ERC
ETHICS RESOURCE CENTER

December 17, 2010

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File Number S7-33-10 -- Proposed Rules for Implementing the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934

Dear Ms. Murphy:

The Ethics Resource Center (ERC), the United States' oldest nonprofit organization devoted to the advancement of high ethical standards and practices in public and private institutions, is pleased to provide the Securities and Exchange Commission with its perspective on the proposed rules for implementing the new whistleblower provisions enacted in July 2010 as part of the Dodd-Frank Act. Since 1922, ERC has been a resource for organizations committed to strong ethical cultures.

In particular, ERC conducts independent research to help inform the public dialogue on ethics and ethical behavior. We believe that fact-based analysis is an essential element of effective regulation. In that spirit, we our pleased to share our new report "Blowing the Whistle on Workplace Misconduct," which provides insights into which employees are most likely to blow the whistle on misconduct, what type of behavior they are more or less likely to report, and to whom they tend to report their concerns. It also highlights the impact of corporate culture on both employee conduct and reporting activity, and finds that employees are more likely to report misconduct in companies with strong ethical cultures. We believe this paper may assist the SEC and other interested parties in the development of final rules and implementation of the new whistleblower provisions of Section 21 F.

In addition, we wish to share a few general observations:

The creation of a monetary reward fund for tips leading to a successful enforcement action under U.S. securities laws is designed to protect investors and the public as a whole from the painful effects of securities-related frauds. By creating an incentive for voluntary reporting by those with knowledge of such frauds, the reward fund aims to discourage misconduct by increasing the odds that violators will be identified and successfully prosecuted. In achieving that end, the fund also should support the effectiveness of U.S. capital markets by increasing public confidence in their integrity. The ERC strongly supports these objectives.

The ERC also believes that prevention is even better than punishment, and that the soundest and most fundamental long-term strategy for discouraging misconduct is the development of strong ethical cultures and the implementation of effective Ethics & Compliance (E&C) programs in business organizations and other private and public institutions. In our experience, institutions with committed leadership and effective E&C programs can build strong ethical cultures that encourage employees to report misconduct and reduce lawbreaking and other wrongful behavior.

Our review of the proposed rules has focused on the potential impact of the reward fund on corporate E&C programs and other voluntary efforts to build strong ethical cultures. We note the concern of other commentators that the proposed rules may incentivize employees with knowledge of misconduct to ignore internal processes for addressing possible bad behavior. That's important because, in the long run, strong E&C programs backed by senior leadership with a strong commitment to ethical conduct are the best way to prevent misconduct.

While employees certainly should assist government enforcement, going outside the organization as an *initial* step can potentially block organizations from identifying weaknesses in internal safeguards and deprive their leadership of an opportunity to make needed adjustments to E&C programs. In our experience, internal communication about ethics and compliance, including the opportunity for institutional leaders to build confidence by an aggressive response to bad behavior, is an invaluable opportunity to enhance ethical culture and make clear that acting with integrity is a core job responsibility for every employee.

To its credit, the SEC has noted the possible tension between the reward fund and internal company processes for responding to misconduct and says that the rules include provisions "intended not to discourage" whistleblowers from reporting violations internally at companies with robust E&C programs.

We respectfully submit that rules for the reward fund should be designed to support E&C programs by actively *encouraging* employees to initially work through their own institutions' processes. We urge the Commission to revisit the proposed rules and identify ways to build support for E&C programs and encourage whistleblowers to avail themselves of internal E&C reporting in addition to the whistleblowing provisions.

This is especially important because, as the Commission notes, the reward program applies only to violations of securities laws. Internal E&C programs must deal with a wide gamut of misconduct not covered by this proceeding. For example, one major company said in response to an ERC inquiry that it receives almost 5,200 calls to its ethics hotline a year, but that on average only two of these calls relate to possible securities fraud. A second company informed us that during 2010 it has averaged 634 hotline reports a month, including a total of three that raised concerns about securities law issues. It would be unpardonable if a program designed to address the single area of securities law violations was to reduce the effectiveness of E&C efforts aimed at a wider range of issues.

