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September 18, 2018

Via E-Mail to rule-comments@sec.gov

Mr. Brent Fields, Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: Whistleblower Program Rules, Exch. Act Rel. No. 83557, File No. S7-16-18

Dear Mr. Fields:

The Securities Industry and Financial Markets Association ("SIFMA")[1] appreciates the opportunity to comment on the Securities and Exchange Commission's ("SEC's" or "Commission's") proposed amendments to its Whistleblower Program Rules. SIFMA has supported and continues to support Congress' and the SEC's efforts to identify and address potential violations of the federal securities laws and regulations. SIFMA generally supported the SEC's current whistleblower rules when they were first proposed in 2010,[2] and SIFMA recognizes the value of robust and effective whistleblower rules.

SIFMA strongly encourages as the best practice for the SEC and other regulatory agencies periodically to conduct a retrospective review of their rules to evaluate whether they have been as effective and efficient as possible, and SIFMA applauds the SEC for doing so with respect to the whistleblower rules in such a timely fashion as the end of their first decade approaches. SIFMA is pleased that some of the negative consequences feared by critics of the original whistleblower rules – that they might undermine internal corporate compliance programs and encourage baseless complaints – appear to have been limited in practice. But we agree that it is always worthwhile to review whether changes are needed to preserve or improve upon the delicate balance intended by Congress and the Commission. In that spirit, SIFMA submits these

[1] SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry's nearly one million employees, we advocate on legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed income markets and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

[2] Letter from Ira D. Hammerman, Senior Managing Director and General Counsel, SIFMA to Ms. Elizabeth Murphy, Secretary, SEC re: Proposed Rules for Implementing the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934 (Dec. 17, 2010) (https://www.sec.gov/comments/s7-33-10/s73310-161.pdf).

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comments on the Commission's Proposing Release[3] concerning possible amendments to its current whistleblower rules (the "Proposed Rules").

I. Executive Summary

SIFMA supports many of the Commission's ideas set forth in the Proposing Release.

- SIFMA agrees that the definition of "action" triggering a potential whistleblower award should be expanded to include Non-Prosecution Agreements or Deferred Prosecution Agreements entered into with the US Department of Justice ("DOJ") or the SEC itself. These important prosecutorial tools should not deprive whistleblowers of an award where companies earn these resolutions through strong compliance programs, cooperation and substantial remediation.

- SIFMA finds merit in the Commission's idea that (within the statutorily mandated 10% minimum whistleblower award and the 30% maximum whistleblower award), some very large whistleblower awards could be reduced so as to increase the size of some of the smaller whistleblower awards.

- That being said, SIFMA is skeptical whether the Commission has legal authority to adopt a discretionary award program for whistleblowers who do not meet the statutory standards for a whistleblower award. There are strong policy reasons not to do so.

- SIFMA agrees that the Commission has inherent authority to sanction people who abuse the whistleblower program and waste both the Commission's and the regulated community's resources by filing baseless whistleblower claims.

- While SIFMA recognizes that the Commission must update its whistleblower rules to reflect the US Supreme Court's decision in the *Digital Realty Trust, Inc. v. Somers* case, SIFMA continues to believe that the first and best line of defense against violations of the securities laws is a robust internal compliance program responding to internal reporting of whistleblower claims. In the wake of *Digital Realty*, it is critical that the Commission strengthen its rules to maximize the incentives to encourage internal reporting of potential violations, and if necessary work with Congress to achieve that objective.

- SIFMA encourages the Commission to provide clear guidance about what language private sector firms may use in employment agreements, severance agreements and during internal investigations to protect nonpublic customer information and trade secrets and preserve firms' attorney-client privilege and work product protections, without running afoul of the whistleblower rules. The Commission has brought several settled enforcement actions in this area which have created a need for clearer industry guidance.

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[3] Exch. Act Rel. No. 83557 (June 29, 2018) (the "Proposing Release").

- SIFMA encourages the Commission to review whether the current provisions of the whistleblower rules relating to culpable participants, which in some cases permit awards to individuals who participated in the violations at issue, effectively achieve the goal of preventing misconduct in the first place.

