



Establishing an Effective Whistleblower Program

By Brad Preber

Immediately following the passage of the Sarbanes-Oxley Act (SOX), companies and their audit committees were primarily concerned with adhering to the letter of the law with respect to complaint handling. They donned the trappings of compliance by creating and disseminating policy manuals, sending out special messages from leadership and the audit committee, initiating employee ethics training, hiring a compliance officer, and realigning reporting relationships.

Despite all the energy companies have channeled into establishing complaint-handling initiatives, many are finding that they are not achieving the results they had hoped for. The solution to this is to develop a comprehensive process for handling whistleblower complaints.

Stakeholder Considerations

There is always a temptation when developing any process to rush into the specifics of design. But this would be especially shortsighted in the case of whistleblower programs. It is essential to take a step back and consider the wide range of stakeholders, whose needs and desires are often in direct conflict with one another.

Stakeholders tend to fall into three major categories: users (whistleblowers); accused parties; and other interested parties (e.g., shareholders, creditors, or auditors). It is incumbent on the audit committee to acknowledge stakeholder needs and tailor the complaint-handling process to meet them.

Anyone wishing to express a concern about accounting controls or auditing matters should feel comfortable using the organization's com-

plaint-handling process. This is especially critical for employees who may fear that filing a complaint could cost them a job or have some other negative consequence. In general, internal whistleblowers should have the following:

- **Choice of reporting venues:** Complaints should be able to be reported through discussions with supervisors, confidential conversations with HR, anonymous tip lines, company websites, and e-mail.
- **Confidentiality and anonymity:** SOX requires that employees who have concerns about questionable accounting or auditing be able to submit these to the company's audit committee and be assured both confidentiality and anonymity.
- **Ease of use:** Stakeholders need to know how to use the system and be able to do so with ease.
- **Information on the progress of the complaint:** Because this area can be especially sensitive, audit committees will need to develop policy guidelines for communicating appropriately with whistleblowers, without compromising other stakeholders.

There are a range of potential external users of the complaint-handling process, including vendors, customers, and suppliers. While SOX does not protect the anonymity of these sources, it is nevertheless important for them to be able to file complaints with the same ease as internal users of the system.

The second set of stakeholders—the accused parties—are especially concerned with confidentiality, because claims can be potentially damaging to their reputations and their careers. An individual accused of wrongdoing must be afforded due process and protection from unmerited personal and professional harm. Building such considerations into the complaint-handling system usually requires the assistance of HR professionals and legal counsel.

On the other hand, parties who are affected by the investigation are generally looking for as much information as possible. Management,

Director Summary: Audit committees that are looking to improve their whistleblower complaint-handling processes should analyze stakeholder needs, tailor the individual steps, and establish appropriate metrics for measuring success.



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employees, directors, and the audit committee must be apprised of the progress of investigations. Public and investor relations professionals want to understand the situation so that they can communicate with external stakeholders, especially those such as investors, bankers, and other creditors who have a financial stake in the outcome of the investigation.

Because the needs of many interested parties may be in direct conflict with the confidentiality needs of whistleblowers and accused parties, audit committees often struggle with how much information should be released. To be prepared for this balancing act, audit committees should consider adopting a set of guidelines for the phased distribution of information to interested parties.

Designing the Process

Every whistleblower program will naturally be customized to fit the culture and capabilities of an individual organization. Grant Thornton has compiled six core steps for companies looking to implement a successful approach to complaint-handling.

Step One: Receive

The approach to receiving a complaint is critical to the smooth functioning of the rest of the process, and it involves myriad details. Specifically, it should address: 1) a method for documenting and housing claims; and 2) a process for screening claims and determining if they need to be passed on to the audit committee for review.

Especially critical for successful claims intake is training the parties who are responsible for initial contact with complainants. These individuals must be able to accurately document the claim while remaining sensitive to issues of confidentiality and anonymity. A longer claims report should track the entire investigation and its resolution. Often companies will outsource claims processing to an outside vendor.

Any claim that has the potential to materially impact the financial statements must be referred to the audit committee. However, most audit committees do not have the time to review every incoming complaint to make this determination. It therefore makes sense for them to appoint a screening committee drawn from areas such as

legal, human resources, and risk management. The committee is responsible for determining whether complaints have merit, and whether they are relevant to accounting or auditing matters. Complaints that have merit but which are not relevant to the financial statements (for example, numerous HR-related complaints) can be referred to other parties in the organization for handling.