The Commission correctly notes that whistleblowers should be protected against retaliation. The 2009 National Business Ethics Survey prepared by the ERC found that about 15 percent of employees who reported misconduct perceived some retaliation. Much of the payback was in the form of subtle snubs and abuse by co-workers and may not rise to the level of an actionable offense. In addition to legal action against corporate retaliation, the SEC should work *with* employers to develop strong E&C programs to discourage any type of retaliation by a whistleblower's co-workers and supervisors.

Finally, we believe that the Commission has an opportunity to support private E&C programs by detailed reporting on the results of the new whistleblowing provisions, the reward fund, and their impact on E&C programs. E&C officials consistently say that information about the impact of E&C programs on enforcement decisions, particularly when such programs have a mitigating effect on prosecutorial decisions, is critical to improving E&C programs. It also enables them to build internal budgetary support for enhancing internal compliance initiatives. We urge the SEC to commit to a strong reporting program that provides E&C officers the information they require to strengthen their own compliance work.

We wish to commend the SEC for its ongoing efforts to improve its enforcement of securities law and to successfully implement the new whistleblowing provisions. We are pleased that the proposed rules recognize the value of internal E&C programs and also the possible tension between those programs and the new monetary reward fund. We would be pleased to provide the SEC with any additional information, research or other assistance to support both this rulemaking and subsequent implementation of the whistleblowing provision.

Should you have questions or need additional information, please do not hesitate to contact me at 703-647-703-647-2185.

Sincerely,

Patricia J. Harned, Ph.D.
President

ERC
ETHICS RESOURCE CENTER

Blowing the Whistle on Workplace Misconduct

December 2010

Founded in 1922, the Ethics Resource Center (ERC) is America's oldest nonprofit organization devoted to the advancement of high ethical standards and practices in public and private institutions. For 88 years, ERC has been a resource for organizations committed to a strong ethical culture. ERC's expertise also informs the public dialogue on ethics and ethical behavior. ERC researchers analyze current and emerging issues and produce new ideas and benchmarks that matter — for the public trust.

To learn more about ERC, visit www.ethics.org

BLOWING THE WHISTLE ON WORKPLACE MISCONDUCT

Like it or not, from time to time, people do the wrong thing. Some mistakes are unintentional; simple human errors that happen despite our best efforts to do the right thing. Other times, misconduct is deliberate; whether out of anger, frustration, or a desire to further their own self-interest, individuals will break the rules for any number of reasons. Depending on which rules are broken and who violates them, misconduct can hurt others – especially when it happens in a large business or other organization in which many people have a stake.

Given the potential of law breaking and other misconduct to destroy companies and the people who work for them, the development of ethical cultures that encourage people to act with integrity should be a high priority for both public and private institutions. With that in mind, the Ethics Resource Center is continuously working to understand workplace behavior, to identify how employees feel about the places they work, what factors affect their conduct, how they react when they see others break the rules, and what motivates them to take action. Our research is a constant work in progress; every day we learn more. The information we gather evolves continuously as circumstances change, environments transform, and employees revisit their attitudes and behavior.

Still, there is much that we know. For example, employees are more likely to blow the whistle on bad behavior when they feel good about their company and believe management has a strong commitment to ethical conduct. We also know that attitudes change depending on how management behaves, and also in response to external factors. Data collected by the ERC over the years show that conduct improves, at least for a time, after periods of public scandal and other difficulties — and seems to fall during boom times. Our most recent National Business Ethics Survey, for example, shows that response to misconduct was at its weakest in 2005 when the economy was strong, but strengthened after the recent recession. Employees surveyed in 2009 report that the amount of misconduct is down and company cultures are stronger.

As part of our commitment to advance public dialogue and assist the enforcement community, including company management and boards, government enforcement agencies, and ethics & compliance (E&C) officers, the following pages share some of what we've learned.

