

## News & Events

### Securities & Employment Law Alert: Whistleblower Protections Expanded

#### **WHISTLEBLOWER PROTECTIONS EXPANDED NEW SECURITIES AND EXCHANGE COMMISSION (SEC) RULES EFFECTIVE AUGUST 12, 2011**

SEC whistleblower rules added under the Dodd-Frank Act now in effect will have a significant impact on private and public companies. Companies should become familiar with the new rules and train their management and employees to prevent any unintentional violations of the rules. Background On May 25, 2011, the SEC adopted whistleblower rules - contained in Regulation 21F - to implement Section 21F of the Securities Exchange Act of 1934 (Exchange Act). Regulation 21F, which became effective on August 12, 2011, applies to both private and public companies and establishes a process for whistleblower reporting that could award whistleblowers up to 30 percent of the government's recovery if the total recovery exceeds \$1 million.

#### **NEW WHISTLEBLOWER PROVISIONS UNDER THE DODD-FRANK ACT: WHAT YOU NEED TO KNOW**

Section 21F and Regulation 21F generally provide that the SEC is required to pay whistleblowers awards equal to 10 to 30 percent of the aggregate monetary recoveries obtained by the SEC, the U.S. Department of Justice and certain other authorities in a judicial or administrative action. This could happen where one or more whistleblowers voluntarily provide original information regarding a violation or possible violation of the federal securities laws and the information leads to one or more enforcement actions that result in monetary sanctions exceeding \$1 million. Section 21F and Regulation 21F also expand anti-retaliation employment protections and remedies for whistleblowers.

#### **GENERAL RECOMMENDATIONS**

Companies should have policies and procedures that encourage employees and others to first report their concerns about possible securities law violations to the company. Because of the potential for large awards for whistleblowers, which encourage employees to bypass a company's internal reporting system, companies should redouble their efforts to encourage employees to report violations and possible violations internally. In this regard, companies may wish to consider the following:

- Adopt a comprehensive whistleblower policy which clearly states that there will be no retaliation for reporting.
- Provide several ways to report a violation, including by email, a toll-free hotline and a confidential/anonymous disclosure system.
- Offer periodic training on the company's whistleblower policy and assure employees that their complaints will be handled appropriately and seriously.
- Review employee confidentiality agreements, employee handbooks, and other employee materials that may limit employees' dissemination of information outside the company to

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assure that nothing might be construed as prohibiting protected whistleblowing.

- Obtain confirmation from employees in exit interviews or separation agreements that the employee is not aware of any possible violations.
  - Take immediate action upon receipt of a whistleblower complaint. The SEC has emphasized that the promptness with which a company self reports misconduct is an important factor in considering whether to grant leniency for cooperating in the SEC's investigations and enforcement efforts.
  - Review and potentially expand the scope of the company's directors and officers insurance policy to ensure adequate coverage in the event of an SEC investigation, as the new whistleblower rules are likely to result in additional SEC investigations. It is important to review your policies and ensure it is protecting what you wish.
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#### **ADDITIONAL INFORMATION REGARDING**

##### **SECTION 21F AND REGULATION 21F**

Neither Section 21F nor Regulation 21F requires the whistleblower to first report the violation or possible violation to the company. This makes it particularly important for companies to increase their efforts to create internal policies and procedures to encourage employees to report any suspected violations internally through implementation of an effective whistleblower policy. If an employee reports to the SEC first, the company may be placed in the unfortunate position of learning about the possible violation from the SEC.

- Although internal reporting is not required, the SEC has attempted to counterbalance the potential disincentives for internal reporting by providing some reward for whistleblowers to go through internal channels first. A whistleblower's cooperation in the company's internal compliance program can be used by the SEC as a factor to increase the award. In addition, a whistleblower's unreasonable delay in reporting or interference with the company's internal compliance program can reduce the size of the award.
- Whistleblowers who first report internally may delay reporting to the SEC for up to 120 days and still receive an award. Whistleblowers may also receive awards even if the company reports the information to the SEC that ultimately results in a successful award action.
- The definition of a whistleblower includes not only employees of the issuer or its consolidated subsidiaries. The definition is broad enough to include an employee of a competitor, an angry ex-spouse, or even an unaffiliated academic.
- Violations of the securities laws include violations of the Foreign Corrupt Practices Act (FCPA). The anti-bribery provisions of the FCPA apply to both private and public companies. Thus, the new whistleblower provisions raise the specter of enhanced enforcement of FCPA provisions against both public and private companies.
- In addition to the whistleblower bounty provisions, Section 21F and Rule 21F create additional anti-retaliation provisions which both supplement and expand upon those protections already provided under Sarbanes-Oxley Act of 2002 (SOX). Many employees are now covered by both SOX and Section 21F/Regulation 21F.
- The statute of limitations for retaliation claims under Section 21F is six years or more, which is much longer than the ninety days originally provided for in the anti-retaliation provisions of SOX.
- The anti-retaliation protections provide not only for reinstatement and attorneys' fees but also double back pay plus interest. Under SOX, the anti-retaliation remedies consist of one times back pay plus interest and attorneys' fees. Coupled with the longer statute of limitations, this raises the possibility of significantly larger awards to whistleblowers for retaliation claims.
- The anti-retaliation provisions apply even if the whistleblower does not qualify for an award and even if the information provided does not relate to an actual violation of law. The only requirement is that the whistleblower has a reasonable belief that there was a violation of securities laws.

The SEC estimates that it will receive 30,000 tips, complaints and referrals annually through its

new whistleblower system and that there will be approximately 150 SEC actions resulting in monetary sanctions of greater than \$1 million. As a result, the plaintiff's bar now is actively recruiting potential whistleblowers, so employers need to be prepared.

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**ADDITIONAL INFORMATION**

If you have any questions on adopting a new whistleblower policy or in implementing changes to an existing policy in light of the changes described in this alert, please contact shareholders Michele D. Vaillancourt or Laura A. Pfeiffer.

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