

# Regulatory and Enforcement Alert

## Key Takeaways From the SEC's Recent Amendments to Its Whistleblower Program Rules

October 5, 2020

On September 23, 2020, the Securities and Exchange Commission voted to amend its rules governing the Commission's whistleblower program. The amendments, characterized principally as clarifications rather than material alterations to the existing rules, purportedly aim "to increase efficiencies around the review and processing of whistleblower award claims, and provide the Commission with additional tools to appropriately reward meritorious whistleblowers for their efforts and contributions to a successful matter."

The SEC's whistleblower rules, as originally promulgated under Dodd-Frank, provide for payouts to a whistleblower of not less than 10% and not more than 30% of a monetary sanction collected by the SEC in an enforcement action. Within these requirements, the statute provides that the final award amount is subject to the SEC's discretion, and is to be guided by a number of factors, including the significance of the information, the degree of assistance provided by the whistleblower, the SEC's interest in deterring violations of the securities laws and "such additional relevant factors" that the SEC may establish by rule or regulation.

While reaffirming the SEC's position that it is (and always has been) authorized under the whistleblower statute to exercise its discretion in deciding the amount of a whistleblower award based on the factors set forth in Rule 21F-6(a) and (b),<sup>1</sup> the amendments introduce a presumption that the amount awarded will be at the 30% statutory maximum—assuming the award is \$5 million or less (which captures the majority of whistleblower awards), and there are no negative factors that counsel against the payout. Along with the adoption of the amendments, the SEC released guidance requiring that a whistleblowers' provision of "original information" justifying an award must include "independent analysis" that provides "evaluation, assessment or insight" beyond what would be reasonably apparent to the SEC from publicly available information.

The recent amendments do not include, as originally proposed, a rule allowing for downward adjustments in whistleblower awards in cases with monetary sanctions exceeding \$100 million. The Commission determined that such a rule was unnecessary in light of its view that it *already* had the power to reduce an award on the basis of its size. Commissioner Allison Herren Lee, joined by her fellow Democratic Commissioner Caroline Crenshaw,

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<sup>1</sup> These factors include those that may increase the amount of the award, such as the significance of the information provided by the whistleblower, the assistance provided by the whistleblower, the SEC's interest in deterring violations of the securities laws, and whether the whistleblower participated in internal compliance systems, as well as factors that may decrease the amount of the award, such as culpability, unreasonable reporting delay, and interference with internal compliance and reporting systems. See 17 C.F.R. § 240.21F-6.

dissented “because of the treatment given to the central issue of the Commission’s discretion to consider the dollar amount of an award in making award determinations.” Commissioner Lee worried that the exercise of such discretion could result in a lowering of payouts, with the result that potential whistleblowers might not be sufficiently incentivized to report their concerns to the government. Commissioner Crenshaw expressed additional concern that the interpretive guidance requiring whistleblowers to provide information amounting to “independent analysis” went too far in limiting the type of information that would allow a whistleblower to qualify for an award.

The differing views within the Commission beg the fundamental question: Is there a point at which size of an award *doesn’t* matter? Once an award reaches into the many millions, is an even higher payout necessary to incentivize that whistleblower (or the next one) to come forward and expose misconduct?

Statistics from this year alone reflect that whistleblowers are producing results for the agency, and that the award program is being used by a growing class of sophisticated and knowledgeable whistleblowers. *See* Press Release, SEC Whistleblower Program Ends Record-Setting Fiscal Year With Four Additional Awards (Sept. 30, 2020), <https://www.sec.gov/news/press-release/2020-240> (“This year the SEC has made a record 39 individual awards of approximately \$175 million, more than in any prior fiscal year.”). The program now has deep roots—roots that have grown stronger under a Republican administration—and the SEC is seeing results across a broad ambit of the financial markets, with the ranks of whistleblowers consisting of both insiders *and* savvy external observers. And while it remains unclear which party will have stewardship of the SEC’s whistleblower program in the next Administration, it seems certain that the program will remain a key element of the SEC’s enforcement efforts going forward. If it is the Democrats, however, one would expect the pace and size of these awards will rise even further, given two Democratic Commissioners already on record expressing discomfort with limits on the type of information that may be rewarded and on the size of awards.

As a result, it is critically important that issuers and all firms registered with the Commission take the time to set up the appropriate channels for whistleblowers to raise information internally, and to cultivate an environment that encourages them to do so, in the hopes of avoiding lengthy (and expensive) government investigations and enforcement actions. The bottom line is that whistleblowers will continue to find a hospitable regulator at the SEC, with staff well-versed in working with whistleblowers and their counsel; to that end, issuers and registrants should redouble their efforts to create a healthy internal environment for whistleblowers to step forward and be heard, rather than having whistleblowers express their concerns through the SEC enforcement process.

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