

May 15, 2017

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Committee Secretary  
Parliamentary Joint Committee on Corporations and Financial Services  
PO Box 6100  
Parliament House  
Canberra ACT 2600

Dear Secretary,

At the request of the Joint Committee, I have reviewed and am responding to Dr. Longstaff's recent submission and testimony relating to whistleblower protections and compensation arrangements in the corporate sector.

It is my deeply-held view that strong legislation is needed to protect Australian whistleblowers and promote whistleblowing,<sup>1</sup> as part of the fight against corporate corruption. I start with the premise that corporations serve a necessary social purpose, but can also cause great harm. Encouraging those who know of wrongdoing in the workplace to speak out is essential to protecting the innocent victims of such misconduct. Being a corporate whistleblower is rarely easy or glamorous. Often, there is great risk for anyone who speaks out. Accordingly, I believe that it is appropriate for Australia to compensate those who perform this valuable public service, in recognition of these significant risks and costs.

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<sup>1</sup> Dr. Longstaff distinguishes speaking up from whistleblowing, but I do not see any such distinction in the corporate world. For the person engaged in misconduct, any report, anywhere, is viewed as whistleblowing, and retaliation will follow no matter where the report is made. For the countless victims of corporate wrongdoing, the choice of terminology represents a distinction without a difference.

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My basic points are these:

- Employees owe a duty to employers, but have many other important duties including to their company's shareholders and fellow citizens.
- The public compensating whistleblowers does not create corrupt companies, but allowing wrongdoers to get away with crimes because knowledgeable employees and culpable corporations remain silent surely does.
- Australia's primary focus should be on the real harm caused to real people through corporate wrong doing.
- Whistleblowing works: it ferrets out crime, leads to reform of corrupt corporate cultures, and protects innocent victims from corporate harm.
- The option of whistleblowing to the government can and does promote more robust internal corporate compliance and speak up programs.
- Establishing impossibly subjective eligibility standards will ensure that corporate whistleblowers remain silent.
- Since whistleblowers often pay a heavy price for speaking up, Australia should compensate these courageous individuals for the hardships they experience.

### What is an employee's duty?

A major premise of Dr. Longstaff's arguments appears to be this assertion:

"With the exception of contract negotiations (and/or enterprise or award bargaining rounds), when at work, an employee has no right to advance his or her own private interest. Everything that they do during the time that they are employed must be directed to the task of advancing the interests of the employer."

*What is the employee's duty to the employer?* I believe Dr. Longstaff's statement is much more categorical than what is generally understood about employment relations.

I agree that an employee is not supposed to pursue interests of a separate business while working for an employer. In other words, if I work at a restaurant, I should not be taking food home to use in my own restaurant, or recommending my own restaurant to the customers of my employer. But to suggest that everything an employee does must be focused on the interests of the employer is not grounded in human behavior or law. As long as a worker does the job he or she is paid for, whatever else may occupy the employee's mind is no one else's business. Employees sell their time to their employer, but not their souls.

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His statement also appears to equate humans to econs, i.e., the economists' concept that humans act only as rational economic actors.<sup>2</sup> While an employee is hired to perform work for the employer, it would be fiction and folly to act as if this is all an employee is about. Employees have many thoughts and ideas during the course of any workday. It is not my experience that they focus 100% on their employer's interests. All employees have various interests and areas of focus. They certainly have a duty to the employer, but it not an absolute commitment.

Additionally, his idea that employees can't advance their own interests relies on two flawed assumptions. First, reporting wrongdoing by the company and/or its employees is inconsistent with their companies interests. Stopping clients and shareholders from being harmed and ensuring that they are made whole, sooner, is very much in an employer's long-term interest. Second, it assumes that reporting can't be both in the company's interest and the employee's interest. There are lots of things in life that benefit the interests of more than one party—hence the popularity of “win-win” business opportunities and deals.