II. SIFMA Supports Broadening the Definition of "Action" Triggering Potential Eligibility for a Whistleblower Award

The Proposing Release suggests allowing Non-Prosecution Agreements (NPAs) or Deferred Prosecution Agreements (DPAs) entered into with the DOJ or a state attorney general, or a similar cooperation-based resolution of an investigation with the SEC, to trigger eligibility for a whistleblower award.[4] SIFMA supports this proposal, and agrees with the Proposing Release that the Commission has statutory authority to adopt it. The DOJ has adopted guidelines that make corporations and individuals eligible for NPAs or DPAs if they have strong compliance programs and provide extraordinary cooperation in DOJ investigations.[5] NPAs and DPAs can involve monetary recoveries in the tens or even hundreds of millions of dollars – well over the $1 million threshold for a whistleblower award. In rare cases, the SEC has also utilized NPAs[6] or DPAs[7] for companies that have provided extraordinary cooperation in investigations.

The DOJ and the Commission have concluded, very reasonably, that providing incentives for strong internal compliance programs, cooperation during investigations and remediation furthers the nation's interest in preventing or detecting wrongdoing in the first place. NPAs and DPAs are effective tools for providing those incentives. At the outset of an investigation, it is impossible for a whistleblower to know if the investigation will result in a formal enforcement action or in a DPA or NPA.[8] SIFMA also believes it would be contrary to the public interest in encouraging vigorous compliance programs and extraordinary cooperation in investigations if the DOJ or SEC decided not to offer a company a DPA or an NPA, for fear that as a result, a whistleblower who contributed to the success of the investigation would not receive a

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[4] *See generally* Proposing Release at pp. 17-18.

[5] *See* US Attorney's Manual 9-47.120 (Mar. 2018) (https://www.justice.gov/criminal-fraud/file/838416/download) (announcing presumption of declination of prosecution in certain FCPA matters); Deputy Attorney General Rod Rosenstein, Remarks at the 32nd Annual ABA National Institute on White Collar Crime (Mar. 2, 2018) (https://www.justice.gov/opa/speech/deputy-attorney-general-rosenstein-delivers-remarks-32nd-annual-aba-national-institute) (discussing cooperation credit more generally).

[6] *See, e.g.*, SEC Announces Two Non-Prosecution Agreements in FCPA Cases (June 7, 2016) (https://www.sec.gov/news/pressrelease/2016-109.html).

[7] *See, e.g.*, Regions Financial Corporation (June 25, 2014) (https://www.sec.gov/news/press/2014/2014-125-dpa.pdf). *See generally* Securities and Exchange Commission, Enforcement Cooperation Program (listing SEC DPA and NPA agreements) (https://www.sec.gov/spotlight/enforcement-cooperation-initiative.shtml).

[8] In statutory terms, SIFMA agrees with the Proposing Release that both a DPA and an NPA comfortably fit within the definition of a "covered action" in Section 21F of the Securities Exchange Act of 1934 ("Exchange Act"), so there is no legal obstacle to the SEC's proposed change in the regulatory definition to include these types of actions.

whistleblower award. Similarly, it is unfair to whistleblowers who provide timely information about potential misconduct to be deprived of an award simply because of positive conduct by the very entities on which they are reporting. Allowing awards to whistleblowers whose information leads to a successful DPA or NPA will fairly balance the important goals of both rewarding whistleblowers, and also encouraging companies to adopt effective compliance programs and to cooperate fully during investigations in the hope of obtaining a DPA or NPA.

III. SIFMA Supports Giving the Commission the Ability to Adjust Whistleblower Awards Based on Size

A. Adjusting Whistleblower Awards Based on Size

The Proposing Release suggests giving the Commission the discretion to adjust upward some whistleblower awards less than $2 million, and to adjust downward some whistleblower awards in cases involving recoveries greater than $100 million (but always within the 10% minimum floor and 30% maximum ceiling set by the statute).[9] SIFMA supports this proposal. The whistleblower program is effective if it provides potential whistleblowers with a sufficient incentive to take the risks involved in coming forward. SIFMA agrees with the Proposing Release that awards over $30 million (the maximum award in a case with a recovery over $100 million) provide little marginal incentive for a whistleblower to come forward; individuals who win awards over that amount should be financially secure for the rest of their lives. It is simply not necessary to pay a whistleblower $45 million (instead of $30 million) to convince that person to come forward in the first place, particularly when the amount of a potential penalty is virtually impossible for a whistleblower to predict in the first place.[10]

By contrast, a whistleblower who receives an award of less than $2 million may have taken substantial career and personal risks for an award amount that (while generous) still likely requires them to find future employment under difficult circumstances. Because award amounts are inherently uncertain, a whistleblower might well choose not to come forward if he or she did not think the likely award would be sufficient to warrant the risk, and increasing that person's potential award might make the difference in convincing that person to become a whistleblower in the first place. SIFMA believes that providing a marginally greater incentive to whistleblowers at the lower end of the award scale (and funding that incentive through a marginal reduction in the payouts at the very highest end of the scale) is a beneficial tradeoff that, among other things, would produce the most valuable mix of whistleblower tips to the Commission's enforcement program.

