

SEC Announces Whistleblower Award for Government Employee

By Douglas Paul, Richard Parrino, Emily Lyons, and Ann Koppuzha

On July 25, 2017, the Securities and Exchange Commission (SEC) announced that it would grant \$2.5 million “to an employee of a domestic government agency whose tip helped launch an SEC investigation and whose continued assistance enabled the SEC to address a company’s misconduct.” The government employee assisted the SEC by providing tips that led to the opening of the case, and by furnishing key documents and testimony. Importantly, the SEC indicated that the agency where the whistleblower worked had law enforcement responsibilities. The SEC’s order makes government employees eligible for whistleblower awards and creates both uncertainty and opportunity for a monetary award for government employees who may possess information relevant to SEC enforcement actions.

Background

Subject to certain exceptions, individuals are eligible for an award when they voluntarily provide the SEC with “original information that leads to a successful enforcement action.” Whistleblowers are eligible for 10 percent to 30 percent of the money collected when the monetary sanctions exceed \$1 million. According to the SEC, it has awarded \$156 million to 45 whistleblowers since inauguration of the program in July 2010. All awards are paid out of an investor protection fund established by Congress, which is funded by monetary sanctions paid to the SEC. Whistleblowers are not guaranteed a reward and must apply for the reward after the monetary sanction has been decided.

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Broad Interpretation of Government Employees Eligible for Whistleblower Awards

The July 25 order represents the first time that the SEC has announced a whistleblower award for a government employee. In a footnote in its July 25, 2017, Order Determining Whistleblower Award Claim, the SEC explained that federal, state, and local government employees are eligible for this award except when they work for (1) an “appropriate regulatory agency” or (2) “a law enforcement organization.” The Securities Exchange Act of 1934 (Exchange Act) defines an “appropriate regulatory agency” as the SEC and related banking agencies listed in the Exchange Act, including the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance Corporation.

The SEC relegated to a lengthy footnote the most complex part of its order, in which it indicated that although an employee of a law enforcement organization is not normally eligible as a whistleblower, there may be an exception when law enforcement is just one component of the agency’s purposes and the employee does not work for that component of the agency. According to the SEC, employees of law enforcement organizations—defined as organizations “having to do with the detection, investigation, or prosecution of potential violations of law”—are eligible for the award so long as they do not work for the “sub agency components that perform the law enforcement responsibilities.” The SEC cited Congress’s choice of the word “organization” instead of “agency” or “authority” in the Exchange Act as affording the SEC the opportunity to “interpret the exclusion flexibly.” Under the SEC’s reading, the law enforcement exception applies to agency components that perform law enforcement actions, not to all employees of an agency that “happens to have been

granted law enforcement powers among its many other separate responsibilities and powers.”

In this case, the employee did work for an agency that possessed law enforcement responsibilities, but the SEC still granted the award because the employee did not work in a law enforcement division of the organization. The SEC emphasized that this was not a situation in which the employee “sought to circumvent the potential responsibilities that his or her government agency might have to investigate.”

In its order, the SEC thus narrowed the definition of “law enforcement organization,” which in turn broadened the scope of government employees eligible for awards as whistleblowers. In its wake, the SEC left both opportunity for potential government-employee whistleblowers and ambiguity relating to the scope of the law enforcement exception.

Implications of SEC’s Order for Sharing of Information with Government Agencies

Despite speculation under the Trump Administration that the SEC was likely to

step away from enforcement and regulation, the agency’s grant of a whistleblower reward to a government employee demonstrates that the SEC will continue aggressively to use the whistleblower program to bring enforcement actions. It is once again encouraging those with relevant and reliable information, whether they work in the private or public sector, to come forward and cooperate with the SEC. Accordingly, companies should expect cooperation by whistleblowers to contribute to future SEC investigations and enforcement actions.

The order also reinforces the potential for information-sharing between government-agency employees and the SEC. Personal gain could motivate a government employee to pass along information to the SEC in hopes of receiving an award, especially if the reward encourages competition among government employees to provide information to the SEC. Companies that regularly work and communicate with regulatory agencies should consider the risk of sharing information that could serve as evidence of securities violations, particularly if the likely sanctions could exceed \$1 million, which is the threshold required to receive a whistleblower award.