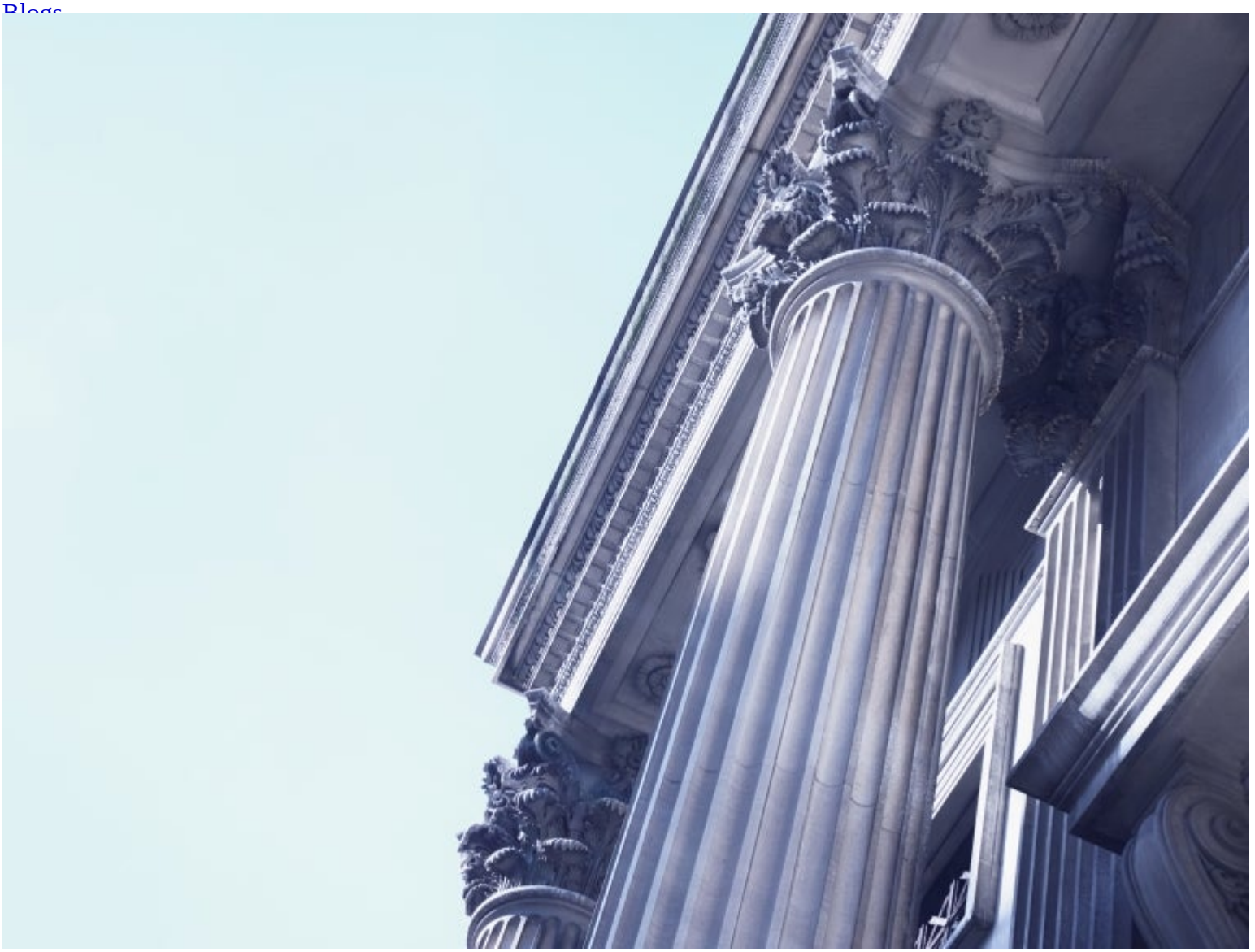

On June 28, 2018, the U.S. Securities and Exchange Commission proposed three rule changes to the Commission's Whistleblower Program, including one that would authorize the SEC to "downward adjust" monetary awards in large actions for which an award might "exceed an amount that is reasonably necessary to advance the program's goals"—in the view of the Commission.

