

The employee strikes back

Recent US amendments, combined with longstanding UK protections, will lead to more whistleblower activity

On May 25 2011, in a 3-2 vote, the US Securities and Exchange Commission (SEC) approved its final rules (US rules) to implement the whistleblower award program of Section 21F of the Securities Exchange Act of 1934, which was added by Section 922 of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

The US rules establish the standards and procedures the SEC will apply in awarding whistleblowers monetary compensation for providing tips about possible securities law violations (including violations of the Foreign Corrupt Practices Act) that lead to successful SEC enforcement actions and make definitions which set the contours for protections of whistleblowers under the Dodd-Frank Act's anti-retaliation provisions.

Under the US rules, a whistleblower who voluntarily provides the SEC with original information that leads to a successful enforcement by the SEC that results in monetary sanctions of more than \$1 million arising out of the same core facts is eligible for an award of 10 to 30% of any amounts recovered.

As a result, there is little doubt that there will be an increase in external whistleblower activity. Indeed, the SEC has said that it expects to receive approximately 30,000 tips per year and plaintiffs' law firms have set up websites to attract whistleblower leads in

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the US and abroad.

The Dodd-Frank Act significantly expands the protections afforded to whistleblowers under the Sarbanes-Oxley Act of 2002 (Sox) by increasing the scope of companies subject to the Sox anti-retaliation provisions, providing whistleblowers more time to make retaliation claims and increasing the penalties for such retaliation.

These laws, which apply in the context of securities law violations, supplement numerous existing US whistleblower laws designed to protect whistleblowers in a variety of other specific contexts, including workplace health and safety, environmental protection, energy, transportation safety, and taxation.

Another important law in the US whistleblower landscape is the False Claims Act (FCA), which imposes liability on persons and companies (typically government contractors) who defraud governmental programs. The law includes a *qui tam* provision that allows people who are not affiliated with the government to blow the whistle by filing actions on behalf of the government.

Whistleblowers in the UK have enjoyed protection against dismissal and retaliation since 1999 when the Public Interest Disclosure Act 1998 (PIDA) came into force, inserting new protections into the Employment Rights Act 1996 (ERA).

UK law protects employees and workers against retaliation for making a protected disclosure (of which more below).

Protection against retaliation

For the purposes of the anti-retaliation protections under the Dodd-Frank Act, an individual is a whistleblower if that individual possesses a reasonable belief that the information he or she is providing relates to a possible securities law violation that has occurred, is ongoing, or is about to occur, and he or she reports that information in accordance with the procedures delineated in the rules.

Protection from retaliation is only afforded to employees, but other classes of whistleblower may be eligible to receive an

award under the whistleblower award program.

The original anti-retaliation provisions of Sox extended only to employees of publicly traded companies, but the Dodd-Frank Act has amended those provisions to include employees of subsidiaries or affiliates of publicly traded companies. Eligibility for protection from retaliation under other US laws varies depending on the applicable law, but protection is typically afforded only to employees under these laws.

In the UK, PIDA only affords protection to employees and other categories of worker.

Under normal circumstances, an employee may only claim unfair dismissal if he or she has the necessary period of qualifying service (currently one year) and any compensation will be subject to a maximum statutory cap (currently between approximately £68,000 and £80,000 depending on length of qualifying service).

However, employees who are dismissed for making a protected disclosure may claim unfair dismissal without any requirement to establish qualifying service. Furthermore, in such cases, compensation for unfair dismissal will be awarded without applying the statutory cap on compensation which usually applies in cases of unfair dismissal.

Workers, comprising not only employees but also other certain self-employed contractors, home workers and agency workers, also enjoy protection against retaliation should they make a protected disclosure and also stand to recover appropriate compensation including damages for injuries to feelings and aggravated damages in appropriate cases.

When is an eligible whistleblower protected?

The protection provided under the US rules is available to persons with information concerning a possible securities law violation.

Similarly, Sox prohibits companies from engaging in retaliation against an employee for providing information regarding conduct the employee reasonably believes constitutes a violation of any rule or regulation of the SEC, federal criminal provisions relating to securities, bank, mail, or wire fraud, or any federal law relating to fraud against shareholders.

A patchwork of other federal and state laws protects whistleblowers from retaliation in various other specific contexts.

