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New York Issues Whistleblower Guidance to All DFS-Regulated Institutions

Consumer Finance Monthly Breakfast Briefing

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DFS Guidance

- New York State Department of Financial Services (DFS) issues guidance on January 7, 2019
- Applies to all entities chartered, licensed, or regulated by the DFS
- Enunciates principles that all regulated institutions should account for when designing and implementing a whistleblowing program

What Is Whistleblowing?

- Report of information or concern – by virtually anyone
- May involve reasonable belief of:
 - Illegality
 - Fraud
 - Unfair or unethical conduct
 - Mismanagement
 - Abuse of power
 - Unsafe or dangerous activity
 - Other wrongful conduct (may affect reputation or safety and soundness)

Elements of An Effective Program

1. Clear and consistent reporting channels
2. Anonymity protections
3. Procedures for managing conflicts of interest
4. Adequately trained staff to handle the investigation
5. Established investigation procedures
6. Established follow-up procedures for valid complaints
7. Retaliation protections
8. Confidential treatment
9. Appropriate oversight
10. Top-down culture of support for whistleblowing program

Barclays Bank Consent Order

- December 18, 2018: DFS announces Consent Order with Barclays Bank
- Bank is fined \$15 million under New York banking law provisions for conducting business in an unsafe and unsound matter by failing to implement effective governance and controls around whistleblowing program
- Bank received two anonymous letters concerning the recruitment and hiring of a senior executive that the CEO had recruited
- CEO then personally directed the head of security to attempt to identify the author(s) of the anonymous letters

What the Bank Did Right

- Commissioned a broad, independent review of business practices & culture
- Adopted substantially thorough whistleblowing policies and procedures
- Implemented anonymous reporting channels via phone or email to internal or external service
- Implemented a program through which senior managers are placed in Group Compliance for a 3-month rotation
- Established a dedicated Investigations & Whistleblowing Team
- Annual employee training
- Created a “Whistleblowers’ Champion” position to oversee the I&W Team
- Created a “Global Head of Whistleblowing” position
- Drafted an Anonymity Policy

What Went Wrong

- Anonymous letter sent to several members of Board
 - Letter contains accusations about personal issues of a recently-hired bank executive
 - CEO is specifically criticized for his role in soliciting this executive to join the bank
 - CEO believed the bulk of the allegations to be false, but understood that certain accusations were accurate
- Letter should have been forwarded directly to I&W Team but was not immediately recognized as a whistleblower complaint and instead was circulated among senior execs
 - CEO expresses desire to know who wrote the letter
- 2nd anonymous letter arrives three days later
- CEO contacts chief information security officer (CISO) and asks him to identify sender

What Went Wrong (cont.)

- CISO enlists a cybersecurity intelligence analyst who is temporarily assigned to an outside cybersecurity organization that included law enforcement agents
- The analyst asks contacts in US law enforcement agencies for assistance
- CISO learns from General Counsel and HR that the letters might be whistleblows, such that efforts to identify the author would be improper
- In a meeting among the executives, the GCCO and GC both firmly advise the CEO against trying to ID the author (discussion not memorialized)
- I&W concludes allegations were unsubstantiated; advises CEO of risks to bank that would flow from attempting to ID author (not documented)
- Three days later CEO resumes efforts to ID the letters' author
- He also texts a former colleague about it

DFS Findings

- Failure to follow or apply the whistleblowing policies and procedures in a manner that protected the bank and its CEO
- Incomplete positive cultural transformation
- CEO erred in seeking to identify the author(s) and by communicating about the matter outside of the bank
- As a principal witness, he had a conflict of interest
- He failed to consult directly with either the GCCO or GC before resuming his search for the author's identity
- His actions failed to serve the independence of the whistleblowing function

DFS Findings (cont.)

- Undermined the process and exposed the bank to additional risk by discussing the letters outside of the bank
- Other senior executives missed opportunities to intercede
- Despite generally suitable policies and procedures, there was a limited gap in guidance concerning identification and handling of whistleblower complaints that —
 - Both *involved* senior management and
 - Might also be *received* by senior management or the Board

Cooperation and Corrective Action Taken

- Acceptance of responsibility
- “Very substantial” cooperation with the DFS investigation
- To address the deficiencies in its whistleblowing program, the Bank:
 - Engaged an outside consultant to perform an independent review of whistleblowing policies, processes, and controls
 - Revised its procedures to recognize that concerns raised outside certain whistleblowing channels may nevertheless constitute whistleblows
 - Established procedures to avoid escalating a whistleblower to the subject of the concern
 - Instituted controls to preserve whistleblower anonymity

What Does the DFS Guidance Mean for Non-Bank Institutions Regulated by DFS?

- No express legal requirement to establish a whistleblowing program
- Many institutions already have programs in place – but they may merit reevaluation
- Remember no “one size fits all” approach
- Lessons learned from Barclays story



Questions?



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