

# SPIES AMONG US?

Understanding and Demystifying the New  
Dodd-Frank Whistleblower Provisions

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# Speakers



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*Partner, Securities Litigation and SEC Enforcement*

Concentrates her practice in the areas of securities litigation, including class action defense; SEC investigations, numerous internal investigations for audit committees and other board committees into accounting and other corporate governance-related issues; derivative litigation and other fiduciary duty claims; M&A litigation; founder and partnership disputes.



## **David B. Pitofsky**

*Partner, White Collar Crime & Government Investigations*

Represents individuals and corporations in connection with white collar criminal investigations and prosecutions, regulatory investigations and lawsuits, internal corporate investigations. Prior to joining Goodwin Procter, Mr. Pitofsky worked for the United States Attorney's Office for the Eastern District of New York, where he was Principal Deputy Chief of the Office's Criminal Division.



## **Heidi Goldstein Shepherd**

*Partner, Labor & Employment*

Extensive experience representing the firm's management and institutional clients in all aspects of the employment relationship. She has successfully represented clients in a variety of labor and employment litigation matters, including employee whistleblower and breach of employment contract actions arising under federal and state laws.

# Agenda

- WHISTLEBLOWER PROVISIONS OF THE DODD-FRANK ACT
- PROPOSED SEC IMPLEMENTING REGULATIONS
- WHAT CAN YOU DO TO BE PREPARED ON THE COMPLIANCE SIDE?
- WHAT TO DO WHEN THE WHISTLE BLOWS?
- QUESTIONS

# WHISTLEBLOWER PROVISIONS OF THE DODD-FRANK ACT

# 2010 Financial Regulatory Reform - Whistleblower Revisions

- Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 contains sweeping changes to whistleblower claims.
- Encouraging whistleblowers to go directly to SEC to obtain increased monetary incentives (award of 10%-30% of monetary sanctions obtained by the government over \$1 million for providing original information, and double back pay for retaliation claims).
- Bypasses prior administrative process of DOL / OSHA for retaliation claims; can bring suit directly in Federal Court.
- Establishes SOL for retaliation claims:
  - › 6 years from occurrence; or
  - › 3 years from discovery or facts that should have reasonably led to discovery; but
  - › no greater than 10 years after the occurrence.

# What is a “Whistleblower”?

- “Whistleblower” is used broadly to mean any person who voluntarily provides “original” information relating to a violation of the securities laws to the SEC.
- Whistleblower provisions apply to conduct prior to enactment of Dodd-Frank if the “whistleblowing” occurs after July 21, 2010.
- Need not be an employee or even have first-hand knowledge.
- Need not have experienced any retaliation or negative employment consequences.
- Can be anonymous at reporting stage if represented by counsel.
- Excludes regulators, DOJ, PCAOB, self-regulatory bodies, attorneys, auditors, law enforcement and individuals *convicted* based on facts that are the subject of the covered action and others per SEC rules.

# Prohibited Retaliation Conduct

- No employer may discharge, demote, suspend, threaten, harass, directly or indirectly, or in any other manner discriminate against, a whistleblower in the terms and conditions of employment because of any lawful act done by the whistleblower
  - › in providing information to the SEC;
  - › in testifying, assisting in or initiating an investigation or action; or
  - › in disclosing information required to be disclosed or for protected disclosures under SOX or any other securities law, rule or regulation.
- Anti-retaliation applies whether or not whistleblower qualifies for an award

# Who Must Comply? What Violations Qualify?

- Anyone subject to the securities laws
  - › Publicly-traded companies (including foreign companies to the extent their shares are listed on a U.S. exchange)
  - › Subsidiaries of publicly-traded companies where acting as an agent of the parent
  - › Registered investment advisers, investment companies and others subject to SEC or CFTC regulation
  - › Individual employees and officers of the subject company
  - › Private companies to the extent they must comply with securities laws, e.g., private offering of securities subject to SEC enforcement under antifraud provisions
- What violations create whistleblower claims?
  - › Broader than under SOX and includes at least:
  - › '33 Act, '34 Act, Advisers Act, '40 Act
  - › The FCPA



# What Incentive?

- On December 15, 2008, the SEC announced a \$1.6 billion settlement with Siemens AG “for bribing government officials around the world to obtain business.”
- SEC notes that its portion of the Siemens settlement — \$350 million in disgorgement — is by far the largest settlement amount ever obtained by the SEC under the Foreign Corrupt Practices Act (FCPA).
- If you were the whistleblower, you could have obtained between \$160 - \$480 million.