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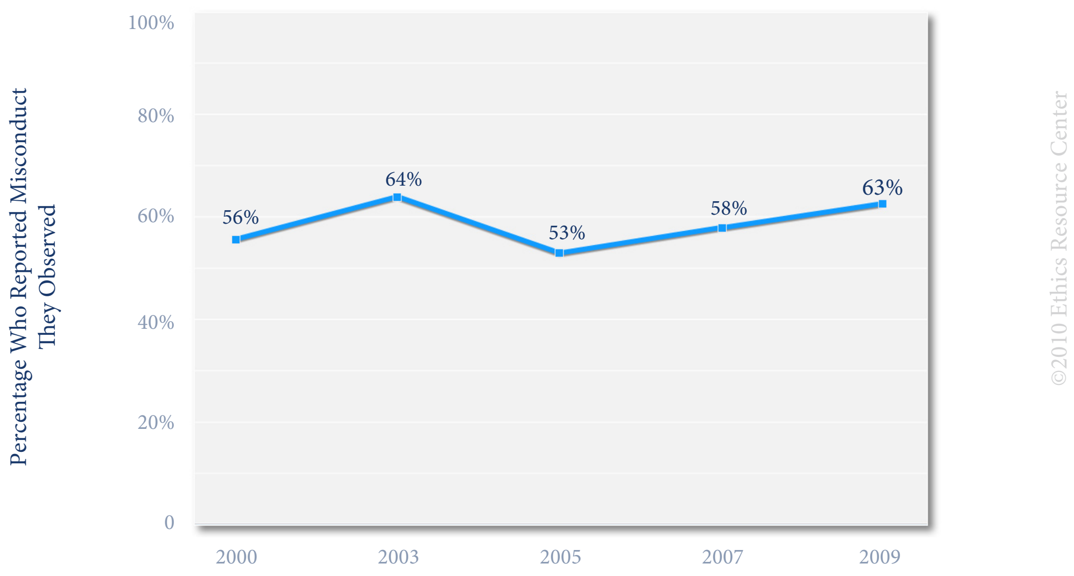
1. *"Ethics in the Recession," 2009 National Business Ethics Survey*, p. 9,The Ethics Resource Center, http://ethics.org/nbes

Corporate executives know that one of the best ways to pinpoint problems in their organization is to listen to whistleblowers. Experience shows there are more whistleblowers than many might expect. In 2009, more than six out of ten employees said they reported workplace misconduct when they saw it.

Employees, the people who know best the work environment, the attitudes of their peers, whether management means what it says about ethics, and whether people are breaking the rules, tell the ERC they will blow the whistle on bosses as well as co-workers. More than three-quarters surveyed by the ERC say they would not "look the other way" if their employer did something questionable.

ERC's annual National Business Ethics Survey (NBES), widely considered the U.S. benchmark on ethics, found that the share of workers who report negative behavior rose to 63 percent in 2009, a solid gain from 58 percent in 2007. Between 2000 and 2009 about 59 percent of employees on average said that they observed and reported misconduct, usually to an internal company authority. To an optimist, that data say the ethics glass is about 6/10ths full. That's encouraging because a lot of misconduct is being challenged. But it also means that there is still much work to do because over the decade, four in ten employees who witnessed workplace misconduct did not typically report it.[2]

Percentage Who Reported Misconduct They Observed: 2000 - 2009



2. *"Reporting: Who's Telling You What You Need to Know, Who Isn't, and What You Can Do About It, Supplemental Research Brief, 2009 National Business Ethics Survey*, pp. 1-2, The Ethics Resource Center, http://ethics.org/nbes

Thus, one of the critical challenges facing both E&C officers and government enforcement officials is convincing employees to step forward when misconduct occurs. Successful E&C programs work toward that goal by building cultures in which reporting misconduct seems like a normal part of the job. To that end, some companies have linked ethical conduct to performance reviews to make clear that good behavior is a job expectation. Other companies, believing that some workers do not report violations because they fear retaliation, have set up hotlines that assure reporting can be done in private with less risk of being seen by a co-worker. Similarly, Congress has included legal protections for whistleblowers and even established monetary rewards for tipsters to encourage insiders to come forward with information that could send wrongdoers to jail.

