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CORPORATE WHISTLEBLOWING – KEY ISSUES IN RESPONDING TO POSSIBLE VIOLATIONS

Whistleblower provisions in the Sarbanes-Oxley and Dodd-Frank Acts have generated an explosion of tipster reports of corporate wrongdoing, payment of large bounty awards in some cases, and suits over alleged retaliation. Focusing on the SEC's whistleblower program, the authors examine the window of opportunity for internal investigation before the tipster goes to the Commission. They then turn to issues surrounding the coverage of the statutes and close with a discussion of some key points to consider in investigating tipster allegations.

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The need to detect and investigate reported allegations of wrongdoing within a corporation has long been a fact of corporate life. In the last 15 years, however, a combination of circumstances has contributed to an explosion of activity in this area. Among the contributing factors was Congress' passage of laws and related agency regulations encouraging and, in some cases, mandating that employees report suspected corporate misconduct; creating financial incentives for employees to do so; and prohibiting retaliation against those who report. For companies, understanding their obligations pursuant to this statutory regime and the unsettled issues still surrounding it is crucial both for purposes of complying with applicable law and responding appropriately to alleged wrongdoing. This article discusses certain significant whistleblowing provisions of the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley") and the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), as well as best practices for responding to tips where these statutes apply.

BACKGROUND

In response to numerous high-profile accounting scandals of the early 2000s, including Enron and

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WorldCom, Congress passed Sarbanes-Oxley in July 2002. At the time, President Bush characterized Sarbanes-Oxley as implementing "the most far-reaching reforms of American business practices since the time of Franklin Delano Roosevelt."[1] A key measure prohibits retaliation against whistleblowers who report certain suspected fraudulent activity to superiors or the federal government.[2] More specifically, Sarbanes-Oxley's anti-retaliation provision prohibits: (1) public companies (and their officers, employees, contractors, subcontractors, and agents) (2) from retaliating "against an employee . . . because of any lawful act done by the employee" to provide information or assistance, (3) "which the employee reasonably believes constitutes a violation of [18 U.S.C. §] 1341, 1343, 1344, or 1348, any rule or regulation of the [SEC], or any provision of Federal law relating to fraud against shareholders," (4) when the information or assistance is provided to a federal regulatory or law enforcement agency, any member or committee of Congress, or an employment supervisor.[3] An employee can only pursue a claim for retaliation under Sarbanes-Oxley, for which civil damages resulting from retaliation may be available, if he or she files a complaint with the Secretary of Labor within 180 days of the violation, or after the date on which the employee becomes aware of the violation.

In 2010, Congress passed Dodd-Frank in response to the global financial crisis. Under Dodd-Frank, a whistleblower is an individual, or two or more individuals (i.e., not a business organization) acting jointly who "provide…original information" to the SEC leading to "successful enforcement" (i.e., monetary sanctions exceeding $1 million) of a violation of the securities laws.[4] Dodd-Frank contains its own anti-retaliation provision, which bars retaliation against an employee who (1) provides information to the SEC; (2) initiates, testifies in, or assists in any investigation, or judicial or administrative action based on or related to the information; or (3) makes disclosures that are either required, or protected, by Sarbanes-Oxley or any other law, rule, or regulation subject to the jurisdiction of the SEC.[5]

Dodd-Frank also amended the Securities Exchange Act of 1934 by, among other things, adding a section that provides the possibility of significant monetary awards for those who "blow the whistle" on corporate misconduct and whose information leads to a successful SEC enforcement action. This bounty provision, which is backed by a $450 million investor protection fund, was designed to incentivize corporate whistleblowing and provides that in any action by the SEC resulting in monetary sanctions exceeding $1 million, the SEC "shall pay an award" in an amount between 10 – 30% of the monetary sanctions collected.[6] Dodd-Frank also provided, in contrast to Sarbanes-Oxley, a longer period for the whistleblower to assert a claim for retaliation (six years), permitted him or her to do so in federal court without having to pursue an administrative remedy in the first instance, and provided for the possibility of a greater recovery if the plaintiff is successful (i.e., two times the back pay otherwise owed to the individual, plus interest).[7]

Dodd-Frank also mandated the creation of the SEC's Office of the Whistleblower, which administers the bounty program and, among other things, is required to issue annual reports on the Whistleblower Office's activity.[8] The Annual Report for fiscal year 2011 disclosed that the SEC that year received 334 tips from whistleblowers. In the subsequent two fiscal years, that number increased to 3,001 and 3,238, respectively.[9] As

[1] *Sarbanes-Oxley Act of 2002*, SEC.GOV | FEDERAL SECURITIES LAWS, http://www.sec.gov/about/laws.shtml#sox2002 (last visited Oct. 28, 2014).

[2] As discussed below, the scope of this protection may go even further.

[3] 18 U.S.C. § 1514A(a).

[4] 15 U.S.C. § 78u-6(b).

[5] 15 U.S.C. § 78u-6(h)(1)(A).

[6] 15 U.S.C. § 78u-6(b).

[7] 15 U.S.C. § 78u-6(h)(1)(B) & (C).

[8] *See generally* 15 U.S.C. § 78u-6.