Step Two: Analyze

Once the audit committee receives a referred complaint, it should perform an in-depth analysis, assisted by legal professionals and other counselors. Claims should be examined based on two factors: 1) sensitivity, and 2) materiality to the financial statements. Many issues will rate high in both areas. For example, when a company is under investigation for options backdating, there is generally a financial impact, but because the issue is so sensitive, negative publicity and investor backlash are likely to exacerbate the problem.

Step Three: Investigate

The audit committee will need to appoint an investigations team based on how the complaint is viewed in terms of sensitivity and materiality. Any time a complaint is material, the team will probably involve legal counsel, the investor relations department, management, and internal audit. The external auditor must be apprised of the team's activities but cannot be involved in the investigation due to independence considerations.

Step Four: Resolve

The resolution of a complaint generally involves developing a corrective action plan which lays out a set of procedures that must be followed and documented. Procedures might be as simple as correcting an internal control or as far-reaching as instituting a company-wide ethics training program.

Step Five: Report

The audit committee must communicate the resolution of a complaint to the stakeholders—the accused parties, the whistleblower, and the investment community. The company's responsiveness signals that it takes these complaints seriously and is prepared to deal with them appropriately. Proper communication sets a tone at the top, which serves as its own control against future infractions.

Step Six: Retain

Documentation produced during the complaint-handling process should be preserved, protected, and retained in accordance with the company's document retention policy. Confidential material must be appropriately safe-



guarded. Documentation of the measures taken to resolve complaints also demonstrates that the audit committee is in compliance with its responsibilities under Sarbanes-Oxley.

Measuring Program Success

No whistleblower program can be considered complete without a set of performance metrics that can determine success and contribute to process improvement. Metrics will also assist audit committees in conducting trend analyses and in answering such questions as whether more complaints are coming from particular departments or if they tend to occur more at certain times of year. Among the metrics companies can use to track the success of their whistleblower programs are:

- Complaints per month/year
- Complaints by division, department, branch, store, country, etc.

- Complaints by type
- Number of investigations in process or completed
- Average cost per complaint/investigation
- Average cycle time (from complaint receipt to resolution).

Metrics will not only provide important insights into the whistleblower program itself, they can also be used to monitor and tighten the company's internal control environment. By analyzing stakeholder needs, tailoring the individual steps, and establishing an appropriate set of metrics, audit committees will be in a much better position to say that they are fulfilling a critical aspect of their fiduciary responsibility for the companies they govern. ■

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Corporate Hotline Activity: A View from the Top

The *2006 Corporate Governance and Compliance Hotline Benchmarking Report* presents an analysis of nearly 200,000 hotline reports from 550 organizations over a four-year period. The report, prepared by The Network, the CSO Executive Counsel, and the Association of Certified Fraud Examiners (ACFE), answers a number of commonly asked questions regarding hotline usage, including:

What is being reported?

More than half of reported incidents involved personnel management issues. Company and professional code violations were the next most commonly reported incidents.

Did people remain anonymous?

Overall, a slim majority of people (nearly 54 percent) opted to remain anonymous. People reporting issues like corruption and fraud were less likely to remain anonymous than those reporting other issues. The level of trust plays a role in this: if participants don't believe that their organization will protect their confidentiality, they will likely choose to remain anonymous.

Was management aware of the problem?

One of the most surprising results of the report was the fact that a vast majority (71 percent) of participants had not notified management before making a hotline report. This may indicate that, if given a choice, people prefer alternative reporting methods, rather than having face-to-face conversations with management, particularly when sensitive issues are being reported.

Are companies taking action?

A significant majority, 65 percent of reports in the study, were serious enough to warrant an investigation, and some form of corrective action was taken 46 percent of the time.

A Measure of Success

To obtain a complete picture of the state of organizational integrity, an analysis of culture, communication, and other factors is also necessary. Organizations should consider a number of important questions, including:

- Are we communicating effectively about our policies and our hotline?
- How is our culture affecting our results?
- Is report volume evenly distributed throughout the organization?
- Are there hot spots of activity or inactivity in certain divisions or locations?
- Are reports providing sufficient information to investigate?

Ultimately, the responsibility to demonstrate success in governance and compliance rests squarely on the shoulders of directors and board members. They are expected to set an ethical tone from the top and present tangible results. Organizational leaders that step up to this challenge with a thoughtful analysis ensure that their business is driven by ethics and integrity at every level.

For more information regarding the Benchmarking Report, contact The Network at benchmarking@report-line.net.