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Executive Exchange

Investigating Whistleblower Allegations Reported to the Board

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Investigating Whistleblower Allegations Reported to the Board:

The Hypo You Hope to Never See

November 4, 2015

Panelists

- **Alisa Swire**
Vice President, General Counsel & Secretary, Johnson Outdoors, Inc.
- **Scott Shaffer**
Forensic, Investigative & Dispute Services Wisconsin Practice Leader,
Grant Thornton
- **Gene Cahill**
Forensic, Investigative & Dispute Resolution, Grant Thornton
- **Tryg Jacobson**
Director, Orion Energy Systems, Inc.
- **Neill Blundell**
Partner, Eversheds LLP
- **Bryan House**
Partner, Foley & Lardner LLP

The Players

- Best Bet Insurance, Inc. is a U.S. public company (NYSE: BEST) engaged in a wide variety of insurance related businesses in the U.S. and overseas, with substantial operations in the U.K.
- Jim Whistler is Best Bet's Chief Investment Officer and is responsible for Best Bet's vast investment portfolio and decisions relating to that portfolio.
- Best Bet's General Counsel is Wise Sage. She used to be a partner at Best Bet's primary law firm, Holy & Gartner.
- Bill Junior is Best Bet's assistant General Counsel.
- Tom Boss is Best Bet's founder, Chairman and CEO.

The Players



The Problem

- Whistler is concerned that Boss, the CEO, has engaged in wrongdoing. Issue No. 1: Insider Trading:
 - Boss approached Whistler three times to buy shares of public insurance companies and sought Whistler's view.
 - Whistler's typical analysis suggested two companies seemed like a decent value; the third was not. Boss demanded that Whistler buy all three for Best Bet, adding that he was purchasing shares of two companies for his own portfolio.
 - Sage was aware of the Best Bet (and Boss) purchases and did not object, but did not document that approval with any analysis.
 - Two companies were acquired within weeks, stock prices jumped, and Boss directed that the shares be sold at a profit.
 - Boss knows CEOs at companies 1 and 2; his brother works for company 3.

The Problem

- Issue No. 2: FCPA
 - Whistler is also concerned that Best Bet may have an FCPA problem relating to the acquisition of a company in the U.K. and possibly another in Italy.
 - Best Bet has been in serious acquisition mode for several years, and Whistler has heard through people reporting to him in Europe that money was paid to a public official in order to secure certain approvals associated with the acquisitions.

Whistler Raises the Issue

- Sharing a cab to the airport with Junior, Whistler raises his concerns: (1) Boss constantly bullies employees to get what he wants; these trades were too good to be true (i.e., Boss must have inside information); (2) Sage always protects Boss and inexplicably approved the trades without documenting that approval.
- Whistler fears retaliation from the CEO, Sage and others and says he does not want to be identified as having raised concerns.
- Whistler says Best Bet should have an independent investigation, and insists that Holy & Gartner cannot do it due to its relationship with Best Bet and Sage.
- Junior speaks to Sage about what he's heard but does not identify Whistler as having raised the issues.

Questions

- What should Sage do? If you are on the board, do you want to know about this or is this an HR issue for Whistler?
- Should Best Bet begin an internal investigation?
- If so, who should lead the investigation? Audit Committee? Special Committee? Full board?
- Should Sage be involved?

The Investigation Is Considered

- Sage informs Chair of the Audit Committee (“AC”). AC Chair is not happy and says that the insider trading is ridiculous. Nevertheless, he agrees to investigate and determines that the AC will run the investigation. Sage will not be involved.
- AC Chair, however, does not like to be told what lawyers to use. AC Chair wants to hire Holy & Gartner to lead the investigation because Holy knows Best Bet and its executives best.
- AC Chair also tells Sage that he’d like Junior to tell him “off the record” who has raised the issue. He says he has no authority over this person and, in any event, promises not to tell senior management.

Questions

- Should Holy & Gartner conduct the investigation on behalf of the AC?
- Should the AC Chairman know the identity of the whistleblower?