[9] All reports *available at* RESOURCES : SEC OFFICE OF THE WHISTLEBLOWER, http://www.sec.gov/about/offices/owb/owb-resources.shtml (last visited Oct. 28, 2014).

the investigations and enforcement actions derived from those tips have matured, the awards handed out to SEC whistleblowers have increased as well. Since inception, the SEC has made 14 awards in nine different cases. These awards have totaled over $46 million, though the bulk of that amount went to two whistleblowers. The SEC announced in October 2013 its second-largest award of over $14 million.[10] A 2014 award of over $30 million was the fourth paid to a tipster located outside of the United States. Sean McKessy, the Chief of the SEC's Office of the Whistleblower, has encouraged this international scope, stating that "[w]histleblowers from all over the world should feel…incentivized to come forward with credible information about potential violations of the U.S. securities laws."[11]

The SEC is far from the only federal agency with a whistleblower program. Among others, federal agencies including the Department of Justice, U.S. Commodity Futures Trading Commission, and Occupational Safety and Health Administration enforce a variety of whistleblower provisions designed to protect individuals who report alleged corporate wrongdoing to the government. The at-times overlapping regulatory coverage of similar conduct has created something akin to a regulatory "arms race." Multiple, competing bounty programs designed to incentivize whistleblowing has led to competition among regulators to "attract" tips.

For example, a whistleblower who provides information that leads to a successful prosecution under the False Claims Act ("FCA") can receive an award of up to 30% of the government's recovery.[12] Dodd-Frank similarly calls for an award of between 10-30% of the total amount collected. By contrast, the Financial Institutions Reform, Recovery, and Enforcement Act ("FIRREA"), 12 U.S.C. § 1811 et seq., which was passed in the wake of the 1980's savings and loan crisis and is enforced by the Department of Justice, caps all whistleblower awards at $1.6 million. In a September 2014 speech, then-Attorney General Eric Holder recognized that this $1.6 million cap may not be enough incentive to bring forward tipsters from the financial sector, calling that amount "a paltry sum in an industry in which, last year, the collective bonus pool rose above $26 billion."[13] In order to induce more individuals to come forward with information, Holder suggested aligning the FIRREA and the FCA's bounty provisions.

INVESTIGATING AND RESPONDING TO TIPSTER REPORTS

Given the significant monetary bounties potentially available, and the publicity surrounding the existence of incentives for individuals who come forward with information of alleged corporate misconduct, companies need to be prepared to respond appropriately and effectively when they receive a tip. Moreover, while any allegation of misconduct requires a serious response in proportion to the materiality and credibility of the information, there are certain unique considerations involved in responding to information covered by Sarbanes-Oxley or Dodd-Frank.

To be eligible for an award, the SEC requires that the whistleblower provide the SEC with "original information."[14] The existence of the Dodd-Frank bounty program potentially makes it more likely that an individual will report such information to the government, perhaps without reporting internally or before giving the company time to complete an inquiry into the matter and self-report. In order to encourage internal reporting without sacrificing eligibility for an award, the SEC provides internal whistleblowing incentives. For example, the SEC has provided for a 120-day "look-back period" for whistleblowers who first report internally.[15] Under this rule, if a whistleblower reports to the SEC within 120 days of reporting

[10] Press Release, Sec. Exch. Comm'n., SEC Awards More than $14 Million to Whistleblower (Oct. 1, 2013) (*available at* SEC.GOV, http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539854258#.VDxxt_ldWGc).

[11] Press Release, Sec. Exch. Comm'n., SEC Announces Largest-Ever Whistleblower Award (Sept. 22, 2014) (*available at* SEC.GOV, http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370543011290).

[12] In October 2014, four whistleblowers were granted a combined $3.9 million award (17% of a $23 million settlement) for reporting that Boeing defrauded taxpayers by intentionally overcharging the U.S. Air Force for maintenance work. *See* Joel Schectman, *Whistleblowers Win $3.9 Million in Boeing Case*, WALL ST. J., Oct. 13, 2014, 5:58 PM), http://blogs.wsj.com/riskandcompliance/2014/10/13/boeing-whistleblowers-win-3-9-million-in-false-claims-case/.

[13] Eric Holder, Attorney General, U.S. Department of Justice, Remarks on Financial Fraud Prosecutions at NYU School of Law (Sept. 17, 2014), (*available at* OPA | DEPARTMENT OF JUSTICE, http://www.justice.gov/opa/speech/attorney-general-holder-remarks-financial-fraud-prosecutions-nyu-school-law) (last visited Oct. 28, 2014).

[14] 17 C.F.R. § 240.21F-2(a)(2).

[15] Implementation of the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934, Exch. Act Rel. No. 34-64545, 76 Fed. Reg. 34300, 34365 (June 13, 2011).

internally to the company, the whistleblower will receive 'credit' for reporting the information as of the date of the internal report.[16] This allows the whistleblower to maintain priority status over any subsequent whistleblowers. On top of the 120-day "look-back" rule, the SEC has also said that it will consider whether a whistleblower first reported the information internally before reporting to the SEC when it is considering whether the whistleblower should receive an award and, if so, where the award should fall in the 10 – 30% discretionary range. According to the SEC, "a whistleblower's voluntary participation in an entity's internal compliance and reporting systems is a factor that can increase the amount of an award, and … a whistleblower's interference with internal compliance and reporting is a factor that can decrease the amount of an award."[17] Finally, the SEC has announced that if a whistleblower's internal report causes the company to conduct an internal investigation, the SEC will base the amount of the whistleblower's award on the entirety of the conduct that is uncovered by the investigation, not just the conduct that the whistleblower reported.[18] Given those incentives, a company faced with an internal report will probably have some period of time – at most a 120-day window – in which to respond before the whistleblower "reports out" to the SEC. Of course, nothing guarantees that a whistleblower will wait as long as 120 days before reporting to the government. This timing is crucial, and companies responding to internal allegations of misconduct should bear it in mind when considering how to address the allegations.