*Is duty to the employer the only duty of an employee?* Beyond these disagreements, however, I disagree with the implication that an employee's only duty is to the employer. Even while working, one has many other legitimate duties beyond those to the employer. An employee may have religious duties that are exercised while on the job. One may have duty to their family, so that an urgent call from home may necessitate taking immediate action. And most relevant to the issue of whistleblowing, an employee has a duty to the shareholders of their company and their fellow citizens. Whether or not these are all legal duties, they certainly are moral ones. Again, the employer is not the only important stakeholder and not the only interest that an employee or any other citizen should consider. During the hearing, Ms. Butler brought this point to a head with this question:

**Ms BUTLER:** But to get to my point, Dr Longstaff, isn't it the case that the interests of all of those stakeholders are served if the whistle is blown on a matter, for example, international bribery, even if that is done in breach of the duty to the employer, even if that is done out of a motive that is additional to the motive about blowing the whistle? Is it not the case that the interests of all those stakeholders, including taxpayers and the national interest, are served if a maliciously reported but completely true allegation of international bribery is made?

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<sup>2</sup> Lawrence M. Mead, *Econs and Humans*, 9 CLAREMONT REV. BOOKS 18 (2009), <http://www.claremont.org/crb/article/econs-and-humans/> (last visited Jan. 4, 2017), (reviewing RICHARD THALER & CASS R. SUNSTEIN, *NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH, AND HAPPINESS* (2009)) (“[T]he efficient calculators imagined in economic theory, able to weigh multiple options, forecast all the consequences of each, and choose rationally.”).

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I agree with Ms. Butler's line of questions because she is focusing on doing what is necessary to protect the Australian public from the real harm of corporate wrongdoing. If government invites the public, including all employees, to report illegal conduct, I simply do not see anything in this that could be considered unethical, or against public policy, or contrary to an employee's duty to an employer. Employers have no right to engage in illegal conduct. If they do they forfeit any claim to an employee's loyalty. Employees have at least as much moral duty to the shareholders of their company and fellow citizens as they do to whoever signs their paycheck. I do not see even a shadow of an argument against taking action to prevent harm and injury to others, including reporting to the government.

**Should those who speak up receive some form of compensation?**

That leads us to the issue of whistleblower compensation. Dr. Longstaff accepts that some compensating payment is appropriate, in his example coming from the employer. Thus he says:

is [sic, probably "it"] would be fair and proper for an employer to compensate a person who reports wrongdoing for:

- any direct costs incurred in the performance of their duty, and
- any detriment or loss suffered as consequence of performing their duty.

Additionally, it should be open to employers to recognise the discretionary efforts of employees – for example, by means of acknowledgement and the payment of a discretionary bonus (providing this is not seen to create an incentive for reporting).

Of course, the idea that the bonus would be "discretionary," but would not act as an incentive is at best problematical. It is likely that any employee thinking of raising an issue would know if a bonus had been paid, even once, and could not help but have this in mind. But Dr. Longstaff's concession appears to cross the extreme line drawn earlier about the employee's interest being solely the welfare of the employer. If any payment for those acting on a duty to raise issues is appropriate, as Dr. Longstaff concedes, the question is no longer "whether" payment is acceptable, but only a matter of source and degree.

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I believe there is no duty-based argument against compensating a whistleblower in a way that makes that person whole, and makes up for the harm one suffers from taking a virtuous action. So the legitimate question becomes, how does the government compensate for the enormous and pervasive risk faced by any citizen who considers reporting misconduct? Merely covering costs might make sense if whistleblowing were some minor, administrative step with no predictable adverse consequences. But that is not reality. In the corporate world today, there is significant risk of retaliation and blacklisting. Given that risk, there needs to be at least a multiple of “costs” to account for these very real risks. Too often, corporate whistleblowers end up in a bad place - depressed, pushed out of their jobs, and in other bad circumstances.<sup>3</sup> One can fairly debate the appropriate structure and degree of whistleblower incentives, but there is no good policy basis to bar all forms of compensation.

