SEYFARTH SHAW

One Minute Memo®

SEC Claws Back Award for Dawdling Whistleblower, as Feds Signal Changes in Award Eligibility

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Seyfarth Synopsis*: Last week, the Securities and Exchange Commission released an Order Determining Whistleblower Award Claim holding that the whistleblower's award should be reduced to 20% of the monetary sanctions collected in the covered action because the claimant was both involved in the illegal conduct and delayed in reporting the violations.*

On February 28, 2017, the Securities and Exchange Commission ("SEC") released an Order Determining Whistleblower Award Claim, Release No. 80115, which affirmed the Claims Review Staff's Preliminary Determination that the claimant's whistleblower award be reduced because of the claimant's culpability in the securities violations and the claimant's delay in reporting the award. The SEC adopted the Preliminary Determination and reduced the whistleblower's award to 20%. This penalty is meant to encourage whistleblowers to promptly report violations and act in a manner that curtails, and does not further, the alleged illegal actions.

Under Section 21F of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank"), the SEC is directed to grant monetary awards to "eligible individuals" who offer information to the SEC leading to successful enforcement actions involving monetary sanctions over $1 million. The bounties range from between 10-30% of the sanctions collected. This award program acts as an incentive for employees in the financial industry to report violations of the securities laws. We previously reported on a near record breaking whistleblower award of $22 million in June 2016, bested only by a $30 million award in September 2014. According to the 2016 Annual Report to Congress on the Dodd-Frank Whistleblower Program, more than $111 million has been awarded in bounties to 34 whistleblowers through the Program.

The recent award, however, does not withhold the full amount of the potential recovery, and is only a 10% reduction from the maximum possible award of 30%. While some potential whistleblowers may consider this partial reduction an incentive for prompt reporting, there is also a countervailing consideration that allowing the harm to continue may lead to greater recovery by inflating the potential SEC recovery. Thus as a practical matter, potential whistleblowers might be tempted to weigh the risks and benefits of delay.

As a matter of public policy, however, whistleblowers should not benefit from delay or other less-than-virtuous conduct themselves. Currently, only whistleblowers who are indicted for participation in the underlying misconduct are prevented from receiving bounties. (*See* § 21F(c)(2)(B)). Allowing whistleblowers to benefit from delayed reporting or allowing the misconduct to continue seems contrary to the intent of the law.

Consider the compliance officer who waits until she faces discipline for performance problems and/or unrelated misconduct, and then complains about purported unlawful activity. The compliance officer should have identified and corrected the unlawful conduct as part of her job, yet waited until it was personally advantageous to complain. The delay increased her bounty but also the harm of the misconduct. Although she would likely not be indicted for allowing the misconduct to continue, it seems contrary to the purpose of the Act to allow her to benefit from delay and her failure to correct the misconduct.

House Republicans circulated a non-public memorandum in February taking aim at those involved in the illegal conduct who seek to collect a whistleblower award, and would prohibit claimants from profiting where he or she is found to have compounded the violations by failing to act promptly to report or correct the misconduct.

Further legislative clarity may resolve the issue of whether wrongdoers can continue to profit from deliberate reporting delays or whether prompt action will become a requirement for a whistleblower award. Look out for our posts in the coming weeks which will feature the latest issues with respect to Dodd-Frank.

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