Further complicating matters is the reality that at times it has been the case that a whistleblower is a person involved in the reported misconduct who is seeking to get in front of the problem and/or has improperly taken or used company documents in developing the information in question. The permissible responses on the part of the company are circumscribed if Sarbanes-Oxley or Dodd-Frank applies, putting aside the additional considerations that may counsel against taking action against a wrongdoer who also is a whistleblower, even if legally permissible. And, the universe of people covered by these statutes also was greatly expanded when the Supreme Court determined in 2014 that individuals at private companies who work for public companies are subject to the Sarbanes-Oxley whistleblower provisions.[19] (Dodd-Frank on its face applies to such private company employees.)[20]

In short, companies receiving information concerning alleged misconduct have a very short window, if any, to investigate and respond before a tipster reports directly to regulators. Retaining control of the timing and content of disclosure to the government, as well as having the opportunity voluntarily to disclose, obviously could have significant implications for the remedies demanded by the government in connection with an ultimate resolution of the matter.[21] The range of responses by the company to a whistleblower who is implicated in wrongdoing also is impacted by whether these provisions apply. Adding to all these concerns is the prevailing uncertainty, discussed below, over certain aspects of the Sarbanes-Oxley and Dodd-Frank whistleblower provisions.

ISSUES REGARDING COVERAGE OF THE WHISTLEBLOWER PROVISIONS

First, the Sarbanes-Oxley anti-retaliation provisions apply to individuals who provide information about "a violation of section 1341, 1343, 1344, or 1348, any rule or regulation of the Securities and Exchange Commission, or any provision of Federal law relating to fraud against shareholders."[22] While Sarbanes-Oxley clearly bars retaliation against someone providing information relating to fraud against shareholders, not all courts are in agreement as to whether Sarbanes-Oxley also applies to information about violations of sections 1341 (frauds and swindles), 1343 (wire, radio, or television fraud), 1344 (bank fraud), or 1348 (securities and commodities fraud) unrelated to shareholder fraud. Some courts have interpreted this statute to apply to information that *either* relates to fraud against shareholders *or* falls under one of the enumerated

[16] 17 C.F.R. § 240.21F-4(b)(7).

[17] Press Release, Sec. Exch. Comm'n., SEC Adopts Rules to Establish Whistleblower Program (May 25, 2011) (*available at* SEC.GOV, http://www.sec.gov/news/press/2011/2011-116.htm).

[18] 17 C.F.R. § 240.21F-4(c)(3).

[19] *See Lawson v. FMR LLC*, 134 S. Ct. 1158 (2014).

[20] 15 U.S.C. § 78u-6(a)(6).

[21] For example, in a recent SEC settlement announcement the Director of the SEC's Department of Enforcement emphasized that the company self-reported the issue, "remediated the issues quickly, and cooperated in [the SEC's] investigation." The penalty that was imposed "reflect[ed] credit for that cooperation." Press Release, Sec. Exch. Comm'n., SEC Charges Bank of America with Securities Laws Violations in Connection With Regulatory Capital Overstatements (Sept. 29, 2014) (*available at* SEC.GOV, http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370543065483#.VE1hJfnF-Gc).

[22] 18 U.S.C. § 1514A(a)(1).

statutes. These courts reason that an interpretation that requires each violation to relate to fraud against shareholders would render the enumeration of specific statutes superfluous.[23] Other courts, examining the text, legislative history, and purpose of Sarbanes-Oxley, have interpreted this provision to require that all information relate to "fraud against shareholders" in order to fall under the Sarbanes-Oxley anti-retaliation provision.[24]

An interpretation of Sarbanes-Oxley that provides whistleblower protection to individuals reporting on violations that are unrelated to shareholder fraud expands the universe of activity covered by the anti-retaliation provision. On the other hand, providing information unrelated to enforcement of the securities laws does not entitle a person to an award under Dodd-Frank's bounty program, which reduces the incentive for a person to report in the first place.

Second, the Sarbanes-Oxley anti-retaliation provision is not limited to public company employees. The provision provides that "[n]o [public] company…or any officer, employee, contractor, subcontractor, or agent of [that public] company…may [retaliate] against *an employee*."[25] In 2014, in *Lawson v. FMR LLC,*[26] the Supreme Court held that employees of private company contractors engaged by public companies are covered by the anti-retaliation provision.[27] In so holding, the Court relied not only on a textual analysis of the provision, but the legislative purpose behind Sarbanes-Oxley. Justice Ginsburg, writing for the plurality, stated that "Congress installed whistleblower protection in the Sarbanes-Oxley Act as one means to ward off another Enron debacle."[28] According to the Court, this purpose was served by interpreting the anti-retaliation provision as applying to private companies' employees who blow the whistle on public companies with whom they have contracted to do work. *Lawson* significantly expanded the scope of the anti-retaliation provision of Sarbanes-Oxley, such that it now covers any private company in the course of its work for a public company. Included within its ambit presumably are advisors, such as accounting firms, providers of goods and other services, and many other types of private entities.[29]

Third, Sarbanes-Oxley's anti-retaliation protection applies equally to tipsters who report internally and externally. However, there is a split among federal courts over whether Dodd-Frank's whistleblower provisions apply to internal as well as external reporting. Dodd-Frank's protection applies to three categories of "whistleblowers": those who (1) provide information to the SEC; (2) assist in an SEC investigation; or (3) make "disclosures that are required or protected" under Sarbanes-Oxley, the securities laws, and other SEC regulations."[30] "Whistleblowers" under the Act are defined as "any individual who provides, or two or more individuals acting jointly who provide, information relating to a violation of the securities laws to the Commission in a manner established, by rule or regulation, by the Commission."[31] In *Asadi v. G.E.*

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[23] *See, e.g. Lockheed Martin Corp. v. Admin. Rev. Bd.,* 717 F.3d 1121, 1130-31 (10th Cir. 2013) ("[A] claimant who reports violations of 18 U.S.C. § § 1341, 1343, 1344, or 1348 need not also establish such violations relate to fraud against shareholders to be protected from retaliation under the Act."); *Reyna v. ConAgra Foods, Inc.*, 506 F. Supp. 2d 1363, 1382 (M.D. Ga. 2007) ("The court rejects Defendants' interpretation that the last phrase of the provision, 'relating to fraud against shareholders,' modifies each of the preceding phrases in the provision."); *O'Mahony v. Accenture Ltd*, 537 F.Supp.2d 506, 516-18 (S.D.N.Y. 2008) (same principle).

