U.S. Securities and Exchange Commission

Speech by SEC Commissioner: Incentivizing Whistleblowers to Bring Fraud to Light

by

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Too often, we see frauds revealed only after the money is gone and investors are tragically harmed. In an attempt to systematically combat this, Congress mandated[1] that the SEC promulgate rules so that whistleblowers would serve as an early warning system to detect fraud.[2] Today, we are putting rules into place to achieve that goal.

The goal of the whistleblower program is to create a system that incentivizes individuals to come forward with high quality information to help the Commission expose fraud.[3] The construction of these rules and the whistleblower program required the Commission to grapple with many nuanced issues. I commend the staff for making reasonable judgments to resolve the many competing considerations at issue here. Careful attention was given to the statutory scheme established by Congress,[4] and to Congress's directive for the Commission to consider the public interest, investor protection, and the effects on competition, efficiency, and capital formation.

These rules have been developed through a robust and public process.[5] The substantial efforts of the Commission and the staff have been enhanced by public participation. As the release notes, public commenters who sent in letters and engaged in meetings on our proposal included individuals, whistleblower advocacy groups, public companies, corporate compliance personnel, and many others. I am thankful to all the commenters representing all constituencies who engaged with us during this process — I found the dialogue to be thoughtful and stimulating. These rules evolved from all of the input received from this extensive process.

The result of this significant undertaking are rules that are faithful to the Dodd-Frank Act and that seek to incentivize whistleblowers to come forward

with high quality information.[6] As the rules evolved, the staff balanced the fact that anyone can, and should, be able to report to law enforcement at any time, while at the same time recognizing that companies and whistleblowers have good reasons to want complaints reported internally. I am mindful of the benefits that can result from companies that maintain high-quality compliance programs. As someone who has been on many sides of the table, as the general counsel and head of compliance of a large company, and now as an SEC Commissioner, I see that these interests do not have to be at odds and can co-exist.

For these reasons, our rule does not mandate one reporting avenue. I expect that many companies will continue to maintain robust compliance programs, and by doing so, this should provide employees with more confidence to report matters internally.[7] In fact, the public comment record amassed here seems to indicate that a majority of whistleblowers already choose to report internally,[8] and the rules we adopt today provide certain incentives for them to do so.[9] Nonetheless, not all public companies may maintain reliable compliance programs, and it is important that whistleblowers retain the ability to report directly to the agency responsible for law enforcement.

In closing, I want to take the time to thank the staff for their careful and thoughtful work, especially those in the Division of Enforcement and the Office of the General Counsel.

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[1] *See* Dodd-Frank Wall Street Reform and Consumer Protection Act § 922, "Whistleblower Protection," amends the Securities Exchange Act of 1934 by inserting Section 21F, and provides in part, "(b) AWARDS.—'(1) IN GENERAL.—In any covered judicial or administrative action, or related action, the Commission, under regulations prescribed by the Commission and subject to subsection (c), shall pay an award or awards to 1 or more whistleblowers who voluntarily provided original information to the Commission that led to the successful enforcement of the covered judicial or administrative action, or related action, in an aggregate amount equal to—'(A) not less than 10 percent, in total, of what has been collected of the monetary sanctions imposed in the action or related actions; and '(B) not more than 30 percent, in total, of what has been collected of the monetary sanctions imposed in the action or related actions."

[2] Senate Consideration of S. 3217, 156 Cong. Rec. S4066 (daily ed. May 20, 2010) (statement of Sen. Kaufman) ("Whistleblowers provide a vital early warning system to detect and expose fraud in the financial system. With the right protections, whistleblowers can help root out the kinds of massive Wall Street fraud that contributed to the current financial crisis").

[3] Report of the Senate Committee on Banking, Housing, and Urban Affairs regarding The Restoring American Financial Stability Act of 2010, S. Rep. No. 111-176 at 110 (2010) ("Senate Report") ("The Whistleblower Program aims to motivate those with inside knowledge to come forward and assist the Government to identify and prosecute persons who have violated securities

laws and recover money for victims of financial fraud").

[4] *See* n. 1 & 3, *supra.*

[5] As the release indicates, we received more than 240 comment letters and approximately 1300 form letters on the proposed rules. *See Final Rules for Implementing the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934* ("Adopting Release"). Public comments are available at http://www.sec.gov/comments/s7-33-10/s73310.shtml.

[6] The rules also clarify the employment retaliation protections provided by Section 21F apply irrespective of whether a whistleblower satisfies the requirements, procedures and conditions to qualify for an award. *See* Rule 21F-2.

[7] While an initial review by the staff of incoming tips and complaints indicates that we have received several hundred potential whistleblower complaints, it is reassuring that there appears to be no indication that we have received a significant number of non-securities complaints.

[8] As described in the *Adopting Release*, certain studies indicate that in *qui tam* cases, the majority of insiders first reported matters internally. *See e.g.,* Aaron S. Kesselheim, David M. Studdert, & Michelle M. Mello, *Whistle-Blowers' Experiences In Fraud Litigation Against Pharmaceutical Companies,* 362 New Eng. J. Med. 1832 (2010) ("Nearly all (18 of 22) insiders first tried to fix matters internally by talking to their superiors, filing an internal complaint, or both"); *Impact of Qui Tam Laws On Internal Compliance*, National Whistleblowers Center (Dec. 17, 2010) (indicating that 89.68% of employees studied who filed a qui tam case initially reported their concerns internally, either to supervisors or compliance departments); *also see Letter from Taxpayers Against Fraud* (Dec. 17, 2010) ("it is our membership's experience that the vast majority of whistleblowers do, in fact, report their concerns first to either their superiors or compliance officers, and only avail themselves of statutory whistleblower programs when their concerns have been dismissed or unaddressed, or when they suffer retaliation"). While these studies may have limitations, they provide a basis to conclude that many whistleblowers already report violations internally, and may often do so for non-monetary reasons. *See* 362 New Eng. J. Med. at 1834 and 1839.

[9] *See Adopting Release* (These incentives include providing whistleblowers with a 120-day period to report to the Commission after they report internally (Rule 21F-4(b)(7)); crediting a whistleblower with the company's self-reporting of certain information based on the whistleblower's original information (Rule 21F-4(c)(3)); and including criteria that could increase the amount of an award for participation and cooperation with the company (Rule 21F-6). Importantly, with respect to the 120-day "look back" period, the release makes clear that this provision is for the benefit of whistleblowers and does not provide a grace period for entities in determining their response to violations).

http://www.sec.gov/news/speech/2011/spch052511laa-item2.htm

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