

NEW SEC WHISTLEBLOWER RULES: EARLY RESULT

One notable provision of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) is entitled "Securities Whistleblower Incentives and Protections."¹ It directs the U.S. Securities and Exchange Commission (SEC) to make monetary awards to eligible individuals who voluntarily provide original information leading to successful SEC enforcement actions against listed companies, which result in monetary sanctions over \$1,000,000.

These bounties, or awards, will be 10-30% of the sanctions collected. The SEC was also directed to establish an office within the Commission to administer the whistleblower program and report back to Congress annually on its activities, whistleblower allegations and the response of the SEC to such complaints.² This *Alert* looks at the report recently released by the SEC addressing the early days of the Dodd-Frank whistleblower program.

TIPPING

After soliciting and receiving extensive suggestions and commentary, the SEC revised and refined its proposed rules for the new whistleblower program. These became effective on August 12, 2011 (the Final Rules). Among other things, the Final Rules establish procedures for submitting tips and applying for awards, describe the criteria the SEC will consider in making award decisions and implement Dodd-Frank's prohibition against retaliation for whistleblowing by employees.

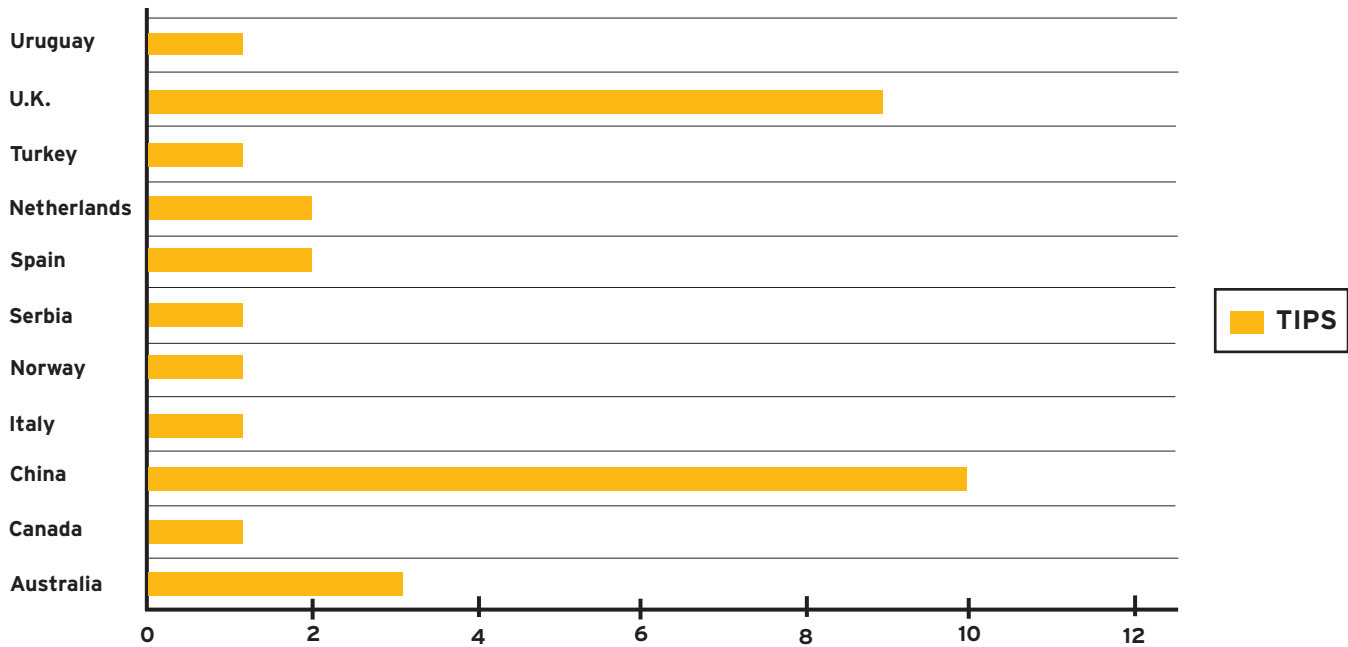
For the report on fiscal year 2011, only seven weeks of whistleblower tip data was available (fiscal years end on September 30; with the Final Rules first becoming effective on August 12, the report only covers the seven weeks between August 12 and September 30).³ This makes it too early to identify with certainty any specific trends or conclusions from the



data collected to date. Even so, there are interesting observations to be made in looking at the early data:

- During the first seven weeks the Final Rules were implemented, 334 whistleblower tips were received – or roughly 50 per week.
- The most common identified complaints alleged market manipulation (16.2%), offering fraud (15.6%) and issues related to corporate disclosures and financial statements (15.3%).
- Tips came from 37 states, with the largest numbers coming from California, New York, Florida and Texas, while 10% came from foreign countries, with the largest number coming from China (31% of overseas tips) and the U.K (28% of international tips).⁴

Overseas Whistleblower Tips Received by Geographic Location 8/12/2011 - 9/30/2011⁵



BOUNTY HUNTERS

The Final Rules set out the procedures for tipsters applying for whistleblower awards. The process begins with the entry of a final judgment or order for monetary sanctions that exceeds \$1 million.⁶ Following the entry of such a judgment, a notice is published on the SEC's website.⁷ Individuals then have 90 calendar days to apply for an award by submitting a completed whistleblower award application.