[24] *See, e.g., Livingston v. Wyeth Inc.*, No. 1:30CV00919, 2006 WL 2129794 at *10 (M.D.N.C. July 28, 2006), *aff'd*, 520 F.3d 344 (4th Cir. 2008) ("To be protected under Sarbanes-Oxley, an employee's disclosures must be related to illegal activity that, at its core, involves shareholder fraud."); *Bishop v. PCS Admin. (USA), Inc.*, No. 05 C 5683, 2006 WL 1460032, at *9 (N.D. Ill. May 23, 2006) ("The phrase 'relating to fraud against shareholders' in this provision must be read as modifying each item in the series."); *Fraser v. Fiduciary Trust Co. Int'l*, 417 F. Supp. 2d 310, 322 (S.D.N.Y. 2006) (same).

[25] 18 U.S.C. § 1514A (emphasis added).

[26] 134 S. Ct. 1158 (2014).

[27] "Company" under the Anti-Retaliation Provision is defined as companies "with a class of securities registered under section 12 of the Securities Exchange Act of 1934 or that is required to file reports under section 15(d) of the Securities Exchange Act of 1934." 18 U.S.C. § 1514A(a).

[28] *Lawson*, 134 S.Ct. at 1169.

[29] Because a whistleblower must be a natural person, the private company itself in theory can be terminated without implicating the Sarbanes-Oxley or Dodd Frank anti-retaliation provisions. Obviously, other common law claims or statutes may prohibit or counsel against taking such action, and taking this step also risks, among other things, upsetting regulators and losing any chance of cooperation from the private contractor.

[30] 15 U.S.C. § 78u-6(h)(1)(A) (LEXIS through Oct. 6, 2014 legislation).

[31] 17 C.F.R. § 240.21F-(a)(6).

Energy (USA), LLC,[32] the Fifth Circuit addressed the issue of whether Dodd-Frank applied to a GE Energy executive who reported a potential violation of the Foreign Corrupt Practices Act internally. He sued, claiming retaliation, after he was subsequently given a negative performance review, pressured to step down from his position, and ultimately fired. The court adopted GE Energy's argument that Dodd-Frank did not protect employees against retaliation in response to internal reporting, stating that "[u]nder Dodd-Frank's plain language and structure, there is only one category of whistleblowers: individuals who provide information relating to a securities law violation *to the SEC*."[33] A number of district courts outside the Fifth Circuit have followed this holding.[34]

Most district courts that have addressed this issue, however, have found that internal reports are covered by Dodd-Frank's anti-retaliation provision. In addition to the textual argument that Sarbanes-Oxley's protection of internal reports is directly imported into Dodd-Frank, these courts have found that Dodd-Frank's purpose is best served by interpreting the whistleblower protection provisions broadly.[35] Whether internal reports qualify for Dodd-Frank coverage has important implications because, among other things, Dodd Frank provides enhanced recoveries and longer time frames for bringing a retaliation claim. A May 2014 decision from the U.S. District Court for the District of Nebraska, *Bussing v. COR Clearing LLC*,[36] stressed that the anti-retaliation protections of Dodd-Frank apply to those who are retaliated against for making any disclosures — not just disclosures to the SEC — that are "required or protected under" Sarbanes-Oxley. The plaintiff in *Bussing* provided information regarding potential violations to FINRA during the course of a formal proceeding and alleged that she was retaliated against for providing that information. In allowing the plaintiff's Dodd-Frank whistleblower claim to proceed, the court held that because the plaintiff had "properly alleged that she made a disclosure required by a rule or regulation subject to the jurisdiction of the SEC" (the FINRA rule governing document requests), her actions constituted a disclosure "required or protected" under Sarbanes-Oxley and afforded her anti-retaliation protection under Dodd-Frank.

Fourth, because certain categories of information are excluded from bounty eligibility, not all employees who otherwise satisfy the criteria for a bounty under Dodd-Frank are eligible. Information provided by legal and compliance personnel largely falls into an excluded category, reflecting that part of these employees' job responsibilities involves reporting and otherwise addressing suspected wrongdoing.

Information will not be considered to be derived from a person's "independent knowledge or independent analysis," and will therefore not be eligible for an award, where the information was obtained "through a communication that was subject to the attorney-client privilege" or "in connection with the legal representation of a client," unless disclosure would otherwise be permitted by an attorney (which would only occur under very limited circumstances).[37] Attorneys will, therefore, rarely qualify. Other exclusions include situations where (1) information is obtained because the whistleblower was an "officer, director, trustee, or partner of an entity" who "learned the information in connection with the entity's process for identifying, reporting, and addressing possible violations of law"; (2) a whistleblower who learned of information because he or she was an "employee whose principal duties involve compliance or internal audit responsibilities"; (3) a whistleblower who learned of information because he or she is "[e]mployed by or otherwise associated with a firm retained to conduct an inquiry or investigation into

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[32] 720 F.3d 620 (5th Cir. 2013).

[33] *Id.* at 625 (emphasis added).

[34] *See, e.g.*, *Banko v. Apple Inc.*, No. CV 13-02977 RS, 2013 WL 7394596, at *6 (N.D. Cal. Sept. 27, 2013) ("Because plaintiff did not file a complaint to the SEC, he is not a 'whistleblower' under the Dodd-Frank Act."); *Wagner v. Bank of Am. Corp.*, No. 12-cv-00381-RBJ, 2013 WL3786643, at *4 (D. Colo. July 19, 2013) (plaintiff who was fired after complaining to her supervisors was "not a 'whistleblower' as defined" by Dodd-Frank because she "did not provide any information to the [SEC]").

