

# PKF PERSPECTIVES

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## SEC ADOPTS RULES IMPLEMENTING DODD-FRANK WHISTLEBLOWER PROGRAM

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On May 25, 2011 by a vote of 3-2, the Securities and Exchange Commission (“SEC”, “agency” or “Commission”) adopted the whistleblower rewards rules of Section 922 of the ***Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010*** (“Dodd-Frank”). These rules reward individuals who provide the agency with original high-quality tips that lead to successful enforcement actions. It also caused the SEC to create an *Office of the Whistleblower*.

### Who Can Be a Whistleblower?

A whistleblower is a person who voluntarily provides information to the SEC relating to a possible violation of the securities laws that has occurred, or that is ongoing, or that is about to occur. They will be considered for an award under circumstances described later in this publication.

Certain people, including the following, generally will **not** be considered for whistleblower awards:

- People who have a pre-existing legal or contractual duty to report information to the Commission.
- Attorneys (including in-house counsel) who attempt to use information obtained from client engagements to make whistleblower claims for themselves.
- People who obtain information by means or manner that is determined by a U.S. court to violate federal or state criminal law.
- Foreign government officials.
- Officers, directors, trustees, or partners of an entity who are informed by another person (such as by an employee) of allegations of misconduct, or who learn the information in connection with the entity’s processes for identifying, reporting and addressing possible violations of law (such as the company hotline).

- Compliance and internal audit personnel.
- Public accountants working on SEC engagements, if the information relates to violations by the engagement client.

There are certain circumstances where public accountants, compliance and internal audit personnel could become whistleblowers, including when:

- The whistleblower reasonably believes disclosure may prevent the entity from conduct that is liable to cause substantial injury to the financial interest or property of the entity or its investors.
- The whistleblower reasonably believes the entity is engaging in conduct that will impede an investigation.
- At least 120 days have elapsed since the whistleblower either (1) reported the information to his/her supervisor or the entity’s appropriate personnel, or (2) had received information indicating that the appropriate company personnel were already aware of it.

### Requirements for Award Consideration

To be considered for an award, the rules require that a whistleblower must:

***... voluntarily provide the SEC with original information that leads to the successful enforcement by the SEC of a federal court or administrative action in which the SEC obtains monetary sanctions totaling more than \$1 million.***

In general:

- If a whistleblower provides information prior to the government, a self-regulatory organization or the Public Company Accounting Oversight Board (PCAOB) asking for it directly from the whistleblower or his representative, the information will be deemed to be provided voluntarily.

- Original information must be based on the whistleblower's independent knowledge or independent analysis, not already known to the Commission and not derived exclusively from public sources.
- Successful enforcement action is deemed if:
  1. The information is sufficiently specific, credible and timely to cause the SEC to open a new examination or investigation, re-open a closed examination, or open a new line of inquiry in an existing examination or investigation.
  2. The conduct was already under investigation when the information was submitted, and the information significantly contributed to the success of the action.
  3. The whistleblower reports original information through his/her employer's internal whistleblower, legal, or compliance procedures before or at the same time it is passed along to the SEC; the employer provides the whistleblower's information (and any subsequently-discovered information) to the Commission; and the employer's report satisfies numbers 1. and 2. above.
- The rules permit aggregation of multiple SEC cases that arise out of a common nucleus of operative facts as a single action. These may include proceedings involving the same or similar parties, alleged violations of the federal securities laws, or transactions or occurrences.

## Award Determination

The new rules describe the procedures for submitting information to the SEC and for making a claim for an award after an action is brought. The claim procedures provide whistleblowers with opportunities to fairly present their claim before the Commission makes a final award determination.

The amount of a whistleblower award will be subject to assessments made by the Claims Review Staff at the SEC's new **Office of the Whistleblower**. The rules provide for between 10% and 30% of the aggregate monetary recovery by the SEC and/or a related action by another

government agency, with various factors increasing or decreasing the award percentage.

One factor that weighs heavily in favor of a higher award is whether the whistleblower used internal compliance processes. On the other hand, if the whistleblower interferes with such processes, the percentage of his/her recovery award will be diminished.

To further encourage the use of internal compliance processes, the rules allow for an employee to report information internally while preserving his/her "place in line" for a possible award from the SEC if the employee discloses the same information to the SEC within 120 days of such internal report.

## For Public-Company Consideration

Careful assessment of your company's internal compliance programs will assist in ensuring that potential whistleblowers have a way to communicate their concerns and that such concerns are properly addressed. Also, re-evaluating internal investigation policies and practices should assist the company to quickly and thoroughly resolve any issues.

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The final rule-making document, SEC Release No. 34-64545, is available at this link:

<http://www.sec.gov/rules/final/2011/34-64545.pdf>

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