatory reporting. McKessy suggested that the SEC could enforce this position using its power to bar lawyers from practicing before it.

Although pronouncements like McKessy's will hopefully discourage the use of agreements to impede whistleblowers, the OSC could send a clear and strong message to discourage the use of these contractual provisions. For example, in Australia, the *Corporations Act* provides that no contractual or other right may be enforced against a whistleblower on the basis of the disclosure of a regulatory violation to the authorities.{20}

We are considering whether our anti-retaliation provisions should expressly provide that provisions of any agreement designed to impede or discourage whistleblowers from reporting possible violations of securities laws to the authorities not be enforceable.

I strongly agree that confidentiality provisions within employment severance agreements should not apply to information being reported to securities regulators. These provisions should not be enforceable by companies. People are required to sign these agreements “under duress” in some cases as they need the money to support their families. Companies use these agreements as an effective tactic to silence whistleblowers.

Specific Consultation Questions -- Whistleblower Protection

1. Do our proposed anti-retaliation provisions provide sufficient protection?

Yes, generally I agree with the proposed anti retaliation provisions.

2. Should culpable whistleblowers also potentially be entitled to anti-retaliation protection?

Yes, I think people should be encouraged to come forward even if they have been coerced or duped into being complicit in a fraud or cover up scheme. I think protection from retaliation should be extended.

However I don't think culpable individuals should be entitled to the same rewards as other people who never participated in the unethical or illegal behaviour from the beginning.

It might also be possible to both extend protection and to punish the same individual for their involvement in different aspects of the case, depending on the circumstances and their involvement.

3. What other means should the OSC consider to pre-empt measures taken by employers to silence whistleblowers?

I think a specific fine related to retaliation on whistleblowers and negative publicity surrounding this behaviour might be an effective tactic to discourage companies from retaliating against whistleblowers.

In some ways, the negative publicity and embarrassment the company would suffer from wide and public disclosure of such behaviour would act as a greater deterrent than the fines.

Companies compete for talented people and being known as a negative and or corrupt culture that retaliates and attempts to silence people would impact an organizations ability to attract people.

10. Impact of OSC Program on Internal Compliance Programs

We recognize the importance of effective internal compliance systems at issuers and registrant firms to identify, correct and enable self-reporting of misconduct as a first line of action in promoting compliance with securities laws for the ultimate benefit of investors and our markets.

When the SEC was developing its whistleblower program, companies in the United States raised concerns that paying for whistleblower tips could result in employees circumventing the organization's internal reporting processes in order to gain financial awards from the SEC.{21} We expect a similar concern to be identified by issuers and registrant firms in Ontario with regard to an OSC Whistleblower Program. We heard these concerns from one commenter in relation to OSC Staff Notice 15-704.{22}

While this is an understandable concern, a U.S. study found that the financial incentives historically offered in the U.S. through the *qui tam* provisions of the *False Claims Act*{23} (prior to the launch of the SEC's Whistleblower Program) have had "no negative impact whatsoever on the willingness of employees to utilize internal corporate compliance programs or report violations to their managers".{24}

Rather, it appears that whether an individual reports internally first (or at all), or reports to a regulator or other enforcement authority, depends on many factors, including the individual's perception as to whether the matter will likely be appropriately addressed internally and whether the individual perceives a risk of retaliation for coming forward.{25} As well, the SEC has recently reported that of the whistleblower award recipients to date who were current or former employees, 80% reported internally first.{26}

An OSC Whistleblower Program would not be intended to undermine internal reporting systems and whistleblowers would be encouraged to report their concerns internally first, in appropriate circumstances.{27} However, the OSC program would be available as a means for an individual to report in circumstances where the individual has concerns with the efficacy of the internal reporting system or where an individual fears retaliation as a result of raising concerns within the organization.

If a whistleblower reports misconduct through internal channels, failure by issuers and registrant firms to then promptly and fully report serious breaches of Ontario securities law to Staff, or continuation of the inappropriate conduct or failure to correct the problems, may result in no credit for cooperation when the issuer or registrant firm is ultimately brought to account for the misconduct.

Further, this would be considered an aggravating factor in Staff's sanctions recommendations in any administrative proceeding. We encourage issuers and registrant firms to review their internal reporting processes to ensure they are robust and effective.

In general, I think the OSC wants to encourage companies to have a robust and transparent internal reporting compliance system.

But I think the evidence is fairly clear that Management has ways to manipulate these systems and they do not always work as intended. Therefore I think the OSC program should both protect and reward people for coming forward either directly to the OSC and or through internal compliance reporting systems.

The overall objective is to improve governance and transparency – so I would not support placing too many restrictions that would make it difficult for people to come forward.

If a company can demonstrate that it is handing an issue internally in an appropriate manner (which may not be known to a whistleblower) then the facts will come out and be taken into consideration by the OSC.