By contrast, the UK protects whistleblowers pursuant to one act, PIDA (whose provisions are now contained in the ERA), which makes protections available to

employees and workers with information concerning which they reasonably believe falls into one or more of the following categories: (i) a criminal offence; (ii) a breach of any legal obligation; (iii) a miscarriages of justice; (iv) dangers to health and safety of any individual; (v) damage to the environment; and (vi) the deliberate concealing of any of the above.

Somewhat surprisingly, the UK courts have made it clear that there need be no public interest in the information being disclosed. An employee can therefore claim protection when disclosing information concerning a breach of his or her own employment contract.

Qualifying for protection

In order to qualify for protection against retaliation under the US rules, a whistleblower must possess a reasonable belief that the information he or she is providing relates to a possible securities law violation that has occurred, is ongoing, or is about to occur, and he or she reports that information in accordance with the procedures delineated in the rules.

“To be eligible for an award, the whistleblower must provide information voluntarily to the SEC”

In order to qualify for protection under the UK regime, the worker or employee must disclose information concerning a matter which qualifies for protection (see above) to their lawyer for the purposes of obtaining advice or in good faith to their employer or another person prescribed by the legislation.

Disclosures to prescribed persons such as the Financial Services Authority or Her Majesty's Revenue & Customs are protected where the whistleblower reasonably believes that: (i) the default in question falls within the remit of that body; and (ii) the information disclosed and any allegation within it is substantially true. Wider disclosure (for example to the police or media) is only protected if a stringent list of criteria are satisfied.

Eligibility for financial award

The US rules provide a potentially significant financial incentive to persons in possession of information concerning possible violations of federal securities laws to blow the whistle to the SEC.

The US rules define a whistleblower as an individual who, alone or jointly with others, “provides the SEC with information . . . [that] relates to a possible violation of the federal securities laws (including any rules or regulations thereunder) that has occurred, is ongoing, or is about to occur”.

A whistleblower may remain anonymous when reporting possible violations to the SEC, but, to do so, must report through an attorney.

The US rules exclude a number of categories of whistleblower from eligibility for an award. The following are examples of categories of individuals who, subject to certain exceptions, are ineligible to receive an award: (i) principals (officers, directors, trustees, or partners of a company who receives information about the alleged misconduct from a company employee or from the company's internal compliance process); (ii) attorneys and information obtained in connection with legal representation; (iii) compliance personnel; (iv) individuals retained to conduct an inquiry; (v) accountants; (vi) those who have obtained information by means judged to be illegal by a US court; and (vii) foreign government officials.

Under certain circumstances, the US rules provide exceptions for excluded individuals who are principals, compliance or internal audit personnel, individuals employed by or otherwise associated with a firm retained to conduct an inquiry or investigation into possible violations of law, or independent public accountants.

An otherwise excluded whistleblower belonging to one of these categories will be eligible for an award if he or she has a reasonable basis to believe that disclosure is necessary to prevent the company from engaging in conduct that is likely to cause substantial financial injury to the company or investors belonging to one of these categories.

A whistleblower is also eligible if he or she has a reasonable basis to believe the company is engaging in conduct that will impede an investigation of the misconduct, or at least 120 days have elapsed since the whistleblower provided the information through the company's internal reporting system.

Eligibility of information

In order to be eligible for an award, the whistleblower must provide information voluntarily to the SEC; that is, before a

request, inquiry, or demand was directed to the whistleblower personally or to his or her representative by the authorities and in circumstances where the whistleblower is not under a pre-existing legal duty to report.

All information provided must be original, being based on the whistleblower's independent knowledge or independent analysis, and must not already be known to the SEC.

If the whistleblower provides the same information to an internal compliance program, the whistleblower will have a 120-day time period during which he or she can alert the SEC and still be considered to have provided original information as of the date the information was provided to the internal compliance program.

A whistleblower provides original information that leads to a successful enforcement action in several situations: first, when the information was sufficiently specific, credible, and timely to cause the staff to commence an examination or open an investigation; and second, the information may lead the staff to reopen an investigation, or inquire concerning different conduct as part of a current examination or investigation.

In both instances, an award may be made if the SEC brings a successful judicial or administrative action based on that information. In contrast, when an examination or investigation was already underway, and the whistleblower's submission significantly contributed to the success of the action, then the whistleblower also may be eligible for an award.

In addition, a whistleblower will be eligible for an award if he or she reports original information through a company's internal legal or compliance reporting procedures before or at the same time it is reported to the SEC and the company then reports the information to the SEC. Further, the SEC may attribute all the information provided by the company to the SEC to the whistleblower, whether or not originally reported by the whistleblower.