[35] *See, e.g.*, *Khazin v. TD Ameritrade Holding Corp.*, No. 13-4149 (SDW)(MCA), 2014 WL 940703, at *6 (D.N.J. Mar. 11, 2014) ("[I]nternal reporting of potential violations is sufficient to qualify as a whistleblower under the Dodd-Frank Act's anti-retaliation provision."); *Azim v. Tortoise Cap. Advisors*, No. 13-2267-KHV, 2014 WL 707235, at *7 (D. Kan. Feb. 24, 2014) (finding complaints to human resources department to warrant whistleblower protection under Dodd-Frank); *Yang v. Navigators Grp., Inc.*, No. 13-cv-2073 (NSR), 2014 WL 1870802 (S.D.N.Y. May 8, 2014); *Genberg v. Porter*, 935 F. Supp. 2d 1094, 1106-07 (D. Colo. 2013) ("I find that [plaintiff] qualifies as a whistleblower under [Dodd-Frank]" even though "he disclosed alleged securities violations to … upper level management").

[36] Case No. 8:12-cv-238, 2014 U.S. Dist. LEXIS 69461, at *17 – 19 (D. Neb. May 21, 2014).

[37] 17 C.F.R. § 240.21F-4(b)(4)(i) and (ii).

possible violations of law."; and (4) a whistleblower who is an "employee of, or other person associated with, a public accounting firm" if the information is obtained "through the performance of an engagement required of an independent public accountant" under the federal securities laws.[38]

Unlike the more stringent exclusion for privileged information learned by an attorney, these four exclusions will not always apply. In fact, these four exclusions will not preclude eligibility for an award if any of the following three conditions is met. First, information will not be excluded if the individual has a "reasonable basis to believe that disclosure of the information to the SEC is necessary to prevent the entity from engaging in conduct likely to cause substantial injury to the financial interest or property of the entity or shareholder." Second, any of these four exclusions will be negated where an individual has a "reasonable basis to believe that the entity is engaging in conduct that will impede an investigation of the misconduct." Third, none of these four exclusions will continue to apply after 120 days "have gone by since the individual provided the information to his or her supervisor, the entity's audit committee, chief legal officer, chief compliance officer, or their equivalents, or at least 120 days have gone by since the individual received the information, if the individual received the information under circumstances indicating that one or more of these individuals or committees was already aware of the situation."[39] These broad exceptions will often swallow the rule, particularly because otherwise ineligible individuals can simply make an internal report and then go to the SEC after 120 days. In fact, in August 2014, the SEC announced its first award to a compliance professional who reported misconduct after the company failed to take action on an internal report within 120 days.[40]

Even in situations where attorneys do not qualify for whistleblower awards under Dodd-Frank, they nevertheless have substantial reporting obligations pursuant to Sarbanes-Oxley. The statute requires attorneys who are advising public companies, whether the attorney is outside or inside the company, to report on evidence they uncover of material violations of the federal securities laws.[41] Initially, attorneys must report the evidence to the "chief legal counsel or the chief executive officer of the company."[42] If no appropriate action is taken following that disclosure, the attorney is required to take the information to the audit committee of the board of directors, another committee of independent directors, or the entire board.[43] Finally, if the reporting attorney still believes that there has been no appropriate response, she must explain her conclusion and the reasons supporting it to the Chief Legal Officer and the board members to whom she reported the violation.[44] After this report, the attorney may, but is not required to, report the violations to the SEC.

Taken together, the obligations imposed on counsel by Sarbanes-Oxley and the chances they have of obtaining a bounty under Dodd-Frank are consistent with a view of counsel's role as a "gatekeeper" against corporate misconduct. For instance, SEC Commissioner Kara Stein recently called for greater attention to the role lawyers can play as "trusted advisors" in increasing compliance and preventing fraud.[45] This is consistent with a growing trend to scrutinize the actions of these gatekeepers. In an October 9, 2013 speech, SEC Chair Mary Jo White stated that the SEC is "focusing on deficient gatekeepers — pursuing those who should be serving as the neighborhood watch, but who fail to do their jobs."[46] In March 2014, Ms. White reiterated this intention, saying, "we have…sought to enlarge our enforcement footprint with a renewed focus on "gatekeepers."[47]

Fifth, a consensus is emerging among federal courts that the Sarbanes-Oxley and Dodd-Frank's whistleblower protection provisions do not apply to

[38] *See generally* 17 C.F.R. § 240.21f-4(b).

[39] 17 C.F.R. § 240.21F-4(b)(4)(v).

[40] Press Release, Sec, Exch. Comm'n., SEC Announces $300,000 Whistleblower Award to Audit and Compliance Professional Who Reported Company's Wrongdoing (Aug. 29, 2014) (*available at* SEC.GOV, http://www.sec.gov/News/Press Release/Detail/PressRelease/1370542799812).

[41] 15 U.S.C. § 7245.

[42] 15 U.S.C. § 7245(1).

[43] 15 U.S.C. § 7245(2).

[44] 17 C.F.R. § 205.3(b)(9).

[45] Kara M. Stein, SEC Commissioner, Keynote Address at Compliance Week 2014 (May 19, 2014) (*available at* SEC.GOV, http://www.sec.gov/News/Speech/Detail/Speech/1370541857558#.VEMn6IvF8so) (last visited Oct. 28, 2014).

[46] Mary Jo White, SEC Chair, Remarks at the Securities Enforcement Forum (Oct. 9, 2013) (*available at* SEC.GOV, http://www.sec.gov/News/Speech/Detail/Speech/1370539872100#.VE1FxIvF-jF) (last visited Oct. 28, 2014).

