

## SEC Issues First Award Under New Whistleblower Program

The United States Securities and Exchange Commission (SEC) recently issued the first “bounty payment” under its one-year-old whistleblower program. While the SEC has protected the identity of the whistleblower by keeping secret many of the details, the existence of tangible rewards for those who provide useful information to the SEC has been widely publicized.

### Background

The SEC’s Whistleblower Program, established by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, provides a monetary incentive for individuals who come forward to report possible violations of federal securities laws. Awards under the program are mandatory and can range from 10 to 30 percent of the money collected in the SEC enforcement action. In order to be eligible for an award under the Whistleblower Program, an individual must provide information that:

- Is original
- Is voluntarily, i.e., before SEC requests the information
- Is high-quality
- Is timely
- Leads to an SEC enforcement action in which more than \$1 million is recovered

To be “original,” information must be derived from independent knowledge or analysis, and not already known to the SEC or obtained from the news, legal representation, an audit engagement, internal compliance processes or by illegal means. The Whistleblower Program also contains provisions that prohibit retaliation by employers who discover a whistleblower’s identity, and provides a private cause of action in federal court for those individuals who believe they have suffered retaliatory action from their employers.

### First Whistleblower Award

On August 21, 2012, the SEC issued an award of \$50,000 to a whistleblower who helped “stop a multi-million dollar fraud” (See [SEC News Release 2012-162](#)). According to Robert Khuzami, Director of the SEC’s Division of Enforcement, “[h]ad this whistleblower not helped to uncover the full dimensions of the scheme, it is very likely that many more investors would have been victimized.” The SEC indicated that the \$50,000 award represents 30 percent of the amount collected in the enforcement action. The recipient of the award has chosen to remain anonymous, and the SEC has taken pains to protect that anonymity.

Additionally, the SEC announced that it had denied a claim from a second individual seeking an award in this matter because the information provided did not “lead to or significantly contribute to the SEC’s enforcement action,” as is required for an award.

### The Whistleblower Program and Internal Compliance Initiatives

One noteworthy and controversial feature of the Whistleblower Program is the absence of any requirement that individuals first report the information to their employers. A whistleblower can simply bypass internal compliance, report directly to the SEC and remain eligible for an award. This facet of the Whistleblower Program has generated a significant amount of debate. Corporations argued that the lack of an internal reporting requirement would effectively gut the very same internal reporting mechanisms and compliance programs set up in the wake of the Sarbanes-Oxley legislation. Moreover, direct reporting to the SEC could trigger an expensive and public investigation without first providing the company with a fair opportunity to investigate what may be a frivolous complaint. The SEC ultimately rejected these arguments, though it took the following actions to incentivize whistleblowers to report internally:

- Whistleblowers who first report internally are granted 120 days to report the same information to the SEC without losing their “place in line” for purposes of the SEC’s determination of whether the information provided was original.
- If a whistleblower’s internal complaint triggers an internal investigation by the company and the company then reports its findings to the SEC, the whistleblower will benefit from all the information provided by the company after its internal investigation.
- In determining the amount of the award, the SEC will consider whether and to what extent the whistleblower reported internally.

### Key Takeaways

- **Expect Awards to Be Issued on a Regular Basis**  
SEC officials have stated repeatedly that they have benefitted from the information whistleblowers have provided, and the recent award appears to confirm this claim. Sean McKessy, Chief of the SEC’s Whistleblower Office, stated in the previously mentioned [press release](#) that the SEC receives about eight tips a day. More importantly, the SEC has publicly stated that the quality and specificity of the information has improved dramatically since the start of the Program. According to Mr. McKessy, “[t]he fact that we made the first payment after just one year of operation shows that we are open for business and ready to pay people who bring us good, timely information.” Indeed, the timing of this first payment—only a year after the Whistleblower Program commenced—is unsurprising. According to the SEC’s Fiscal Year 2011 annual report, only 61 percent of SEC enforcement actions are filed within two years of an investigation’s commencement.
- **Expect Increased Internal and SEC Complaints**  
Whistleblower bounties are no longer hypothetical. The SEC has now paid, and will continue to pay, those who provide information that leads to enforcement actions against their employers and others. As a result, corporations can safely expect an increase in both internal and SEC complaints. Companies would be well advised to establish a meaningful and anonymous internal complaint reporting mechanism and to take seriously all internal complaints. Failure to respond quickly and appropriately, which will usually include an internal investigation, may prompt a whistleblower to call the SEC directly.

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