Blowing the Whistle: SEC Style

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Overview

• How did we get here?
• Dodd-Frank Whistleblower Provisions
• Who blows the whistle?
• Why is the whistle blown?
• Who hears the whistle?
• How can a company minimize the number of whistles?
How did we get here?

- Sarbanes-Oxley Act – established internal control environment and compliance programs. Section 806 is the whistleblower provision.
Dodd-Frank
Whistleblower Provisions

• Designed to incentivize and protect individuals who provide “original information” to the SEC, relating to any violation of the securities laws, that results in monetary sanctions exceeding $1.0 million

• Original information is derived from the independent knowledge of the whistleblower and is not known to the SEC from any other source
Dodd-Frank Whistleblower Provisions

• Awards can be made in the amount of 10% to 30% of the monetary sanctions collected
• Awards are paid from the Investor Protection Fund ($452 million in fund at September 30, 2011)
• Separate office of the SEC Enforcement Division established to administer program; current chief is Sean McKessy
Who blows the whistle?

- SEC is required to issue an annual report after the end of each fiscal year
- First report issued after September 30, 2011, so the results cover the first seven weeks
  - 334 whistleblower tips received from August 12 through September 30, 2011 (annual rate of 2,500)
  - Tips received from 37 states
    - California: 34 tips
    - New York: 24 tips
    - Florida: 19 tips
    - Texas: 18 tips
Who blows the whistle?

– 32 tips received from foreign countries
Who blows the whistle?

- Anyone can blow the whistle
  - Company personnel, competitors, investors, former spouses
- Compliance and internal audit personnel
  - “reasonable basis to believe” that disclosure is necessary to prevent substantial injury to the company or its investors
  - “responsible management or governance personnel at the entity were aware of the imminent violation and were not taking steps to prevent it”
Why is the whistle blown?

• Common complaint categories
  – Market manipulation: 54 tips
  – Offering fraud: 52 tips
  – Corporate disclosures and financial statements: 51 tips
  – Insider trading: 25 tips
  – Other: 79 tips*

* The whistleblower chose not to use one of the predefined compliant categories
Why is the whistle blown?

- Blank, 5
- Manipulation, 54
- Offering Fraud, 52
- Other, 79
- Market Event, 11
- Unregistered Offerings, 18
- Municipal Securities & Public Pension, 9
- FCPA, 13
- Trading & Pricing, 17
- Insider Trading, 25
- Corporate Disclosure & Financials, 51
Who hears the whistle?

- SEC
  - Office of the Whistleblower works in tandem with the Office of Market Intelligence to undertake a triage process
  - If it is worth investigating, Office of the Whistleblower will work with the investigative staff of the Enforcement Division
  - The SEC’s proposed FY 2013 budget requests funding for 191 more positions
  - During FY 2011, the Division of Enforcement filed 735 enforcement actions, more than any other year in its history
Who hears the whistle?

- Other agencies:
  - FBI: plaintiffs lawyers are directing whistleblowers to contact the SEC because the monetary rewards are higher
  - IRS: whistleblower program for years
  - FTC: 1.5 million financial fraud complaints in 2011
  - DOJ
  - OFAC
  - CFTC
  - DOL (OSHA)
  - Others
How can a company minimize the number of whistles?

Tone at the Top

This characteristic cannot be emphasized enough

• Must be a priority of the Board
• Must be credible
• Culture must earn employee confidence