### **Can we simply rely on companies to do the right thing?**

One of Dr. Longstaff’s assumptions appears to be that corporations will embrace internal whistleblowers because it is in the corporation’s interest. Thus, in his analysis, the best approach is simply to await a transition from a hostile corporate culture to a corporate welcoming of those who speak up. While I, too, would applaud such a transition, he offers, and I see, no basis for believing that such a new state of corporate affairs will exist in Australia, anytime soon.

A major part of Dr. Longstaff’s assumption appears to conflict with what has been learned from agency theory and the agency dilemma. In agency theory it is recognized that there is an inherent potential for conflict between the interests of an entity and the interests of its agents – the ones who act for the company. So while a “company” may logically have an interest in acting legally and ethically, and in encouraging its employees to report misconduct without fear of retaliation, its managers and officers, as agents, may not share this corporate interest. Notwithstanding the corporate interests, the individual managers (i.e., agents) who deal with whistleblower reports have their own, personal interests within the organization. Showing care and concern for whistleblowers is often not within the usual scope of the agent’s interests. Rather, those who speak out are seen, at best, as annoying distractions to be shunted off to some place where they cannot interfere and, at worst, a threat that needs to be neutralized. The “corporation” may have no interest in harming the whistleblower, but the corporation can only act through its agents. History, and countless surveys and media stories, consistently show that those agents can and do retaliate against corporate whistleblowers.

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<sup>3</sup> For one collection of the experiences of whistleblowers in Australia, see Dempster, *Whistleblowers* (1997; ABC Books): noting the fate of whistleblowers as “not being believed or trusted, from a shattering of self-esteem, from harassment, from intimidation, from being publicly discredited or abused.” *Id.* 1.

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**Is the answer to do nothing and wait for companies  
to provide complete safe harbors for whistleblowers?**

Dr. Longstaff's alternative to government incentives is to assume an environment where employees feel completely safe to report violations in-house. As he expresses it, "smart employers create conditions of absolutely [sic] safety" for those who report concerns.<sup>4</sup> I urgently wish that were true. Unfortunately, many organizations have not achieved this lofty goal and it is unclear what the catalyst of future change will be for them. Meanwhile, in the real world of today, Australian legislators should consider the strong resistance that exists for whistleblowing, and the price many corporate whistleblowers pay for speaking up. If there is a universal truism in this field, it is that many people do not like whistleblowers and that retaliation is the norm, not the exception. Surveys show the fear of retaliation is the biggest or second biggest reason people do not raise issues (the other reason is the expectation nothing will happen – employees do not have the faith in managers' good will that Dr. Longstaff apparently has). I have heard this expressed brutally but directly in the US as "snitches get stitches and end up in ditches."<sup>5</sup>

Should Australia simply wait for companies to develop systems that comfort those who speak up and fully protect them from any form of retaliation for doing so? This is surely a worthy objective, but as Ms. Butler said at the hearing "you are taking the world as it should be, not as it is. Unfortunately, as legislators, we are often concerned with the way that the world is and we are trying to develop a way that does promote a pro whistleblowing culture." Realistically it continues to be difficult anywhere and anytime for corporate whistleblowers to speak up. Meanwhile, if Australia just sits by waiting for this hoped-for transformation, innocent people will continue to suffer from corporate crimes.

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<sup>4</sup> Dr. Longstaff would allow employees to raise concerns externally apparently only if:

"a) there is a risk to the safety or wellbeing of an individual, group or wider society,

b) the relevant conduct is criminal in nature, and

c) the report is made to a third party that acts in a spirit of public service and for the public interest." We do not agree with such deliberately restrictive tests. We can see no justification for requiring *both* that the conduct be criminal (even lawyers are not always sure when this standard is reached – how would an employee know?) *and* that it involve risk to others. If conduct is criminal, society has already decided it causes harm; nothing more should be required. If the conduct causes harm, it should be reported to the government, so that authorities can decide what steps are needed to prevent further harm. As we all know, much harm is caused by conduct that is not necessarily criminal. The distinctions proposed by Dr. Longstaff would create another artificial and improper barrier to employees speaking up to their government.