But, it turns out, that when employees report misconduct, the company hotline is one of the last places they go. Although hotlines provide confidentiality or even anonymity for employees nervous about tattling on a co-worker, only three of 100 reports about internal misconduct come to company hotlines, according to data collected by the ERC. Indeed, according to ERC's 2009 NBES, 15 percent of employees who observed and reported misconduct perceive retaliation as a result – most commonly a cold shoulder or verbal abuse from colleagues or a supervisor. About six in ten report snubs by co-workers and a similar number believe their supervisor excluded them from decisions or work activity as payback for reporting misconduct. More than four in ten say they almost lost their job or were denied a raise.[3]

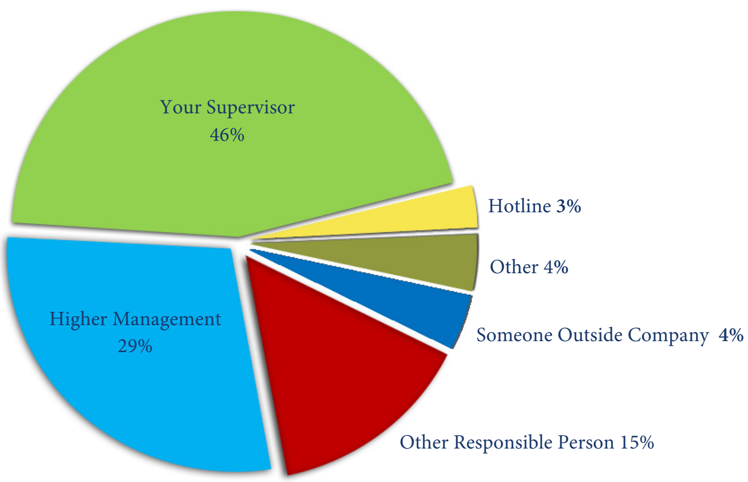
Specific Forms of Retaliation Experienced as a Result of Reported Misconduct (2009)

3. Op. Cit. *"Ethics in the Recession,"* p. 36

Despite the prospect of retaliation, the data show most employees would rather report wrongdoing directly to somebody they know than to a hotline. Some employees may believe their tips are more likely to be investigated when shared face-to-face instead of with a voicemail or an unfamiliar voice on a phone call.

For the largest number of employees (46 percent), the most likely place to report is an immediate supervisor. Higher management was the second favorite reporting location (29 percent) in 2009. Only three percent used company hotlines to report misconduct. A slightly larger number, four percent, took their suspicions outside the company as their initial action.[4]

In 2009, as in 2007, Vast Majority of Reports Made to Managers



Most employees would rather report wrongdoing directly to somebody they know than to a hotline.

4. Op. Cit. *"Reporting: Who's Telling You What You Need to Know, Who Isn't, and What You Can Do About It,"* p. 15

One major U.S. company receives an average of 431 hotline tips every month.

That's not to say that hotlines lack value. While hotline reporting makes up a relatively small percentage of all employee tips about misconduct, the absolute number of hotline reports can be large. One major U.S. company, for example, told ERC confidentially that it receives an average of 431 hotline tips every month and that, on investigation, almost 20 percent of these lead to findings of misconduct.

