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Business Ethics: To Report or Not to Report?

Compliance and Ethics

Environmental



While serving as senior safety, health, and environmental counsel for a multinational specialty chemical company, a vice president named “Jim” came to my office and spoke the magic words that always get a corporate counsel’s attention: “I think we have a big problem. We need to talk.”

Jim and I sat down at a table in my office. He explained that a mass balance calculation for two units in one of our manufacturing facilities in Louisiana yielded some alarming data. Specifically, the calculations revealed that these two production units were emitting 400 tons per year of a hazardous air pollutant (HAP).

That fact in itself would not necessarily have been a problem. It is possible to obtain a permit for such emissions. The problem was that the permit for one of these units allowed emissions of no more than 100 pounds per year. And, to my astonishment, the other unit had no permit at all.

To make matters worse, the plant had declared itself a “minor source” of air pollutants. In so doing, we represented to federal and state regulators that the plant’s annual emissions were less than 10 tons for any single HAP and less than 25 tons for any combination of HAPs.

The upshot of all of this was that the entire plant was grossly out of compliance with federal and state environmental laws that imposed tens of thousands of dollars of fines per day for every violation. Given the time that had elapsed since we made our minor source declaration, we calculated that our potential maximum fine could be astronomical. I was on a plane to Louisiana the next day.

Ultimately, I recommended that we avail ourselves of a voluntary disclosure program the EPA had initiated that offered the possibility of a significant penalty reduction if we were forthcoming, took swift corrective actions, and met other agency requirements. We also made a voluntary report to Louisiana

regulators. I'm pleased to report that our company was able to satisfy all of the voluntary disclosure program criteria and, miraculously, we escaped with no enforcement action and no fines.

Our HAP emissions issue is an example of circumstances in which the decision to voluntarily report a violation of law was a fairly easy one. We had made false representations to state and federal regulators that we were compelled by law to correct.

Moreover, many people in the plant were aware of the issue. Had we elected to keep the violation to ourselves and quietly take corrective actions, there was a strong possibility that one or more conscientious employees would have blown the whistle, in which case significant fines and a possible criminal enforcement action might be levied against the company and its management team.

However, there are many other circumstances in which there is no duty to report violations of law where it might be more prudent to avoid putting your fate in the hands of prosecutors. The following are three factors you should consider in making such a determination.

Magnitude of the violation

Corporations frequently discover actual or potential violations of law via routine vigilance or internal audits. But not all violations are created equal. Many may be fairly minor transgressions that can be swiftly corrected.

For example, a safety audit of a manufacturing operation may find that a mandatory machine guard is missing or that employees were not uniformly wearing hearing protection in designated areas as required by law. Such findings are common, and you can be assured that regulators do not want to hear about them. Instead of engaging in the costly exercise of voluntarily reporting such minor violations, your company's resources are better spent taking prudent and timely corrective actions.

By contrast, if your internal audit team discovers that senior executives have routinely paid bribes to win business in several countries around the world, serious consideration should be given to voluntarily reporting such violations of law to the appropriate authorities.

Risk of discovery

In many circumstances the risk of government regulators detecting a violation of law is very low. There simply aren't that many "cops" on the beat. But if the type of violation your company has committed is likely to be detected by government regulators, voluntary disclosure might be the right play.

Often, your employees pose the most significant risk that enforcement agencies will discover a violation of law. Many government agencies have whistleblower programs that not only give safe harbor to employees who come forward, they also pay sizable bounties in the event violations are confirmed and fines levied.

For example, the vast majority of False Claims Act enforcement actions brought by the DOJ originate from "relators" in *qui tam* actions often initiated by company employees. In the event fines are levied against perpetrators, relators can receive up to 30 percent of the take. Accordingly, if a significant fraction of employees is aware of a material violation of law, you should give serious consideration to getting in the regulator's door first.

Availability of government voluntary disclosure programs

Multiple state and federal agencies administer voluntary disclosure programs. A key factor you should consider in determining the prudence of self-reporting a violation of law to a government agency is whether it is possible to avail yourself of such a program. But your analysis should not stop there.

Before making a call on whether to self-report, take the time necessary to study the factors enforcement agencies will consider in determining your firm's eligibility for a penalty reduction. You should perform this work as soon as possible so you can advise your client on what to expect if they elect to make a voluntary disclosure and to ensure your company is ticking and/or is willing to tick all the necessary boxes to satisfy the regulators.

Finally, check with outside counsel who frequently interact with the enforcement agency that has jurisdiction over the violation in question. Ask counsel what the agency's track record is in crediting companies that avail themselves of voluntary disclosure programs. If the enforcement agency has a history of giving little to no credit for a voluntary report, that alone might be a good reason to quietly take corrective actions and move on.

Deciding whether to advise your client to self-report a violation of law is never easy. But by considering the three factors detailed above, you can be assured your opinion will rest on solid ground.

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