<sup>5</sup> Notwithstanding the popular myth that Americans like or even worship whistleblowers, the common view of whistleblowers in the US is just as hostile as anywhere else. Having traveled extensively, I can tell you the list of countries around the world where whistleblowers are fully embraced is zero.

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**Should we develop standards that make it more difficult to protect whistleblowers?**

Dr. Longstaff makes an assertion that can serve to undermine whistleblowers, and that is often used in attacking those who blow the whistle:

“Unfortunately, there are times when people report suspected or actual wrongdoing for entirely selfish reasons. That is, they do not act out a duty to their employer but simply in order to advance their own interests.”

I believe this suggests an approach that is too narrow – like the view of employees as econs, making one-dimensional decisions based on after-the-fact, third-party, analytical determinations of financial interest. In fact, the decision to speak up, like many human decisions, is often a complex mix of motives. Different factors and emotions may come into play, and even the whistleblower him- or herself may not be able to describe them fully. There is much to be learned from the new types of behavioral studies that show the deep flaws of one-dimensional thinking associated with the econ model.<sup>6</sup> Human nature is more complex than this, and if we are to prevent corporate crime we need to emphasize reality over theory. Human nature is

Dr. Longstaff would require us all to divine what was at the heart of each whistleblower to determine if they were worthy, and what our response should be. Aside from the cost, delay and uncertainty this would entail, I believe it is completely unnecessary, and is also not the standard used globally in whistleblower programs.

What would happen if Australia followed Dr. Longstaff suggestion to discount anyone who reports misconduct if they do so for any but the purest motives? Given that it is usually impossible to know what is happening inside another's head, Dr. Longstaff must realize that his assertion threatens to provide a broad license to ignore whistleblowers on a wholesale basis. In his proposed analysis, the truth of their report is not the relevant consideration; rather, we must look into the minds of those who speak up. Sadly, the usual reaction of scoundrels to allegations of wrongdoing is to challenge the motives of the one raising the issues. Investigate the whistleblower! This is one of the most-often used tools to deflect attention from wrongdoing and to retaliate against corporate whistleblowers. His approach opens the door to legitimizing what would otherwise be viewed as a transparent dodging technique. Given the choice between a test that can be objectively determined (did the company do something wrong or did it not do something wrong) and one that is impossible to determine (what was going on in the mind of the

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<sup>6</sup> For example, Dan Ariely's fascinating studies of human behavior illustrate the errors of the narrow, logic-bounded thinking proposed by Dr. Longstaff. See Ariely, *The Honest Truth About Dishonesty* (2012; HarperCollins)

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person speaking up), I see no rationale for adopting a test that is impractical and prone to error<sup>7</sup> over one that is based on results and societal benefit. In my mind, and that of U.S. law enforcement and regulatory authorities, the best measure of employees' ethics are their actions and reporting crime to cops is unquestionably an ethical act. I encourage Parliament to adopt a similar view.

It is also worth noting that if the concern is to prevent false reports, it should be remembered that the consequence of making a false report internally is limited to being rebuked or having to find another job. But lying to the government can constitute a crime and can result in legal actions against the whistleblower. Thus, logic would suggest that the route of government whistleblowing is more likely to produce valid reports than those confined to the company.

**What policy steps are likely to prevent harm and corruption,  
and which ones will breed more misconduct?**

Dr. Longstaff makes an assertion that I found startling, and would have found difficult to accept even if it had been supported by extensive empirical work (none was cited). His proposition was that the government offering to compensate whistleblowers will lead to an ethical degradation in the corporate world. Under this premise, when the government cracks open a corporate corruption case, whether the company and its employees reform would be determined by whether or not a whistleblower reported this to the government and was compensated. While I have been a first responder to corporate wrongdoing for almost two decades, I do not know of any examples where this occurred or was even hinted at. I have also seen no studies suggesting that corporate corruption anywhere originated from a whistleblower reporting crime to the government and then receiving compensation for doing so. On the other hand, there are numerous examples of companies that reformed only after the government was brought in, without regard to how that came about.