[47] Mary Jo White, SEC Chair, Perspectives on Strengthening Enforcement (Mar. 24, 2014) (*available at* SEC.GOV, http://www.sec.gov/News/Speech/Detail/Speech/1370541253621#.VE1GYYvF-jE) (last visited Oct. 28, 2014).

persons working abroad. Under *Morrison v. National Australian Bank, Ltd.*[48], there is a presumption that statutes are "primarily concerned with domestic conditions" unless Congress clearly expressed an "affirmative intention" to give that statute extraterritorial effect. Because "United States law governs domestically but does not rule the world,"[49] a statute with no indication of extraterritorial effect has none.[50] Both Sarbanes-Oxley and Dodd-Frank are silent as to the extraterritorial effect of their anti-retaliation provisions. Consequently, most courts have found that they do not apply extraterritorially. In *Carnero v. Boston Scientific Corporation*,[51] for instance, the First Circuit declined to extend Sarbanes-Oxley's anti-retaliation provision to an Argentinian citizen who was employed by the Argentinian subsidiary of a Massachusetts-based company, Boston Scientific Corporation ("BSC"). Although the plaintiff claimed that he had an "over-arching employment relationship with the United States parent, BSC, resulting from the extensive and continuous control BSC's own Massachusetts employees allegedly exercised over his work and duties in Latin America," the court found that Sarbanes-Oxley did not apply to him.[52] Instead, the court held that "[Sarbanes-Oxley's anti-retaliation provision] does not reflect the necessary clear expression of congressional intent to extend its reach beyond our nation's borders."[53]

Similarly, in *Liu v. Siemens AG*,[54] the Second Circuit found that Dodd-Frank's anti-retaliation provision did not apply overseas. In *Liu*, a Taiwanese resident brought a claim against a German corporation following retaliation for reports about corruption in a Chinese subsidiary's actions in China and North Korea. Following *Morrison*, the court stated that "[t]here is no indication Congress intended [Dodd-Frank's] whistleblower protection provision to have extraterritorial application."[55] *Liu* did not foreclose the possibility of international whistleblowers receiving bounty awards under Dodd-Frank. Rather, *Liu* observed that "[p]roviding rewards to persons … who supply information about lawbreaking is far less intrusive into other countries' sovereignty than seeking to regulate the employment practices of foreign companies with respect to the foreign nationals they employ in foreign countries."[56]

The SEC's September 2014 award of approximately $30 million to a foreign whistleblower demonstrated the agency's view that the bounty provisions should apply overseas even if the anti-retaliation provisions do not. In the order announcing the claim, the SEC pointed out in a footnote that, in its view, "there is a sufficient U.S. territorial nexus whenever a claimant's information leads to the successful enforcement of a covered action brought in the United States, concerning violations of the U.S. securities laws, by the Commission, the U.S. regulatory agency with enforcement authority for such violations."[57] The SEC stressed that "it makes no difference whether, for example, the claimant was a foreign national, the claimant resides overseas, the information was submitted from overseas, or the misconduct comprising the U.S. securities law violation occurred entirely overseas."[58] As Chief of the SEC's Office of the Whistleblower, Sean McKessy said, "[t]his award of more than $30 million shows the international breadth of our whistleblower program as we effectively utilize valuable tips from anyone, anywhere, to bring wrongdoers to justice."[59]

Companies with employees working in foreign offices now find themselves in the following odd situation: foreign whistleblowers have a monetary incentive to report misconduct because they are eligible for a bounty, but are not protected from retaliation for doing so. As a practical matter, however, companies need to exercise great caution in contemplating the termination of a whistleblower even on legitimate non-retaliatory grounds given potential fall-out from regulators, the possibility of a suit under laws other than Dodd-Frank or Sarbanes-Oxley, and other considerations.

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[48] 561 U.S. 247, 255 (2010).

[49] *Kiobel v. Royal Dutch Petroleum* Co, 133 S. Ct. 1659, 1664 (2013).

[50] Morrison, 561 U.S. at 255.

[51] 433 F.3d 1 (1st Cir. 2006).

[52] *Id*. at 3.

[53] *Id*. at 18.

[54] 763 F.3d 175 (2d Cir. 2014).

[55] *Id. at* 177.

[56] *Id.* at 183.

[57] Party Redacted, Exch. Act Rel. No. 73174 at *2 (Sept. 22, 2014) (*available at* SEC.GOV | ORDER DETERMINING WHISTLEBLOWER AWARD CLAIM, http://www.sec.gov/rules/other/2014/34-73174.pdf).

[58] *Id.*

[59] Press Release, Sec. Exch. Comm'n., SEC Announces Largest-Ever Whistleblower Award (Sept. 22, 2014) (*available at* SEC.GOV, http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370543011290).

ADDITIONAL CONSIDERATIONS IN RESPONDING TO ALLEGATIONS OF WRONGDOING

While it is important to understand whether or not a person providing information regarding suspected wrongdoing is covered by Sarbanes-Oxley or Dodd-Frank, regardless of the answer, the company still must decide the scope and methodology for investigating the allegations.[60] Failure to do so risks civil, criminal, and regulatory liability, with the resulting exposure (depending on the scope and magnitude of the wrongdoing at issue if it in fact occurred) not only to substantial civil damages, and criminal or regulatory fines, but also to the imposition of a compliance monitor, potential revocation of operating license, and, for individuals, a bar from serving as an officer or director of a public company. In fiscal year 2013, for example, enforcement actions brought by the SEC resulted in $3.4 billion in total fines and disgorgement.[61] A recent trend, particularly in the context of FCPA enforcement actions, is the imposition of a "hybrid monitor," meaning that an external monitor is assigned to the company for a certain amount of time, followed by a stint of self-monitoring.[62] Factors that the SEC and DOJ consider when deciding whether to assign a compliance monitor include: seriousness of the offense, duration and pervasiveness of the misconduct, the nature and size of the company, the quality of the company's compliance program when the misconduct occurred, and subsequent remediation efforts.[63] Companies will stand a far better chance of mitigating or avoiding those consequences via a good faith and thorough internal investigation, and/or cooperating with any government investigation.[64]

While a full-blown discussion of conducting an investigation is beyond the scope of this article, a few key points bear mention.