The Investigation Begins

- The AC hires a law firm with no connection to Best Bet that will report to the AC Chair regarding the investigation.
 - The AC Chair tells the partner to leave no stone unturned, but questions how thorough the investigation can be with anonymous whistleblower.
 - AC Chair reminds partner that the 10-Q has to be filed in ten days.
- With respect to insider trading, there are few documents and few witnesses, the most important one being Boss. Boss agrees to be interviewed, but he wants his team of lawyers to be there, and he wants Best Bet to pay their fees. AC Chair wonders why Boss needs a lawyer at all.

Questions

- How can the AC and its counsel conduct a thorough investigation with an anonymous whistleblower?
 - Should the AC and its counsel seek to keep the whistleblower apprised of the investigation?
- Must/should Best Bet agree to pay fees for Boss's team of attorneys?

FCPA Complications

- Law firm has no office in Europe and discusses the issue with AC Chair.
- AC Chair does not want to hire even more lawyers and wants law firm to send a team to Europe to get to the bottom of this quickly.
- The FCPA allegations require a more exhaustive search for documents and discussion with witnesses in the U.K. and Italy to understand alleged payments and accounting for them.

Questions

- Should the AC hire in-country lawyers?
- What are the issues that Best Bet needs to think about with respect to investigations in foreign countries?
- Should Best Bet disclose the FCPA investigation to the SEC or DOJ?

Friendly Audit Partner Calls

- A few days after the investigation starts, Best Bet's auditor calls the AC Chair to make sure everything is set for next week's AC meeting to approve the 10-Q.
- AC Chair reports to audit partner what is going on, explaining that there are some very suspect allegations by an anonymous whistleblower.
 - Audit partner is very upset that he was not told immediately.
 - Audit partner is concerned about "tone at the top" and wants to see documents collected, interview memos, and wants regular briefing.

Questions

- Should AC Chair have reported the issue to audit partner immediately?
- Does Best Bet have to provide all of this requested information to its auditor?
 - Does it have to provide privileged memos of witness interviews?
 - What should Best Bet do to placate its auditor?

Investigation Wraps Up

- Law firm finds no evidence that Boss had material nonpublic information or otherwise engaged in insider trading. (He knows the industry and is a good stock picker.)
- Law firm, with help from in-country experts, determines that payments related to approval of acquisitions were, at worst, “facilitating payments” falling under FCPA exceptions and Best Bet gets legal opinion to that effect.
- Auditor gets comfortable and 10-Q gets filed on time.

Whistler Revealed

- Whistler “outs” himself at a subsequent AC meeting, telling two AC members that the investigation of his concerns was “a total whitewash.”
- The AC members tell Boss that Whistler outed himself. Boss, stating that Whistler was “dead wrong” and showed terrible judgment, tells Sage that Whistler is not the kind of person who should be working at Best Bet.
- Sage would like nothing more than to get rid of Whistler, but is concerned about the consequences of doing so.

Questions

- Can Best Bet fire Whistler now? Can it negotiate an amicable departure?
- If Sage can negotiate a severance agreement with Whistler, can Best Bet incorporate language preventing Whistler from going to the SEC with his allegations?

Takeaways

- Take all whistleblowers seriously and protect anonymity. Mishandling the whistleblower can lead to worse consequences than any alleged misconduct.
- Take precautions early to be as independent as possible. Take away the argument from that the investigation was biased from the start.
- If the situation requires it, directors may have to step up and be directly involved in an investigation by working with internal personnel or outside counsel.
- Support your executives if the facts allow, but keep an open mind.

Takeaways

- Keep your auditor in the loop. This is a critical relationship and being crossways with your auditor can cause tremendous problems because these things always seem to arise before a significant public filing.
- If you are in a high-scrutiny business, have a team ready to go for internal investigations and have a plan. Document the investigation and how it is going to be handled.
- Consider law and customs in applicable jurisdictions to avoid surprises, including local whistleblower issues, data privacy and local criminal authorities.

Thank You For Attending