The proposed change prompted an immediate response from Commissioner Kara Stein who issued a separate Statement on Proposed Amendments to the Commission's Whistleblower Program Rules ("Statement") in which she highlights concerns that a move towards a more subjective standard in determining monetary awards could threaten a whistleblower's incentive to come forward, given the added uncertainty in outcome. Additionally, Stein questions whether the SEC has the statutory authority under the Dodd-Frank Act to alter the rules impacting awards in this way. ***Current Rules Governing Monetary Awards*** On May 25, 2011, in a 3-2 vote, the SEC adopted its final rules for its Whistleblower Program, as required under Section 922 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. The rules authorize the SEC to reward individuals who provide the Commission with information leading to successful enforcement actions that exceed $1 million in monetary sanctions. Eligible whistleblowers can earn a payout of 10% to 30% of any monetary sanctions collected because of the tipster's information. To earn a whistleblower bounty, a tipster must voluntarily provide "original information" about a possible federal securities law violation that has occurred, is ongoing, or is about to occur. The rules require this original information to be based on the whistleblower's independent knowledge or analysis and not on information that has already been provided to the SEC by another source—unless the whistleblower is the original source of the information. In an effort to accommodate concerns about whistleblowers bypassing internal reporting systems at their corporations to instead go directly to the SEC with their concerns, the rules provide that the SEC will consider whether a whistleblower first reported any potential violations through internal procedures when it determines the amount of the whistleblower's reward. Under this structure, higher percentage awards may be awarded to whistleblowers who report violations internally before turning to the SEC. ***Defining "Monetary Sanctions Collected" and Prohibiting "Double Recovery"*** As noted above, to be eligible for a whistleblower award, the information provided to the Commission must lead to a successful enforcement that exceeds $1 million in monetary sanctions. The first of the three proposed amendments would expressly allow for the payment of awards based on money collected under:

- Deferred prosecution agreements ("DPAs") or non-prosecution agreements ("NPAs") entered into by the U.S. Department of Justice ("DOJ");
- A state attorney general in a criminal case; or,
- A settlement agreement entered into by the Commission outside of the context of a judicial or administrative proceeding to address violations of the securities laws.

Under this proposed amendment, any money paid under these additional arrangements would be deemed qualifying "monetary sanctions." The second proposed amendment would clarify that a "related action" brought by an authority outside of the SEC would not qualify for award eligibility if the Commission determines that there is a separate whistleblower award scheme that "more appropriately applies to the enforcement action." The amendment would thus prohibit "double recovery" for a whistleblower trying to avail him or herself of more than one whistleblower program. ***Upward or Downward Adjustments in Monetary Awards*** The third proposed amendment promises to generate the most discussion and controversy, given the potential impact on monetary payouts to whistleblowers. First—and subject to the 30% statutory maximum—the proposed rules would authorize the Commission to adjust the award percentage *upward* in the context of potential awards that could yield a payout of $2 million or less to a whistleblower. The stated rationale for the change is that it would not only reward meritorious whistleblowers but also would ensure that future whistleblowers who might otherwise be concerned about the low dollar amount of a potential award still be incentivized to come forward. Second—and subject to the 10% statutory minimum—in the context of potential large awards that could yield total collected monetary sanctions of at least $100 million, the proposed rules would authorize the Commission to adjust the award percentage so that it would yield a payout that "does not exceed an amount that is reasonably necessary to reward the whistleblower and to incentivize other similarly situated whistleblowers." The proposed rule sets a floor at $30 million, such that in no event would the award for a tip that resulted in monetary sanctions of at least $100 million be below $30 million. ***Statutory Concern Raised by Stein*** In addition to concern about a subjective discretionary element being introduced into the SEC's determination of the

appropriate dollar amount of an award, Commissioner Stein's Statement cautions that, in her view, the proposed rule change appears inconsistent with the explicit statutory language in the Dodd-Frank Act. Stein notes that the Dodd-Frank whistleblower statute prohibits the SEC from taking into consideration the balance of the Investor Protection Fund ("IPF") in making a determination regarding an award amount. And while the proposed rule amendments echo this statutory prohibition ("the Commission shall not consider the balance of the [IPF]"), the proposed rule goes on to provide that "the Commission shall consider…the potential impact any adjustment might have on the IPF." Stein argues that it "is legalistic nonsense" and a "distinction without a difference" to suggest that the SEC may not consider the "balance" of the IPF but that it may consider the "impact" on the IPF when determining an adjustment to the size of an award. ***Next Steps*** The proposed rule amendments are now open for public comment and will remain so for the next 60 days. Given the popularity of the SEC's Whistleblower Program, the proposed rule changes—and particularly the changes that would impact large monetary awards—have already begun to generate commentary and concern. Since the inception of the Whistleblower Program through the end of fiscal year 2017, the Commission has received over 22,000 whistleblower tips. The Commission has obtained over $1.4 billion in financial remedies based on original information provided by whistleblowers.

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