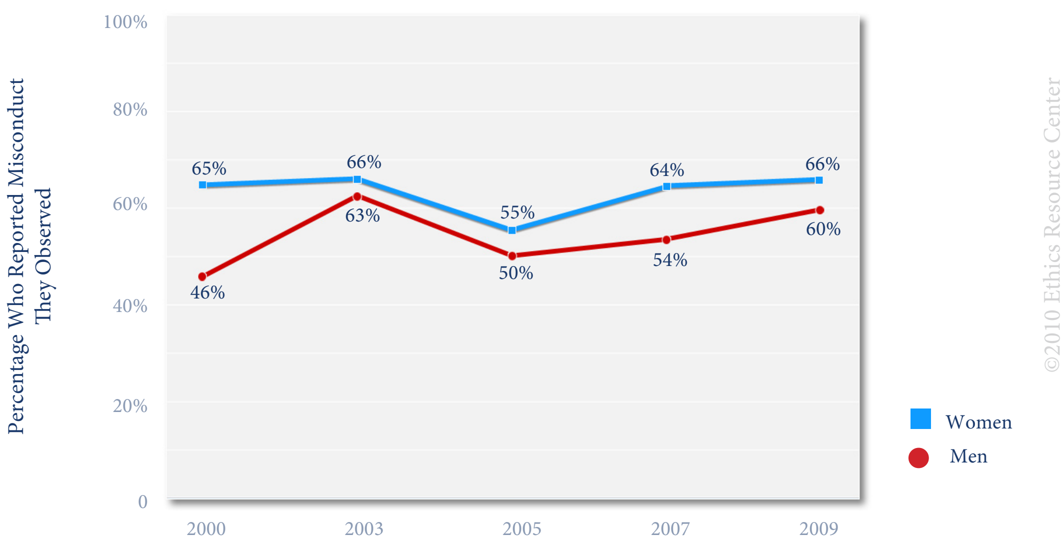
Understanding the venues employees choose for reporting can help us understand what motivates workers to report misconduct and how to encourage more. The data tell us that the decision to report to one's direct supervisor versus higher management is related to the ethical culture and climate of the workplace. In strong cultures – with a tone at the top that makes clear that ethics matter, where supervisors aggressively reinforce the ethics message, and where employees and managers alike are truly held accountable to high standards — more employees report to their direct supervisor. Conversely, reporting to higher management increases in weaker cultures and among employees who feel pressure. When paired with other findings, it appears that employees in weak cultures tend to report to higher management rather than direct supervisors because they aren't confident that lower level managers are fully committed to strong ethics. In some cases, they may fear retaliation for sharing their concerns. Or, they may simply lack confidence that their direct supervisor will pursue the issue. In those instances, turning to senior management can provide the safety of the organizational structure and a belief that higher management has the resources to address the issue effectively.

In designing E&C programs, it also helps to know whether some categories of workers are more likely than others to report misconduct and which behaviors they are most likely to tag. Knowing the answers can help identify deficiencies and possible vulnerabilities so that enforcement programs can be adjusted. Understanding employee expectations is another important factor in designing strong programs.

WOMEN REPORT WRONGDOING MORE OFTEN THAN MEN

In an effort to find out more about likely whistleblowers and what they report, the ERC delved deeper into the 2009 NBES data. We found that women are consistently more likely than men to report misconduct, but that men have been narrowing the gap. During 2009, 66 percent of women who were aware of misconduct said they reported it, compared to 60 percent for men. In some years, fewer than half of men who had observed misconduct shared that information. For women, the low point in reporting was 55 percent in 2005, a down year in reporting across the board.

Women Tend to Report More Than Men



Reporting also varies with the nature of the misconduct. For example, workers of both genders are far more likely to report stealing, abusive behavior, health violations, and product quality problems than "Internet abuse" or privacy violations. Only 41 percent of women and 35 percent of men say they reported instances of lying to customers or the public, but about 45 percent of both genders reported lying to employees. Women are far more likely than men to report sexual harassment, but men are more likely to report co-workers who lie about hours worked or falsify their expense accounts.[5]