As an initial matter, it is imperative that in conversations with an individual who has made an internal whistleblower report, representatives of the company should never discourage the tipster from reporting the information to the SEC or another agency. The whistleblower rules explicitly prohibit companies from entering into agreements with employees that are designed to prevent or inhibit individuals from reporting information to the SEC. In particular, the SEC's rules state that "[n]o person may take any action to impede an individual from communicating directly with the Commission staff about a possible securities law violation, *including enforcing, or threatening to enforce*, a confidentiality agreement . . . with respect to such communications."[65] In March 2014, Mr. McKessey warned that if the Office of the Whistleblower finds companies that are enforcing such agreements, "not only are we going to go to the companies, we are going to go after the lawyers who drafted it . . . we have powers to eliminate the ability of lawyers to practice before the Commission. That's not an authority we invoke lightly,

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[60] An exhaustive analysis of relevant considerations in conducting an investigation is outside the scope of this article. For extensive discussions, *see* MICHAEL DELIKAT & RENEE PHILLIPS, CORPORATE WHISTLEBLOWING IN THE SARBANES-OXLEY/DODD-FRANK ERA (2d ed. 2014); GREGORY A. MARKEL & JASON M. HALPER, INTERNAL INVESTIGATIONS, BUSINESS AND COMMERCIAL LITIGATION IN FEDERAL COURTS (3d ed. 2011).

[61] Press Release, Sec. Exch. Comm'n., SEC Announces Enforcement Results for FY 2013 (Dec. 17, 2013) (*available at* SEC.GOV, http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370540503617#.VDwmSBZ0pMg).

[62] In 2013, out of FCPA settlement agreements with seven companies, hybrid monitors were imposed on three: Diebold, Inc., Weatherford International, and Bilfinger SE.

[63] CRIMINAL DIV. OF THE U.S. DEP'T OF JUSTICE & THE ENFORCEMENT DIV. OF THE U.S. SEC. AND EXCH. COMM'N., FCPA: A RESOURCE GUIDE TO THE U.S. FOREIGN CORRUPT PRACTICES ACT 71 (Nov. 14, 2012) (*available at* http://www.justice.gov/criminal/fraud/fcpa/guide.pdf).

[64] For example, in a FCPA enforcement action against Ralph Lauren, comparatively low fines were in part due to significant self-reporting, cooperation, and remediation. *See* Press Release, Sec. Exch. Comm'n., SEC Announces Non-Prosecution Agreement with Ralph Lauren Corporation Involving FCPA Misconduct (Apr. 22, 2013) (*available at* SEC.GOV, http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171514780#.VD0mXvldWGc) ("The SEC has determined not to charge Ralph Lauren Corporation with violations of the [FCPA] due to the company's prompt reporting of the violations on its own initiative, the completeness of the information it provided, and its extensive, thorough, and real-time cooperation with the SEC's investigation."). The Department of Justice's Principles of Federal Prosecution of Business Organizations lays out factors for prosecutors to consider when deciding whether to bring charges against a corporation. Those factors include "the corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate in the investigation of its agents" and "the corporation's remedial actions" including implementation of compliance programs, termination of wrongdoers, restitution, and cooperation with investigators. DEP'T OF JUSTICE, PRINCIPLES OF FEDERAL PROSECUTION OF BUSINESS ORGANIZATIONS, USAM 9-28.300(A)(4)-(6) (1999).

[65] 17 C.F.R. § 240.21F-17(a) (emphasis added).

but we are actively looking for examples of that."[66] In October 2014, Mr. McKessy again expressed concern about companies requiring employees to sign non-disclosure or confidentiality agreements that prevent external reporting to the SEC and warned that his team intends to crack down on this practice. As he put it, "[t]his is now the new thing that I've got people really enthusiastic for."[67] And unlike anti-retaliation provisions in other statutes, the SEC has interpreted Dodd-Frank as allowing the agency to bring anti-retaliation lawsuits itself.[68] For instance, it recently settled an action against Paradigm Capital Management, Inc. and its founder, in part for allegedly retaliating against a whistleblower.[69] Among other sanctions, the order included over $2.1 million in civil penalties and disgorgement, and an undertaking to implement a series of internal reforms, including the retention of an independent compliance consultant.

Another key issue to address is collecting relevant documents in the face of increasingly stringent personal privacy laws, particularly in Europe and Asia. The E.U. restricts the processing of personal data, which includes any communication between natural persons, regardless of the subject matter.[70] Individuals must be notified and give explicit permission before their data can be processed. Companies should consider having implicated employees sign a consent form as soon they initiate an investigation. E.U. law also requires that collected personal data be given adequate confidentiality protection throughout the life of an investigation. Companies may want to consider setting up virtual data rooms that have access controls and limitations on authorized users. Investigations in China pose a different problem. China has state secrets laws that can prevent sensitive materials from leaving the country, although it may be possible to address this problem by conducting on-site document review.

