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Should the UK pay financial rewards to whistleblowers?

UK authorities have so far balked at the suggestion of introducing significant US-style financial rewards for whistleblowers. **Hannah Laming** of law firm Peters & Peters asks if it is time for a rethink.

Whistleblowing is a critical intelligence source for agencies charged with investigating and prosecuting serious financial crime. As the importance of whistleblowing in identifying and preventing wrongdoing - whether in the private or public sector - has been increasingly recognised by policymakers, the legal protections in place to shield whistleblowers from retaliatory action have never been stronger.

However, the debate continues as to what extent whistleblowers should be incentivised to bring wrongdoing to light.

Reform in the US

From 2010, the US Dodd-Frank Act has provided that individuals bringing suspected breaches of securities laws to the attention of the Securities and Exchange Commission (SEC) are entitled to a percentage of any financial penalty levied against the wrongdoer (typically the whistleblower's employer), so long as the eventual penalty is greater than $1m.

The rewards on offer can be staggering. The largest award made under the programme, in 2014, is understood to have been circa $35m, and was awarded to a tipster living outside the US. During the 2016 financial year, the SEC received more than 4200 whistleblowing tips, awarding more than $57m to 13 claimants.

In the view of Andrew Ceresney, the SEC's director of enforcement, the programme has been "transformative" to the commission's work, "both in terms of the detection of illegal conduct and in moving our investigations forward quicker and through the use of fewer resources". The SEC has argued that, without the prospect of these awards, firms responsible for misleading the market, bribing foreign public officials, Ponzi schemes and other investment frauds would all have escaped justice.

UK reluctance

Some benefits are available to those who blow the whistle on corporate misconduct in the UK. Individuals who participate in cartel conduct may seek immunity from prosecution from the UK competition regulator, and awards of up to £100,000 ($125,000) are on offer for the supply of useful intelligence on an existing cartel. HM Revenue & Customs also offers financial rewards to whistleblowers, paying out some £600,000 in the 2014-15 financial year. These schemes are of limited application, and are unlikely to incentivise individuals to report significant wrongdoing in, for example, UK financial services firms.

The question is whether some kind of UK Dodd-Frank provisions would assist? The UK's financial services regulators think not.

A 2014 report from the Financial Conduct Authority (FCA) and Prudential Regulation Authority (PRA) argued against the introduction of financial incentives for whistleblowers. The report suggested that there was no empirical evidence of incentives leading to an increase in the number or quality of disclosures received by the SEC.

In addition, it highlighted a number of "moral hazards" presented by financial incentives: malicious reports might be encouraged, conflicts of interest would arise that could be exploited in court by the subjects of any enforcement action, and internal compliance programmes would be undermined, as would the duty of approved persons to be open with their regulator.

Most tellingly, the report argued that Dodd-Frank style multi-million pound awards would offend public opinion: it was against "UK norms" to reward well-paid individuals for complying with a public (and, in some cases, regulatory) duty.

Time for a rethink?

Suggesting that those in the US are not aware of the potential moral hazard in incentivising whistleblowing is somewhat unfair; in 2016, a former Deutsche Bank employee turned down his share of an $8m award on the basis that the penalty from which it derived had been paid by the bank's shareholders, with no action taken against the firm's senior management charged with oversight of the bank's conduct.

More importantly, the FCA/PRA report's contention that both the number and quality of tips did not improve following the implementation of financial incentives conflicts directly with the stated experience of SEC enforcement.

UK authorities appear to consider that the risk of societal distaste for rewarding individuals within the financial services industry outweighs the potential benefits of encouraging those individuals to report the same kinds of wrongdoing that have tarnished the reputation of banking in the public eye. Perhaps this should be revisited, particularly in relation to cases where the conduct has been sufficiently egregious in nature to warrant the imposition of fines in excess of $1m.

The FCA and PRA's approach ignores the fact that many whistleblowers in financial services will be putting their career at risk, and therefore their lifelong earning potential. It also fails to recognise the very real prospect that whistleblowers dedicate substantial amounts of time to providing information, assistance and witness testimony, often to multiple law enforcement agencies, not just in the UK, but also overseas.

The UK's approach is starkly at odds with the US experience. In an environment where regulators and investigative agencies have limited budgets, there are strong arguments for the pursuit of evidence-led policy responses that encourage whistleblowers to bring serious wrongdoing to light, as well as protecting them when they do so.

Hannah Laming is a partner and business crime specialist at the law firm Peters & Peters.

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