The greatest and most fundamental flaw of Dr. Longstaff's analysis is the tendency to ignore or brush over the great harm that companies are capable of producing. Instead, he holds up the

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<sup>7</sup> Dr. Longstaff also states "those who report wrongdoing have an obligation not[sic – probably "to"] make their 'best efforts' to determine the truth of what they say. This can sometimes [sic – probably "be"] difficult to achieve – especially when a loyal employee is at risk should it be discovered that they know of the alleged wrongdoing." But experienced law enforcement and regulatory authorities regularly advise against this. Investigations need be left to professional investigators. An amateur sleuth risks tainting evidence and leading wrongdoers to cover up evidence. It is best if knowledgeable employees pass along their concerns at an early stage to those with the experience to effectively conduct investigations.

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specter of government help for whistleblowers creating an ethical apocalypse. For such a counter-intuitive assertion, I would expect to see compelling empirical evidence that this has happened or could happen (indeed, I am aware of no evidence of this anywhere, including in countries where such rewards have been routine).

In his testimony, Dr. Longstaff responds somewhat curtly to Senator O'Neill's legitimate concerns about powerful incentives in the corporate world to do wrong, with the statement "two wrongs don't make a right." I simply do not see any wrong at all in a citizen standing up for what is right and reporting wrongdoing. But the truly fatal flaw is that he equates an unproven concern (government compensation for whistleblowers subverting corporate morals) with real harm – the losses that hit victims when corporate crime and misconduct are not stopped.

No one should walk lightly past the issue of corporate harm. This is real and can be devastating. Yet his argument seems basically to dismiss anyone reporting corporate crime, unless they are motivated solely and purely by a duty to their employer. Putting aside the impossible standard – since we do not know what motivates others – to the victims of corporate crime it does not matter why someone acts to prevent it. What matters is protecting the public.

I note that Dr. Longstaff's theory knows no limits and would apply to all reports of all forms of corporate misconduct. So it is worth spending some time talking about the real victims of corporate misconduct – those injured from dangerous products, those who may die from contaminated food or drugs, those who suffering from malnutrition because of bribes paid to corrupt officials, those who lose their jobs and their pensions from corporate fraud.

We should not get lost in general terms, such as "corruption" and "public interest." The real meaning of "right and wrong" comes through when you see people suffering in collapsed buildings because building inspectors were bribed, or you see school children in ramshackle structures because the money intended for schools was stolen by corrupt officials. These are not theoretical concepts – these are real people suffering from real crimes.

Despite being an expert in this area, I know of no experience with whistleblowing programs where society offering a reward for those reporting violations has undercut the moral fiber of the corporate world. To the contrary, the American experience tells us that governments offering incentives for corporate whistleblowers to report misconduct really does work. First, surveys show that more than 80% employees, continue to report internally first—an important sign of a healthy corporate environment. Second, after the establishment of the SEC Whistleblower Program, many companies invested more time and resources in strengthening their internal

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reporting and compliance programs-to encourage their employees to report internally, rather than externally. Third, attorneys, accountants, compliance professionals and other gatekeepers have reported being empowered because they now can argue that failure to do the right thing or invest more in their compliance and integrity programs will result in external reporting. Fourth, more organizations are self-reporting to law enforcement and regulatory organizations because the probability of detection associated with external reporting incentives is much higher than ever before.<sup>8</sup> Finally, the success of American whistleblower programs has had a positive deterrent impact by discouraging potential wrongdoers from engaging in wrongdoing.<sup>9</sup>

I do agree that the government should not undercut company compliance efforts. We can all benefit if employees first turn inside to raise their questions, in a corporate environment where such reports are taken seriously and those who speak up are protected. In this regard, the incentive system developed by the United States Securities and Exchange Commission pursuant to the Dodd-Frank Act offers a practical and effective model. Under this model strong procedural and financial incentives (but not a requirement) are offered to employees to pursue issues in-house first. So an incentive system that encourages individuals to report in-house, but does not mandate that they first clear this high hurdle, provides a good balance to the different societal interests involved.

