

PUBLICATION

SEC Issues Proposed Rules on Whistleblower Protections of Dodd-Frank: Encouraging Whistleblowers to Exhaust Internal Means First

November 5, 2010

Section 922 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, which was enacted into law in the summer of 2010, added new Section 21F, entitled "Securities Whistleblower Incentives and Protection Act," to the Exchange Act. The new section directed that the Securities and Exchange Commission pay awards of between 10 and 30 percent of the amount recovered, subject to certain limitations and conditions, to whistleblowers who voluntarily provide the Commission with original information about a violation of the securities laws that leads to a successful enforcement of an action brought by the Commission that results in monetary sanctions exceeding \$1 million.

On November 3, 2010 the Commission proposed rules to implement the Securities Whistleblower Incentives and Protection Act. Comments on the proposed rules are due by December 17, 2010.

Prior to the Commission proposing its rules, Baker Donelson securities attorneys met with staff members of the Commission on October 4, 2010 to discuss these whistleblower provisions and to advocate for certain key provisions to be included in the rules. We are pleased to report that the Commission took several of our comments in issuing its proposed release, including our suggestion that whistleblowers be encouraged to exhaust internal procedures prior to submitting a complaint to the Commission. Baker Donelson's comment letter was filed on October 12, 2010 and can be viewed [here](#).

There are several key aspects of these very complex proposed rules, but one of the most important provisions is the Commission's providing incentives for whistleblowers to exhaust internal procedures first. In particular, in the proposed rules, the Commission expressed concern that the potential monetary incentives provided to whistleblowers may reduce the effectiveness of a company's existing compliance, legal audit and similar internal processes for investigating and responding to potential violations of federal securities laws.

During the October meeting with Commission staff members, Baker Donelson's attorneys expressed these same concerns. Since the enactment of Sarbanes-Oxley Act in 2002, companies with listed securities have been required to develop and implement whistleblower complaint policies and procedures covering accounting and auditing practices. Securities Exchange Act § 10A, 15 U.S.C. § 78j-1. Since the implementation of the Sarbanes-Oxley whistleblower mandates by the securities exchanges, we have observed that most public companies with listed securities have adopted effective internal whistleblower programs which have become an accepted part of corporate cultures and have helped to foster an atmosphere in which legal compliance is an important corporate objective.

To balance these competing issues, the proposed rules provide, in effect, that when a whistleblower internally reports a complaint, he will be deemed to have submitted his complaint to the Commission and will not lose the characterization as the "original source" of the information so long as the whistleblower submits his claim to the Commission within 90 days.

In addition to giving the whistleblower credit for internally reporting first, the Commission stated in its release that in order to encourage whistleblowers to utilize internal reporting processes, it will give favorable consideration in calculating the amount of an award whether the whistleblower used established internal

procedures for the receipt and consideration of complaints and misconduct. Baker Donelson likewise advocated for this provision in the rules.

If you have questions about this or any other securities-related issues, please contact your Baker Donelson attorney.