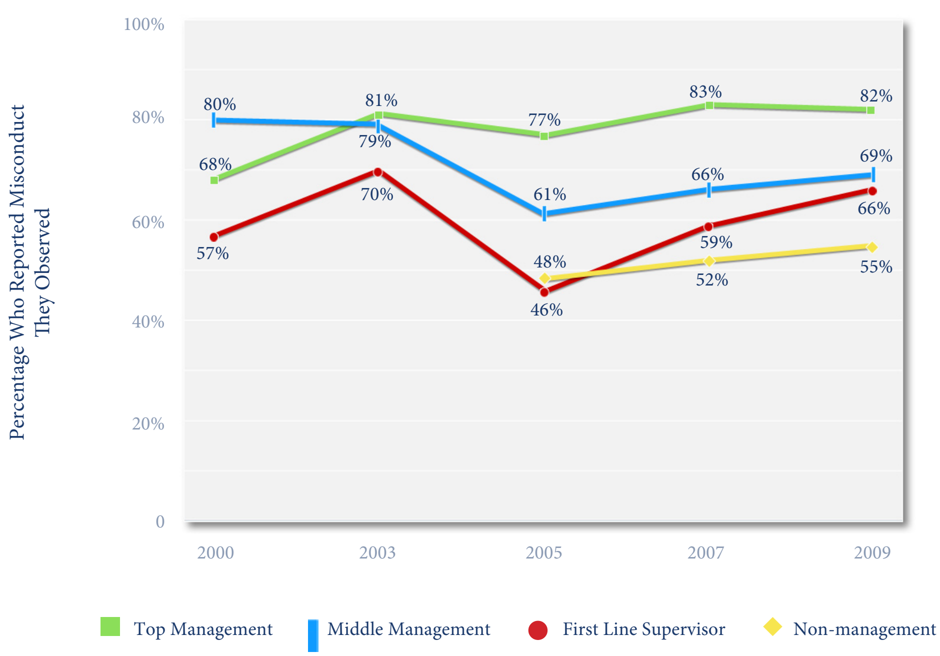
	Women	Men	PPt Differ.
OVERALL REPORTING	**66%**	**60%**	**6%**
Reported Sexual Harassment	64%	39%	26%
Reported Substance Abuse	61%	47%	13%
Reported Abusive Behavior	68%	56%	12%
Reported Stealing	68%	58%	10%
Reported Health Violations	64%	55%	9%
Reported Alteration of Documents	54%	46%	8%
Reported Customer Privacy Breach	45%	38%	6%
Reported Lying to Customers, Vendors or the Public	41%	35%	5%
Reported Employee Benefit Violations	59%	55%	4%
Reported Improper Hiring Practices	39%	36%	2%
Reported Conflict of Interests	54%	52%	2%
Reported Company Resource Abuse	45%	44%	1%
Reported Misuse of Confidential Information	50%	49%	1%
Reported Lying to Employees	45%	44%	0%
Reported Poor Product Quality	60%	60%	0%
Reported Internet Abuse	37%	38%	-1%
Reported Employee Privacy Breach	42%	46%	-4%
Reported Discrimination	42%	47%	-5%
Reported Falsifying Time and/or Expense Reports	47%	52%	-5%

5. Ibid. pp. 3-4

The data also show that managers are significantly more likely than line employees to report every form of misconduct, and that senior management consistently reports wrongdoing more than any other group. The high rates for senior management suggest that those at the top of organizations generally have a greater appreciation of the importance of ethical conduct to the success of the enterprise. It also may reflect less worry about retaliation as individuals move up the organizational ladder.

During 2009, 82 percent of top management said they reported misconduct. That number has been relatively steady throughout the past decade, dipping below 80 percent only in 2005, a year in which all levels of workers and managers say they were less diligent in reporting bad behavior. Almost seven in ten middle managers (69 percent) and two thirds of line supervisors also reported misconduct in 2009, compared to 55 percent of all non-management personnel. Reporting by both middle-management and line supervisors was up significantly from 2007, but below peaks for the decade. In 2003, for example, 79 percent of middle managers who observed misconduct said they reported it, as did 70 percent of line supervisors. Curiously, middle-managers are significantly less likely than first-line supervisors or top management to report misconduct in four of six specific areas surveyed, suggesting possible areas of vulnerability. Middle managers were less likely than line supervisors to report lying, Internet abuse, and abuse of company resources during 2009.[6]

Reporting Rates Rise Along With Management Level



6. Ibid. pp. 9-10

Shining through all the data is the overriding fact that ethical cultures matter. Culture, as defined through ERC research, is the extent to which a strong commitment to ethics is set at the top, that the message is reinforced throughout all levels of management, and that employees perceive the ethical standards really matter in an organization's day-to-day operations.

Employees are more likely to conduct themselves with integrity and report misconduct by others when they believe senior management has a genuine and long-term commitment to ethical behavior. In addition, ongoing work by the ERC Fellows reveals that those who report misconduct are motivated by the belief that their tips will be properly investigated. Perhaps surprisingly, most employees are less concerned with the particular outcome than in knowing that their report was seriously considered.

Most employees are less concerned with the particular outcome than in knowing that their report was seriously considered.