In fact, foreign privacy laws can be so restrictive that they can prevent or at least significantly complicate even the U.S. government's access to documents it needs in order to support its investigations. In *SEC v. Compania Internacional Financiera*, the court dismissed an insider trading case brought by the SEC. The opinion stressed that even though the SEC "submitted dozens of requests to foreign regulators in five countries" and "interviewed or deposed numerous foreign witnesses overseas," it was unable to obtain documents from third parties located in Europe "due to European banking, data protection, and privacy laws."[71] In another case, the SEC filed a subpoena enforcement action in federal court against a Chinese accounting firm after the SEC sought workpapers related to audits of a Chinese company that was listed on a U.S. exchange.[72] The firm asserted that it could not produce the documents to the SEC without violating Chinese law. The case was ultimately dismissed after the SEC received the documents through a Chinese regulator, but not until after several years of litigation with the accounting firm.[73]

Another issue to consider is that, at some point in the course of the investigation, a decision needs to be made about: (1) whether to put the results in writing in the form of a written report and (2) whether and when to disclose the information to regulators (assuming regulators are not already aware of the issue from a third-party source, including the tipster). These decisions require balancing various considerations, including whether disclosing a written report to the government will waive the investigation's privileged status and the importance of obtaining cooperation credit with the regulator.

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[66] Brian Mahoney, *SEC Warns In-House Attys Against Whistleblower Contracts*, LAW360.COM, (Mar. 14, 2014, 5:16 PM), http://www.law360.com/articles/518815/sec-warns-in-house-attys-against-whistleblower-contracts.

[67] Stephanie Russell-Kraft, *SEC Whistleblower Head to Punish Cos. that Silence Tipsters*, LAW360.COM (Oct. 17, 2014, 5:38 PM), http://www.law360.com/articles/587847/sec-whistleblower-head-to-punish-cos-that-silence-tipsters.

[68] Implementation of the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934, Exchange Act Release No. 34-64545, *Id.* note 16 at 34303 ("the Commission may enforce the anti-retaliation provisions of Section 21F(h)(1) of the Exchange Act and any rules promulgated thereunder").

[69] In the Matter of Paradigm Capital Management, Inc., Order Instituting Cease-and-Desist Proceedings, SEC Litigation Release No. 72393 (June 16, 2014) (*available at* SEC ADMINISTRATIVE PROCEEDINGS INDEX, http://www.sec.gov/litigation/admin/2014/34-72393.pdf).

[70] Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the Protection of Individuals with Regard to the Processing of Personal Data and on the Free Movement of Such Data (L 281/31).

[71] No. 11 Civ. 4904 (JPO), 2012 WL 1856491, at *3 (S.D.N.Y. May 22, 2012).

[72] *SEC v. Deloitte Touche Tohmatsu CPA Ltd.*, 942 F. Supp. 2d 43, 47-48 (D.D.C. 2013).

[73] Deloitte Touche Tohmatsu CPA Ltd., Motion to Dismiss Subpoena Enforcement Action, SEC Lit. Rel. No. 22911 (Jan. 27, 2014) (*available at* SEC LITIGATION RELEASES INDEX, http://www.sec.gov/litigation/litreleases/2014/lr22911.htm).

On the question of whether to prepare a written report and, if so, whether to provide a copy to the relevant regulator, it is important to consider the risk that disclosure to the government may waive the report's privileged status and may, therefore, make the document available to other, adverse parties in the course of civil litigation. A recent decision from the Southern District of New York stressed that disclosure of privileged materials to the government, even where a party has entered into a confidentiality agreement with the regulator (which the court called "essentially a fig leaf that permits the producing party to claim, as to third parties, that attorney-client privilege and work product protection are preserved") constitutes a waiver of the attorney-client and work product privileges pursuant to the "standard rule that materials provided to an adversary lose" those privileges.[74] A 2012 decision from the Ninth Circuit similarly emphasized that there is no privilege that protects "disclosures of attorney-client privileged materials to the government" and held that enforcing confidentiality agreements between companies and their regulators "would undermine the public good."[75]

While there is risk in sharing the results of a privileged investigation with the government, companies and their counsel should also keep in mind the potential benefits. The SEC has published a list of 13 criteria it considers "in determining whether, and how much, to credit self-policing, self-reporting, remediation, and cooperation – from the extraordinary step of taking no enforcement action to bringing reduced charges, seeking lighter sanctions, or including mitigating language in documents [it uses] to announce and resolve enforcement actions."[76] Among those criteria are whether a company made the results of its own review available to enforcement staff, including whether the company produces "a thorough and probing written report detailing the findings of its review." The SEC's written release expressly notes, however, that voluntary waiver of work product and other privileges is not "an end in itself," but is rather "a means (where necessary) to provide relevant and sometimes critical information to the Commission staff."[77] In its own release, the Department of Justice has stressed that cooperation is a "potential mitigating factor" by which a corporation "can gain credit in a case that otherwise is appropriate for indictment and prosecution."[78] While that cooperation may come in the form of waiving privileges, prosecutors are instructed that they "should not ask for" waivers of attorney-client or work product protections, though "such waivers occur routinely when corporations are victimized by their employees or others, conduct an internal investigation, and then disclose the details of the investigation to law enforcement officials in an effort to seek prosecution of the offenders."[79] ■

[74] *Gruss v. Zwirn*, No. 09 Civ. 6441 (PGG)(MHD), 2013 WL 3481350, at *8 (S.D.N.Y. July 10, 2013).

[75] *In re Pacific Pictures Corp.*, 679 F.3d 1121, 1128-29 (9th Cir. 2012).

[76] Report of Investigation, Exch. Act Rel. No. 44969 (Oct. 23, 2001) (*available at* SEC.GOV | REPORTS OF INVESTIGATIONS, http://www.sec.gov/litigation/investreport/34-44969.htm).

[77] *Id.*

[78] DEP'T OF JUSTICE, PRINCIPLES OF FEDERAL PROSECUTION OF BUSINESS ORGANIZATIONS, *supra* note 62.

[79] *Id.*

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