

Both Public and Private Cooperatives Should Consider Implementing a Whistleblower Policy

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Many cooperatives in the United States have elected to register their stock with the Securities and Exchange Commission (“SEC”). Examples include Gold Kist, Inc., CHS, Inc., Growmark, Inc., Land o’ Lakes, Inc., and American Crystal Sugar Company. As a result, these cooperatives are considered “public” companies under the federal securities laws and are subject to certain securities laws and requirements. Although non-public cooperatives, referred to here as “private” cooperatives, are not required to register their stock with the SEC, a private cooperative should consider adopting reasonable policies and procedures that deal with accounting and regulatory issues because the adoption of such policies may be what has become known as a “best practice” in the operation and management of the cooperative.

The types of policies and procedures that a cooperative should consider adopting as best practices vary from cooperative to cooperative, but the laundry list of policies to consider usually includes: (1) an audit review policy; (2) a policy regarding accounting and auditing matters; (3) a document retention policy; and (4) a code of ethics. The remainder of this article will focus on the policy regarding accounting and auditing matters, commonly referred to as a “whistleblower policy.”

The Requirements of the Sarbanes-Oxley Act

Section 301(4) of the Sarbanes-Oxley Act (“SOX Act”) requires that public companies establish procedures for the “receipt, retention, and treatment of complaints received by the issuer regarding accounting, internal accounting controls, or auditing matters,” and procedures for the “confidential, anonymous submission, by employees of the issuer, of concerns regarding questionable accounting or auditing matters.” The SOX Act prohibits public companies from taking any retaliatory action against

an employee for commencing or participating in an investigation of conduct the employee reasonably believes violates U.S. securities or antifraud laws.

The Act provides a private right of action and compensatory damages for such retaliation, including reinstatement with the same seniority status, back pay with interest, and compensation for litigation costs, expert witness fees and reasonable attorneys’ fees. Additionally, the SOX Act makes it a crime for anyone, whether in a public or private company, to retaliate against informants involved in exposing a federal offense, including by interfering with the informant’s employment or livelihood. This crime is punishable by a fine of up to \$250,000 for individuals (\$500,000 for organizations) or imprisonment for not more than 10 years, or both. Accordingly, both private and public cooperatives should review and update their personnel policies in light of the broad scope of this protection. Human resource professionals should also consider the whistleblowers and informants covered by this section as a new “protected class” when assessing legal risks involving terminations and other employment actions.

Handling Employee Complaints

For a public cooperative, the SOX Act requires that the cooperative establish an anonymous procedure for handling employee complaints. A cottage industry has sprung up around this requirement, and there are now dozens, if not hundreds, of companies that offer services to public cooperatives and other companies. These services range from operating phone and e-mail hotlines to utilizing private investigators to investigate complaints. Even the well-known security company Pinkerton now offers SOX Act investigation services. However, in order to work, a complaint process must have several key ingredients.

- **The complaint process must be credible.** If employees are to use the system, they must trust that their identity will be confidential and that they will not be retaliated against by management. Making a complaint must be a relatively easy task.
- **The person receiving the complaint must be viewed as neutral.** Employees are less likely to make complaints if the employees believe that the person receiving the complaint is a mouth-piece of the management. In a private cooperative, this may mean using an “ombudsman,” which is a person who may or may not be employed by the private cooperative, but who is charged with being neutral with respect to handling employee complaints. A private cooperative may also choose to utilize the services of its outside legal counsel, a former board member, or a third party service provider. The key ingredient is that employees view the party receiving the complaint as neutral and accessible. Many employees may feel that the risk of retaliation is greater if there is internal involvement in the complaint process.
- **There must be meaningful follow-up.** If a complaint is made anonymously, follow-up may range from asking a few questions to conducting an involved investigation. In order to properly evaluate the complaint, the party who is responsible for following up must either have a reasonable knowledge of accounting and legal matters, or have the authority to retain consultants who can conduct an adequate investigation. If the system is to have integrity with employees, the system must have in place a process for adequate follow-up on complaints.
- **Reporting the results of the investigation.** The SOX Act requires the audit committee of a public cooperative to establish procedures for investigating complaints. The Act also gives the audit committee the authority to hire independent counsel to conduct investigations. In most cases, whistleblower complaints received by a public company will be reported to the audit committee and there will be a discussion at the audit committee level about what action to take. For private cooperatives, there is a broader range of how results will be reported. Many private cooperatives do not have audit committees, and depending upon the magnitude and type of complaint, the complaint may be reported to a

member of management who is not implicated in the complaint or to the board. Regardless of whether the cooperative is public or private, the whistleblower policy should address who gets a copy of the complaint and the report, and equally important, who does not get a copy of the complaint and the report.

- **Taking action.** Once the complaint has been made, investigated, evaluated, and reported, the next step is taking action to address the complaint if the investigation reveals a legitimate violation. Depending upon the severity of the activity that has given rise to the complaint, corrective action may range from employee discipline to contacting legal and regulatory authorities.

There is No “One-Size Fits All” Approach

Cooperatives range in size from just a few members to thousands of members; from thousands of dollars in revenue to billions of dollars in revenue. Some cooperatives are large public companies with regulatory mandates, while others are small local cooperatives with few, if any, formal policies. The methods for handling employee complaints can legitimately run from designating a neutral employee or third party as an ombudsman to formal written policies that establish formal complaint procedures and utilize outside vendors.

Like many areas in the cooperative world, there is not a “one-size fits all” solution. Instead, it is up to the board of directors, the audit committee, and sometimes the members of a cooperative to decide whether or not there are adequate financial controls in place, including a process to receive, investigate, report on, and act on employee complaints regarding accounting and auditing matters.

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