Beliefs About Company	Reporting Rate of Those Who Agree/Strongly Agree With This Belief	Reporting Rate of Those Who Disagree/Strongly Disagree With This Belief	PPt Differ.
Employees can raise concerns to management without fear	67%	55%	12%
I trust executives are being truthful about our company's well-being	67%	56%	11%
The senior-most executive is appropriately compensated	67%	58%	9%
My company motivates me to contribute more than is required	66%	57%	9%
I am aware of the financial health of my company	65%	56%	9%
Overall, I have confidence in executives	65%	56%	9%
I feel optimistic about the company's future	65%	60%	5%

Among the most important indicators of how individuals respond to wrongdoing is personal beliefs. The data show that those with a stricter personal code of workplace conduct are more likely to report than those who are more comfortable with "gray area" behavior. Perhaps more significant for E&C officers is a clear connection between reporting and the way employees feel about their company, its culture, and its leadership. Those with positive attitudes about the company are more likely to help it succeed by reporting when rules are broken.

The data show that reporting of misconduct is significantly higher when an E&C program includes a useful code and meaningful training that prepares workers to assess and respond to bad behavior. That data is striking. More than seven of ten workers who feel "very well prepared" by company training say they report wrongdoing, while only 25 percent who say they are very poorly prepared will blow the whistle on a co-worker.

Workers are far more likely to report misconduct (73 percent to 55 percent) in organizations with strong ethical cultures, including a clear commitment from senior management. By a 72 percent to 60 percent margin, employees who have a personal stake by owning company stock also are more likely than non-shareholders to report misconduct.[7]

But the most significant driver of responses to misconduct is employees' perception of senior management. Only 55 percent of employees in a weaker culture report misconduct, but 73 percent who say they work in a strong ethical culture report wrong doing. By every indicator, employees are more likely to report misconduct when management sends positive messages about ethics.[8]

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7. Ibid. pp. 18-19
8. Ibid. p. 20

Level of Ethical Culture	Behavior	Reporting rate of those who disagree or strongly disagree that management exhibits this behavior	Reporting rate of those who agree or strongly agree that management exhibits this behavior
Top Management	Sets a good example of ethical behavior	52%	69%
	Can be trusted to keep promises and commitments	55%	70%
	Provides satisfactory information about what's going on in the company	55%	69%
	Talks about importance of workplace ethics and doing the right thing	52%	66%
Supervisor	Gives positive feedback for ethical behavior	50%	68%
	Provides satisfactory information about what's going on in the company	55%	67%
Coworker	Talks about importance of workplace ethics and doing the right thing	52%	66%
	Considers ethics when making workplace decisions	57%	67%

The way an employee feels about a company also shows up in his or her attitude about internal investigations. When the ERC Fellows surveyed employees who reported problems to a company hotline, most said they were more concerned about way the inquiry was handled than in the final resolution of the case. Even when they disagree with the outcome, preliminary analysis says that 81 percent were satisfied because they believe the procedure was fair. Procedural fairness also increases employees' commitment to the company. If employees trust that the E&C system is fair, they are more likely to work within that structure than to file complaints outside of the company, the Fellows concluded in a report to be published in 2011. Conversely, those who believe the process is flawed or inadequate are more likely to leave the company or take grievances to outsiders. Preliminary data show that quality of decision-making and trust in the investigatory team are the two elements that matter most.

MOVING FORWARD

Enforcement officials cannot uncover all wrongdoing by their own efforts alone. Discovering misconduct requires the help of others, especially reporting by those who have observed the misbehavior. Therefore, our work to advance ethical behavior in businesses and other organizations requires the assistance of those who are often most in the know – rank and file employees as well as managers who see workplace behavior up close every day. Right now, about sixty percent who observe misconduct are likely to report it. Boosting this percentage is an important goal for private sector E&C programs and government enforcement agencies alike.

Research tells us that employees' willingness to report co-workers' misconduct varies according to a variety of factors, including their own personal standards, their level of corporate responsibility, and their feelings about the place where they work. Some need more support than others; some respond to incentives such as monetary rewards; others are concerned with procedural fairness; and some will report if provided a convenient tool such as a hotline. But across the board, culture is critical. When we succeed at building ethical cultures with strong training programs and committed management, reporting of misconduct goes up and wrongdoing goes down. Attitude matters. If we want to boost the odds of ethical conduct, attitude and culture are places for focus.

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