

Rulemaking Commenters Debate the SEC's Proposed Changes to Its Whistleblower Program

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Securities Litigation and Enforcement

Over 3,000 commenters submitted letters to the Securities and Exchange Commission ("SEC") concerning the agency's recently proposed amendments to its whistleblower rules.¹ This response reflects the perceived importance of the SEC's proposal to companies and employees.

The most controversial of the proposed amendments would allow the SEC discretion to decrease the size of an award if it determines that the award would otherwise be too large to advance the goals of the whistleblower program.² Under current rules, if a whistleblower qualifies for an award, the SEC determines the size of the award by considering a number of specified factors that can increase or decrease the award amount within the range of 10 to 30 percent of the monetary sanctions recovered.³ To decrease the amount of an award, the SEC can consider only the culpability of the whistleblower; whether the whistleblower unreasonably delayed reporting the misconduct to the SEC; and whether the whistleblower interfered with the company's internal compliance and reporting systems.⁴

The SEC has taken the position that the existing rules give it no discretion to take an award's size into account when determining how much money to give a whistleblower. This approach has resulted in several awards that are so large that they present the question whether the SEC's whistleblower program has made good use of taxpayer dollars. For example, the SEC recently awarded \$54 million to two whistleblowers⁵ and \$83 million to three others.⁶ Indeed, without a change in the SEC's approach, awards based on the largest SEC and Department of Justice settlements could reach into the hundreds of millions of dollars. Seeing the possibility of grossly excessive awards in the future, the SEC has proposed giving itself discretion to

¹ Comments on Proposed Rule: Amendments to the Commission's Whistleblower Program Rules, Release No. 34-83557; File No. S7-16-18, <https://www.sec.gov/comments/s7-16-18/s71618.htm>.

² Proposed Rule Amendments, "Whistleblower Program Rules," SEC Release No. 34-83557 (Jun. 28, 2018), at 40-56, available at <https://www.sec.gov/rules/proposed/2018/34-83557.pdf>.

³ *Id.* at 41.

⁴ *Id.*

⁵ SEC Press Release, *SEC Awards More Than \$54 Million to Two Whistleblowers* (Sept. 6, 2018), <https://www.sec.gov/news/press-release/2018-179>.

⁶ Proposed Whistleblower Program Rule Amendments, *supra*, at 12 n. 9.

decrease awards in cases involving monetary sanctions exceeding \$100 million, when a single whistleblower would receive more than \$30 million.⁷

The overwhelming majority of comments were in form letters supporting the position of the National Whistleblower Center ("NWC"), which opposed what it called a "cap" on awards.⁸ The NWC argued that such a cap would deter well-compensated insiders at large financial institutions from coming forward with evidence of violations.⁹ The NWC also cited its own analysis concluding that "larger rewards generate significantly greater publicity which both incentivizes perspective whistleblowers and deters criminal activity/securities fraud."¹⁰ Senator Charles Grassley (R-Iowa), the Chairman of the Senate Committee on the Judiciary, submitted a comment letter contending that the SEC had failed to point "to any compelling reason to veer from award levels that are working and that are comparable to other federal award programs."¹¹ Chairman Grassley cited a 2013 SEC Inspector General report finding that SEC whistleblower awards were calibrated appropriately, but without considering the SEC's largest awards, which were granted after the report was written.

In contrast, the Securities Industry and Financial Markets Association ("SIFMA"), a securities industry trade association, supported giving the SEC discretion to reduce large awards. According to SIFMA, recoveries over \$30 million provide "little marginal incentive" for whistleblowers to come forward, especially when the amount of a "potential penalty is virtually impossible for a whistleblower to predict in the first place."¹²

Another significant SEC proposal is to allow whistleblower awards when the SEC or other governmental agencies, such as DOJ in criminal cases, enter into deferred prosecution agreements ("DPAs") or non-prosecution agreements ("NPAs") that include monetary remedies.¹³ Currently, whistleblowers are denied an award when information they provide leads only to a DPA or an NPA rather than a civil action or administrative proceeding. Positing that DPAs and NPAs accomplish the same goals as more formal enforcement actions, the SEC seeks to treat them the same under its whistleblower program.¹⁴ This change, if adopted, would likely lead to some very large whistleblower awards based on criminal DPAs or NPAs involving substantial monetary sanctions.

The U.S. Chamber of Commerce and SIFMA took opposing views on this proposal. The Chamber, representing a broad base of U.S. companies, criticized it as outside the agency's

⁷ *Id.* at 44.

⁸ Letter Type A, <https://www.sec.gov/comments/s7-16-18/s71618-typea.htm>; Letter Type B, <https://www.sec.gov/comments/s7-16-18/s71618-typeb.htm>.

⁹ National Whistleblower Center (NWC) Comment Letter, Sept., 2018, at 2, <https://www.sec.gov/comments/s7-16-18/s71618-4371152-175237.pdf>.

¹⁰ NWC Comment Letter, *supra*, at 3; see also Comment Letter of Markopolos Research LLC, Sept. 14, 2018, at 4, <https://www.sec.gov/comments/s7-16-18/s71618-4351184-173304.pdf>.

¹¹ Comment Letter of Grassley, Sen. Charles E., U.S. Senate Committee on the Judiciary, Sept. 18, 2018, at 2, <https://www.sec.gov/comments/s7-16-18/s71618-4373264-175545.pdf>.

¹² SIFMA Comment Letter, Sept. 18, 2018, at 4, <https://www.sec.gov/comments/s7-16-18/s71618-4373269-175549.pdf>.

¹³ *Id.* at 16-22.

¹⁴ *Id.* at 19.

authority under the Dodd-Frank Act.¹⁵ SIFMA, on the other hand, endorsed the proposal, arguing that it would "fairly balance the important goals of both rewarding whistleblowers, and also encouraging companies to adopt effective compliance programs and to cooperate fully during investigations in the hope of obtaining a DPA or NPA."¹⁶

The SEC will review the public's comments when drafting the final rule amendments, and has not announced a date for their issuance. As is evident from the public debate concerning the merit of the proposals, the final result is likely to have significant consequences for companies and potential whistleblowers, and may result in protracted litigation over their legality.

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¹⁵ Comment Letter of U.S. Chamber of Commerce, Center for Capital Markets Competitiveness, Sept. 18, 2018, at 5, <https://www.sec.gov/comments/s7-16-18/s71618-4370851-175223.pdf>.

¹⁶ SIFMA Comment Letter, *supra*, at 4.