

Study Proves the Value of Whistleblowers in Bringing Down Fraudsters

August 31, 2017

A recent [study](#) published in the *Journal of Accounting Research* examines whether the participation of a whistleblower affects the outcome of an enforcement action against companies that commit financial fraud. The study seeks to quantify the impact of a [whistleblower's](#) tip or assistance during an investigation on the final penalties levied on a company or an executive, in comparison to enforcement proceedings in which there's no cooperation with government regulators. The study shows there is a stark difference in outcomes, but advises the results should be viewed with caution due to the large range of crimes studied, and wide assortment of outcome variables, including personal financial penalties, firm sanctions, and prison time.

Findings from Whistleblower Study

The study determined that investigations of financial misrepresentation were more likely to lead to sanctions when a whistleblower was involved, and the sanctions were significantly higher in cases with whistleblowers. Specifically when a whistleblower was involved companies were penalized an average of \$22 million more, and personal fines were an average of \$47 million higher than cases where there was no whistleblower.

The probability of criminal sanctions against employees also increased with whistleblower cooperation – by 6.6%. And what may hurt fraudsters the most: whistleblowers' involvement broadly contributes to prison sentences of a year and a half longer.

Variations in Activity and Controlling for Factors

When assessing the findings of the whistleblower study, a number of factors should be taken into consideration. A whistleblower or insider can be of assistance to regulators in numerous ways, and the degree to which they cooperate can vary dramatically from case to case.

Despite what the public may believe to be true, many whistleblowers only become involved with regulators after an investigation is underway. While this may be slightly less dramatic and noble than somebody who brings injustice to light by filing a tip with federal regulators, whistleblowers who speak under these circumstances nonetheless prove invaluable to ensuring more severe penalties. The study did not differentiate based on when, and in what capacity, a whistleblower became involved. It was a binary variable, and a separate study is needed to see if the degree of participation is significant to the outcome.

Additionally, there are many factors, outside of the participation of whistleblowers that could explain the spectrum of penalties. Controlling for external factors is essential for any empirical research. So here the researchers controlled for these “third variables” such as how important the fraud was to the wellbeing of the company, the damage done to innocent people, how widespread the violation was, and many other factors that would undeniably change the extent and degree of the penalties.

Investigating financial fraud is difficult, because of the complexity of financial and accounting

principles and the varied standards and practices of different industries. This study proves the value of whistleblowers in helping regulators acquire the evidence they need to bring those who steal and commit fraud to justice.