As if to emphasize just how theoretical and hypothetical his analysis is, Dr. Longstaff's language brings this into sharp focus:

"Against what we have argued here, some might suggest that the offer of inducements to report (incentives) to those who report wrongdoing will increase the incidence of reporting. In practice, this might be true. However, if this is the sole basis for increased reporting, it will be at the cost of a predictable degradation in the ethical tone of the organisation. In turn, this may foster an increased incidence of wrongdoing amongst a cynical population of employees. Thus, apart from anything else, such an approach may prove to be self-defeating."

This statement appears to acknowledge grudgingly what the overwhelming message of experience proves: offering incentives does increase reporting. It bears emphasis that this is not just someone reporting on the weather. These are reports of crimes and other conduct that breaks

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<sup>8</sup> One of the reasons the SEC Whistleblower Program was deemed necessary was that Corporate America rarely self-reported to law enforcement authorities, either because their employees were afraid to report or they feared the consequences of doing so. Today, I suspect the reality in Australia is no different.

<sup>9</sup> This topic is covered in more detail in my original submission on February 9, 2017.

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the law and harms the public.

This statement also appears to be based on the unjustified conclusion that the incentive will automatically be the “sole” reason for reporting. The experience of those who deal with whistleblowers is that they first raise issues internally because they want to do the right thing, and only go outside after being retaliated against or the problem is not appropriately addressed by the company. As stated above, the SEC has publicly announced, and other surveys have confirmed, that more than 80% of employees still report corporate wrongdoing internally, before reporting externally. Obviously, if the only reason they raised issues was financial they would never have reported internally first. So the assumption that those who report to the government and are rewarded do so “solely” for the reward is simply incorrect.

When someone calls the government there are invariably numerous thoughts and motivations involved. Fear of retaliation and blacklisting is first and foremost what confronts anyone who wants to speak up. The government, by offering an incentive, can balance out this well-justified fear.

As for the “Predictable degradation in the ethical tone of the organization,” this is a purely hypothetical proposition for which Dr. Longstaff offers no studies or proof. The reality, which can be observed by anyone who looks, is that exposure of corruption to the sunlight of public scrutiny has a cleansing effect on companies. The bad actors are removed and the company undertakes reform. The names of such companies are well known and their numbers are legion. On the other hand, there is no list of companies that went downhill and became worse only because the government provided recognition or compensation to a whistleblower.

Will employees become cynical because their bosses’ crimes were reported to the government? I have not seen or heard evidence of this. Where I and others who deal in corporate crime and misconduct do find cynicism and ethical degradation is in companies where management misconduct goes unreported and bad actors continue to thrive because good employees are afraid to speak up. The level of cynicism there is palpable and corrosive.

### **Are we talking “bounties” or compensation?**

How we prevent corruption and other misconduct is a serious question that deserves serious and studied analysis. It is not a function of mere wording. Dr. Longstaff accepts the idea of compensation, but views “bounties” in only pejorative terms. If language is a determinative matter, then we propose that the Australian government simply follow this protocol, and

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“compensate” whistleblowers in a way that truly recognizes the real risks and costs to whistleblowers.

All whistleblowing is risky. As Senator Xenophon accurately observed, “most whistleblowers burn their careers, or burn bridges, when they come forward.” This is a reality that should not be minimized, and represents the extreme price that many whistleblowers must pay for reporting corporate wrongdoing. Government incentives serve to cancel out, at least some of, that risk. A prospective whistleblower knows he or she may pay a price for standing up, perhaps a substantial one. Most often, by the time they go to the government, they already have tried to change things within their own companies. After this courageous act, they could be excused for standing back. So for them to take the additional step of going to the government and all that this entails, is a major risk. It is appropriate for Australia to recognize the depth of this risk, and attempt to negate all the real financial, emotional and even physical risk that awaits those who speak up. It is only fair that the one who speaks up against the odds receive meaningful compensation, and that society, which benefits from such courage, compensate these whistleblowers in a way that outweighs the pain and personal costs that befall whistleblowers.

Respectfully submitted,

Jordan A. Thomas