# Potential Damages for Retaliation

- Double back pay
- Reinstatement
- Attorney's fees
- Costs

# Financial Incentives – Awards to Whistleblowers

- Awards to be assessed and paid to whistleblowers from SEC disgorgement fund.
- To be eligible, whistleblower must:
  - › Voluntarily (before SEC requests information)
  - › provide original information to SEC (independent knowledge or analysis)
  - › that leads to the successful enforcement by the SEC of federal court or administrative action, or a related action
    - Can also include enforcement by DOJ, state regulatory authorities, foreign authorities and self-regulatory organizations where SEC refers information
  - › in which the SEC obtains monetary sanctions totaling more than \$1 million
- Proposed SEC regulations provide clarification and rules for eligibility, exclusions, reporting and award determinations, as well as an attempt to encourage use of internal compliance programs.

# PROPOSED SEC IMPLEMENTING REGULATIONS

# Proposed SEC Regulations

- Released November 3, 2010.  
<http://www.sec.gov/news/press/2010/2010-213.htm>
- Comments due December 17, 2010.
- SEC has mandated April 2011 as time to finalize and implement regulations.

# Interplay with Internal Compliance Programs

- **SEC struggling with interplay with effective internal compliance programs.**
  - › Regulations expressly identify potential of monetary incentives to whistleblowers to “reduce the effectiveness of a company’s existing compliance, legal, audit and similar internal processes.”
  - › SEC attempting “*not to discourage* whistleblowers who work for companies that have robust compliance programs to first report the violation to appropriate company personnel.”
  - › SEC has solicited comments regarding how to implement whistleblower provisions without undermining internal compliance programs.

# Interplay with Internal Compliance Programs (cont'd): Efforts to Support Effective Compliance Programs

- **Whistleblowers incentivized to report internally first.** SEC will consider higher percentage awards for whistleblowers who first report the violation through compliance program. Proposed Rule 21F-6 (Commentary only).
  - › Whistleblowers only “encouraged,” not required, to report internally first – will not be “penalized” for failing to report internally for fear of retaliation.
  - › Where whistleblower bypasses internal reporting, SEC may inform company to allow it to conduct its own internal investigation first.
  - › Because thorough internal investigation followed by cooperation with SEC should result in greatly reduced punishment, financial incentive of whistleblower not aligned with robust compliance program.
- **Gives companies a chance to investigate the problem themselves, but very quickly.** If whistleblower submits information to internal compliance, then submits same information to the SEC within 90 days, the SEC will consider the whistleblower’s submission to be effective as of the date that the information was first reported internally. Proposed Rule 21F-4(b)(7).

# SEC's Proposed Regulations Apply Broadly

- **Anti-retaliation provisions apply broadly:** anti-retaliation provisions apply to all whistleblowers, regardless of whether the SEC ultimately finds that violation of the securities laws has occurred, and regardless of whether the whistleblower satisfies all the conditions necessary to qualify for a monetary award. Proposed Rule 21F-2.
- **Non-employees can be whistleblowers:** whistleblowers can collect on information conveyed to them by third parties. Direct, first-hand knowledge of a securities law violation is not necessary to recover an award. Proposed Rule 21-F(4)(b)(ii).



# Who Cannot Recover Awards?

## ■ Attorneys and accountants

- › Attorneys not eligible based on any information they obtain as a result of representing clients, regardless of whether the information covered by attorney-client privilege. Proposed Rule 21-F(4)(i).
  - Exception were attorney permitted to disclose privileged information under State bar ethics rules – *i.e.*, crime-fraud exception.
- › Accountants not eligible based on information obtained as a result of an audit required by the securities laws. Proposed Rule 21F-4(b)(4)(iii).

## ■ Internal compliance officers

- › No one with legal, compliance, audit, supervisory, or governance responsibilities for an entity may recover an award based on information received with a “reasonable expectation that the person would take appropriate steps to cause the entity to respond to the violation.” Proposed Rule 21F-4(b)(4)(iv).
- › However, these individuals *may* submit information to the SEC and recover awards if the entity does not disclose the information to the Commission within a “reasonable time” or if the entity proceeds in “bad faith.” Proposed Rule 21F-4(b)(iv).

# Culpable Whistleblowers

- **Individuals convicted of related crime.** No award will be made where individual is convicted of a crime based on the same facts that form the basis of the disclosures. Proposed Rule 21F-8(b)(3).
- **Individuals who supervised misconduct.** No award will be made where individual directed, planned or initiated the conduct that forms the basis of the disclosure. Proposed Rule 21F-15.
- **No amnesty for whistleblowers.** No amnesty to individuals who provide information to the SEC, and enforcement actions *may* still be brought against individuals who submit information but are wrongdoers themselves. Proposed Rule 21F-14.