On August 12, notice was posted of 170 applicable enforcement judgments and orders where sanctions were imposed that exceeded the \$1M threshold for whistleblower bounties. This potentially translates into a *minimum* range of \$17M to \$51M in bounties. As the 90-day application period had not elapsed by the end of the fiscal year covered by the report, award applications had not yet been processed. Therefore, the Commission did not pay any whistleblower awards during fiscal year 2011.

Inquiring minds wishing to see the list of settlements or court awards suitable for the Dodd-Frank bounties can view the full updated list at <http://www.sec.gov/about/offices/owb/owb-awards.shtml> on the SEC's Office of the Whistleblower website at <http://www.sec.gov/whistleblower>.

BOUNTY FUNDING

Dodd-Frank also established the Securities and Exchange Commission Investor Protection Fund to provide funding for the whistleblower award program.⁸ Its balance at beginning of the current fiscal year was a robust \$453 million or *close to half a billion U.S. dollars*. The actual funding itself comes from undistributed sanctions from other SEC cases; i.e., for the foreseeable future, there will be no shortage of funding for whistleblower bounties.⁹

INITIAL OBSERVATIONS AND LINGERING CONCERNS

It bears repeating that the published data only covers the first seven weeks of initial application of the Final Rules, so there is much still to be learned. Looking at what we do know, as a number of tipsters may have been waiting for the Final Rules to take affect in order to submit their tips, the initial rate of roughly 50 tips a week may **not** be matched during the next full year's figures. There are, however, currently several large settlements being finalized where there are rumors of whistleblower bounties being considered. So we **are** likely to see significant bounties paid over the coming year. One early concern about the new Dodd-Frank whistleblower rules has been its global reach; the initial tally of 10% of tips coming from outside the U.S. makes this appear to be a valid concern for those operating internationally.

In addition to what the statistics can tell us, we have yet to develop a real understanding of the interaction or perceived potential conflicts between the new whistleblower bounties and protections on the one hand, and existing corporate integrity programs on the other. The significant cash incentives for employees to race to the SEC's door to provide "original information" leading to an enforcement action rather than to utilize the organization's own internal reporting procedures, is troublesome. Combined with Dodd-Frank's new protections from retaliation for whistleblowers – where employees who take their complaint to the SEC have **greater protection** under the law than employees who simply raise their concerns within the company – the potential for an adverse impact on internal compliance programs seems real and sizable.

Please stay tuned as we continue to monitor these developments.

If you would like to read more about some of Dodd Frank's most important provisions, from an executive risks viewpoint, please see: **September 2010 Alert, Executive Risks and the Wall Street Reform and Consumer Protection Act [Dodd-Frank]**.

CONTACTS

Please direct any questions or requests for additional information to your Willis Client Advocate® or **ERPublications@willis.com**.

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¹ For those who love section numbers, this appears in § 922 of Dodd-Frank and adds § 21F.

² The Exchange Act § 21F(g)(5) also requires the SEC to submit to Congress an annual report addressing the whistleblower award program, including a description of the number of awards granted and the types of cases in which awards were granted during the preceding fiscal year.

³ This report can be see at: <http://www.sec.gov/about/offices/owb/whistleblower-annual-report-2011.pdf>

⁴ Page 5 of the SEC's Annual Report on the Dodd-Frank Whistleblower Program, Fiscal Year 2011. With the data on state demographics coming from the Report's Appendix B: Whistleblower Tips Received by Geographic Location – Domestic 8/12/2011 – 9/30/2011 and that of the foreign tips from Appendix C: Whistleblower Tips Received by Geographic Location – Overseas 8/12/2011 – 9/30/2011.

⁵ See: Appendix C.

⁶ This amount is assessed singly or jointly with other judgments or previous orders in the same action or an action based on the same operative facts.

⁷ By posting a notice (formally a Notice of Covered Action) for a particular case, the SEC is not actually making a determination either that (i) a whistleblower tip, complaint or referral led to the Commission opening an investigation or filing an action with respect to the case or (ii) an award to a whistleblower will be paid in connection with the case; merely letting tipsters know to get their application in if this has occurred.

⁸ In Section 922, modifying the Exchange Act § 21F(g)(2)(A). The Fund is also to finance the operations of the SEC Office of the Inspector General's suggestion program. This is a program for suggestions from Commission employees for improvements in the work efficiency, effectiveness, and productivity, and use of resources at the Commission, as well as allegations by Commission employees of waste, abuse, misconduct, or mismanagement within the Commission.

⁹ *Dodd Frank Act Section 922 WHISTLEBLOWER PROTECTION. (g) INVESTOR PROTECTION FUND – 3) DEPOSITS AND CREDITS. – (A) IN GENERAL. – There shall be deposited into or credited to the Fund an amount equal to –*

(i) any monetary sanction collected by the Commission in any judicial or administrative action brought by the Commission under the securities laws that is not added to a disgorgement fund or other fund under section 308 of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7246) or otherwise distributed to victims of a violation of the securities laws, or the rules and regulations thereunder, underlying such action, unless the balance of the Fund at the time the monetary sanction is collected exceeds \$300,000,000;

(ii) any monetary sanction added to a disgorgement fund or other fund under section 308 of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7246) that is not distributed to the victims for whom the

Fund was established, unless the balance of the disgorgement fund at the time the determination is made not to distribute the monetary sanction to such victims exceeds \$200,000,000; and

(iii) all income from investments made under paragraph (4)