



## SEC PROPOSES RULES TO IMPLEMENT WHISTLEBLOWER INCENTIVES & PROTECTION PROGRAM

On November 3, 2010, the Securities and Exchange Commission (the “SEC”) issued [proposed rules](#) to implement the whistleblower provisions added to Section 21F of the Securities Exchange Act of 1934 by the Dodd-Frank Wall Street Reform and Consumer Protection Act enacted on July 21, 2010 (the “Dodd-Frank Act”). Under the proposed rules, the SEC will pay awards to eligible *whistleblowers* who *voluntarily* provide the SEC with *original information* leading to the *successful enforcement* by the SEC of a federal court or administrative action in which the SEC obtains *monetary sanctions* in excess of \$1 million. If all of these criteria are met, a whistleblower could be eligible for an award ranging between 10 and 30 percent of the amount of monetary sanctions obtained by the SEC. Proposed Section 21F provides a complete and self-contained set of rules relating to the whistleblower program, as more fully described below.

### **Award Eligibility**

***Whistleblower.*** The proposed rules define a whistleblower as a natural person (and not an entity), whether acting alone or with others, who provides information to the SEC regarding potential violations of securities laws.

***Voluntary.*** Under proposed Rule 21F-4(a), information must be submitted voluntarily, meaning the information is provided prior to any whistleblower receiving a formal or informal request by the SEC or other regulatory body. Information will not be deemed to be voluntarily submitted if a preexisting legal or contractual duty to report the violations existed. The proposed rules also make clear that if a request or inquiry is directed at an employer, information provided by any of its employees will not be deemed voluntary.

***Original Information.*** Original information is derived from a whistleblower’s “independent knowledge” or “independent analysis” that is unknown to the SEC. “Independent knowledge” is defined as information not derived from publicly available sources, while “independent analysis” means a person’s analysis done alone or in combination with others which may be based on publicly available information. The proposed rules expressly exclude certain classes of information as deriving from an individual’s “independent knowledge” or “independent analysis,” including most information that could be provided by attorneys and accountants retained by an issuer. Additionally, information obtained by persons through an issuer’s internal compliance programs or who are in positions of responsibility for an issuer will not be considered to be derived from independent knowledge or independent analysis to the extent such information is reported to those persons with an expectation that they will take appropriate steps to respond. However, this exclusion does not apply to information disclosed by a person who cooperates in an internal investigation which does not result in the issuer’s disclosure to the SEC or in situations where the issuer otherwise acts in bad faith.

***Successful Enforcement.*** A whistleblower’s information will be deemed to have “led to successful enforcement” where (i) the information caused the SEC to open a new investigation, reopen a closed investigation or inquiry concerning new conduct not part of an existing investigation and the information significantly contributes to the success of the action, or



(ii) the information was related to conduct already under investigation but was essential to the success of the action and would not otherwise have been obtained (the SEC notes, however, that awards under standard (ii) would be rare).

*Monetary Sanctions.* To qualify for an award, monetary sanctions must exceed \$1 million. Monetary sanctions include any money, including penalties, disgorgement and interest, ordered to be paid or deposited into a fund. Proposed Rule 21-F-15 provides that in the event a whistleblower is ordered to pay monetary sanctions in connection with an enforcement action, or where an entity whose liability is based substantially on the whistleblower's conduct, the SEC will exclude such amounts from the determination of whether the \$1 million threshold is met.

### **Amount of Award**

If a person meets all of the requirements relating to qualification of an award, the proposed rules authorize the SEC to award the whistleblower an amount that is not less than 10 percent and not greater than 30 percent of the monetary sanctions collected in the action. For purposes of determining this dollar threshold, an "action" includes all defendants or respondents, and all claims, that are brought within that proceeding without regard to which specific defendants or respondents, or which specific claims, were included as a result of the whistleblower's information. Conversely, sanctions imposed in separate judicial or administrative actions will not be aggregated for purposes of determining whether the \$1 million threshold is met, even if multiple actions arise out of a single investigation.

### **Information Submission Procedure**

The information submission procedure under the proposed rules sets out a two-step process. First, a whistleblower must submit information to the SEC by completing a Form TCR (Tip, Complaint, or Referral) or making an online report through the SEC's Electronic Data Collection System. Second, a Form WB-DEC (Declaration Concerning Original Information Provided Subject to Section 21F of the Securities and Exchange Act of 1934), whereby a whistleblower swears, under penalty of perjury, that his allegations are correct and true, must be submitted. Submission of Form WB-DEC could be made anonymously if accompanied by a separate Form WB-DEC filed and certified by the anonymous whistleblower's attorney. Proposed Rule 21F also sets forth procedures for appealing an SEC decision with respect to a claim.

### **Policy Concerns**

In the proposing release, the SEC identifies several policy issue concerns in crafting the proposed whistleblower rules. Specifically, creating a monetary incentive to report violations could potentially reduce the effectiveness of existing internal compliance programs and lead to increased false tipping. To address these concerns, the proposed rules attempt to discourage employees from bypassing internal compliance programs by treating employees as whistleblowers as of the date the employee first reports the information internally, provided the same information is reported to the SEC within 90 days. The proposed rules also permit the SEC to consider increased awards for whistleblowers first reporting the information in accordance with an internal compliance program. In seeking to reduce possible false tips, the SEC has



required the Form WB-DEC be signed under penalty of perjury, and that an anonymous whistleblower must be represented by counsel who must certify as to the whistleblower's identity.

### **Comment Period and Rulemaking Timeline**

The SEC will accept comments on the proposed rules through December 17, 2010, and the deadline for adopting the final rules is April 17, 2011.

—[\*Allen E. Frederic, III and Charles E. Reeves, Jr.\*](#)



*Remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues, contact:*

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