# WHAT CAN YOU DO TO BE PREPARED ON THE COMPLIANCE SIDE?

# Action Items

- Foster a culture of compliance - education and monitoring.
- Develop/review policies and compliance systems to ensure that they encourage utilization of internal reporting systems.
  - › Are policies well advertised?
  - › Can employees easily submit their complaints?
  - › Is training easily accessible?
- Consider offering incentives for utilization of internal reporting systems.
- Ensure strong anti-retaliation policies are in place and enforced with tone from the top.

# WHAT TO DO WHEN THE WHISTLE BLOWS?

# Whistleblower Community Is Ready To File Complaints

## Business

### Whistleblowers rise to the FinReg bait

By KARA WHITEHOUSE

Wall Street's FINRA would not have an extra set of eyes on its back, but it is now a magnet for whistleblowers. The new regulator's rules, which take effect in 2010, will create a new set of eyes on its back, but it is now a magnet for whistleblowers. The new regulator's rules, which take effect in 2010, will create a new set of eyes on its back, but it is now a magnet for whistleblowers.

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## Business

# GET SNITCH QUICK

### 'Wall Street' stirs whistleblower outreach idea

**EXCLUSIVE** Informants wanted

By KARA WHITEHOUSE

Wall Street's FINRA would not have an extra set of eyes on its back, but it is now a magnet for whistleblowers. The new regulator's rules, which take effect in 2010, will create a new set of eyes on its back, but it is now a magnet for whistleblowers.



Michael Douglas (left) and Tina Lillard (right) are a source from 'Wall Street: Money Never Sleeps'.

The lawyer's clients all

A preview will be shown today at the Dogland theater in Midtown, and the movie opens nationwide on Friday.

# HEDGE HEADACHE

## Whistleblower stirring trouble for Plainfield

**EXCLUSIVE** House of cards

By KARA WHITEHOUSE

Mrs. Hobson has an exclusive look at the hedge fund industry, which she says is a house of cards. She says the industry is a house of cards, and she says she has an exclusive look at the hedge fund industry.



SEC Head Mary Schapiro

Plainfield's about \$100 million in assets, which is a small fraction of the total assets of the hedge fund industry.

# Larger Bounties Spur Surge in Fraud Tips

By Jessica Hogue and Paul J. Rosenthal

WASHINGTON—New awards for informants who help the Securities and Exchange Commission uncover fraud are already prompting a surge in tips, the agency says.

of working through normal corporate channels and letting the company report any issues itself, said William Jordan, a corporate defense attorney at Atlanta law firm Alston & Bird LLP.

"It adds a level of inefficiency, and hyperlegalism to the way you'd want an ethical company

trading cases. Only six people, actually get the awards between them, they received just over \$1 million.

Lawyers said informants had less incentive under the old system to come to the SEC because the agency wasn't obligated to pay anything for tips that

# Working with the Whistleblower

- Ensure that the company works proactively with the “whistleblower” to ensure that he or she feels heard and respected;
- Encourage the employee to put his/her concerns into writing;
- Advise the employee that you will be back in touch after the Company has had an opportunity to investigate his/her claims;
- Do not let the complainant dictate how the investigation will proceed;
- Assure the employee that the Company will not retaliate against employees for making good faith complaints.

# Conducting the Investigation – Developing a Strategy

- Process and timing matters when conducting internal investigations.
  - › Work with counsel to evaluate self-reporting pros and cons as expeditiously as possible.
  - › In many instances, the SEC may give companies an opportunity to investigate whistleblower complaints internally and report back to the SEC with their findings.
- Protect the attorney/client privilege.
- Develop a strategy with respect to the amount of information about the allegations that will be disclosed in the context of the interviews -
  - keep in mind that individuals who learn of that information may become whistleblowers themselves, as long as they do not obtain the information in the course of their legal, compliance, audit, supervisory, or governance responsibilities.



# Finalizing the Investigation -- Assuring No Retaliation

- Participants in the investigation should be reminded of the Company's no retaliation policy to the extent applicable;
- HR should be mindful of any "performance issues" that develop with respect to the complainant in the time frame after a complaint has been made — where appropriate issues have been identified, the Company should document them carefully and ensure participation in the process by neutral parties.

## QUESTIONS?



# Thank you for your time

Please do not hesitate to contact us should you have any questions.

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