As a result, a whistleblower may get credit—and potentially a larger award—for any additional information that is generated by the company in its investigation. This is intended to provide additional incentives for whistleblowers to report internally.

The \$1 million threshold can be met by civil money penalties, disgorgement payments, and prejudgment interest totaling more than \$1 million whether from a single or multiple cases that arise out of the same nucleus of operative facts as a

single action, as well as related actions brought by other government agencies such as criminal prosecutions by the Department of Justice.

The SEC will not pay an award if an award already has been granted to the whistleblower by the US Commodity Futures Trading Commission for the same action.

Factors impacting amount of award

The US rules give the SEC wide discretion in determining the amount of the award within the 10% minimum and the 30% maximum provided in the statute. In determining the amount of an award, the SEC will consider:

- the significance of the information provided by a whistleblower to the success of the SEC action or related action;
- the degree of assistance provided by the whistleblower and any legal representatives of the whistleblower;
- the interest of the SEC in deterring violations of the securities laws by making awards to whistleblowers who provide information that leads to the successful enforcement of such laws; and
- whether the whistleblower participated in internal compliance systems and reported any violation internally, or assisted in any internal investigation.

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The SEC also will consider the personal culpability of the whistleblower (that the whistleblower may have been to blame does not exclude the potential to receive an award in all cases), any unreasonable delay by the whistleblower in reporting the securities violations and whether the whistleblower interfered with internal compliance and reporting systems.

In the UK, PIDA does not provide any

financial incentive for an employee or worker to blow the whistle, although those who do and are subsequently dismissed (in the case of employees) or subject to retaliation (in the case of workers) may recover significant compensation.

While any award compensation will focus upon compensating the employee for loss suffered as a consequence of dismissal or retaliation, damages may also be awarded for injuries to feelings and, in appropriate cases, aggravated damages may also be awarded.

In addition, certain public authorities such as the Office of Fair Trading and Her Majesty's Revenue & Customs offer rewards for information received concerning cartels (in the case of the former) and smuggling and certain other tax evasion (in the case of the latter).

The US rules provide a strong financial incentive for employees in possession of information about possible violation of securities laws to disclose that information to the SEC. While the US rules do not discourage whistleblowers to report matters internally before going to the SEC, neither do they require them to do so.

In contrast, PIDA can be said to encourage internal reporting in that it restricts the circumstances in which disclosures made to persons outside the company will be protected.

Are whistleblowers who go to the media protected?

A recently decided US case ruled that the whistleblower provisions of Sox do not protect employees who disclose information to the media. However, courts have determined that other whistleblower protection laws, such as the Whistleblower Protection Act, which protects government employees from retaliation, protect whistleblowers who expose wrongdoing to members of the press.

The Dodd-Frank Act does not expressly address whether the whistleblower protections afforded by it will protect individuals who disclose information to the media.

Under the UK regime, a disclosure of relevant information to the media will only be protected if: (i) that disclosure is made in good faith; (ii) the worker reasonably believes that the information disclosed and any allegation within it is substantially true; (iii) the disclosure is not made for personal gain; and (iv) the worker has either: (a) previously disclosed the information to the employer or a prescribed person; or (b) reasonably believes either that they will be subject to a detriment or that material

evidence will be concealed or destroyed if they do so.

Can a UK employee claim protection under the US rules?

The provisions of the Dodd-Frank Act and the US rules that define who is eligible to receive a whistleblower award or to be protected by the new anti-retaliation provisions do not require an individual to be a US citizen or located in the US. Consequently, some observers predict the lucrative incentives of the whistleblower award program will generate an influx of complaints relating to alleged violations of the Foreign Corrupt Practices Act.

In contrast, at least one US court has held that the whistleblower protections afforded by Sox do not extend to foreign workers employed by foreign subsidiaries of US companies. While the Dodd-Frank Act specifically amends the Sox anti-retaliation provisions to include subsidiaries and affiliates of US companies, it does not expressly address whether these protections apply to foreign subsidiaries or affiliates of such companies.

While the UK and US regimes differ in a number of important respects, they both operate to provide a strong incentive upon companies to promote a compliance culture and put in place appropriate policies and procedures (including internal reporting procedures) which demonstrate their commitment to compliance and encourage compliance in their employees, customers and suppliers by the use of appropriate incentives and penalties.

It remains to be seen whether the potentially significant awards available under the US rules are made available to non-US citizens located outside the US.

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