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[9] *See generally* Proposing Release pp. 43-44.

[10] Awards substantially over $30 million also create a potential public perception of "jackpot justice" that may harm the overall credibility of the Commission's enforcement program.

B. Discretionary Awards Not Involving A "Covered Action" or "Original Information"

The Proposing Release also seeks comment on the concept of a discretionary whistleblower awards to individuals whose tips do not involve a "covered action" or "original information" or that result in a sanction that cannot be collected.[11] SIFMA's view is that the Commission does not currently have statutory authorization to make discretionary awards to individuals whose tips do not meet the standards set forth in Section 21F of the Exchange Act. As the Proposing Release itself explains, Congress made specific policy determinations when it required whistleblowers to provide "original information" and not just "public information" to be eligible for an award.[12] SIFMA does not believe the Commission should (or is permitted to) overturn unilaterally Congress' determination on this matter; if the SEC believes that Section 21F strikes the wrong balance, then it should ask Congress to amend the statute.

Similarly, SIFMA believes that Congress made a specific set of policy determinations when it defined a "covered action" eligible for an award. In particular, Congress made a considered determination to create incentives for whistleblowers to provide information about serious violations which would result in recoveries over $1 million. In the wake of the financial crisis, Congress wanted the SEC and DOJ to focus on potential large frauds, given their limited resources, and not to waste time and effort on insignificant violations.

Congress understood the costs and burdens that SEC and DOJ investigations impose on SEC-regulated firms, and desired that firms only incur those costs when there is a likelihood of finding a significant violation as a result. For smaller matters, it is better for firms to handle those matters internally and remediate themselves or in the context of the examination program, which is far less expensive and more efficient for the Commission. Encouraging reporting of minor violations by whistleblowers is, therefore, not good policy. Statistics from the SEC Whistleblower Office do not substantiate a need to increase incentives for reporting minor violations. On the contrary, the office's most recent annual report indicates that the number of whistleblower tips has grown to over 4,400 per year, an increase of almost 50% per year since the program began.[13]

For the reasons discussed above, SIFMA does not believe the SEC should (or can) unilaterally overturn the statute's carefully constructed balance in defining the eligibility for whistleblower awards, nor do we believe there are compelling policy arguments to do so.[14]

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[11] *See generally* Proposing Release at p. 110. Notably, the Proposing Release does not actually propose a rule to create such a discretionary awards program.

[12] *See* Proposing Release at pp. 98-102.

[13] SEC Office of Whistleblower, 2017 Annual Report to Congress ("2017 Annual Report") at p. 23 (https://www.sec.gov/files/sec-2017-annual-report-whistleblower-program.pdf).

[14] SIFMA notes that the Anti-Deficiency Act, 31 U.S.C. § 1341, prohibits federal agencies from making expenditures of federal funds without congressional authorization. Creating a discretionary awards fund (and

IV. The Commission Can and Should Sanction Individuals Who Make Abusive Whistleblower Claims

The Commission suggests in the Proposing Release (at pp. 76-79) strengthening the Commission's authority to sanction claimants who submit false information or otherwise abuse the whistleblower process.[15] The Commission states in the Proposing Release that a small number of claimants have made frivolous claims (often on a repeated basis), and thus have diverted SEC staff attention away from potentially meritorious cases.[16] SIFMA agrees that the SEC can and should sanction individuals who abuse the Commission's processes in this way. SIFMA observes that in addition to wasting the SEC staff's time and attention, such meritless claims also can waste substantial amounts of time, money and attention at private-sector firms registered with or regulated by the SEC, which must respond to sometimes expensive and burdensome enforcement inquiries based on those abusive claims.

The courts have long held, in the context of what is now SEC Rule of Practice 102(e), that the Commission has inherent authority to sanction individuals who abuse the Commission's processes.[17] The same logic that applies to professionals who appear before the SEC should apply to purported whistleblowers who abuse the Commission's processes. The Commission has inherent authority to sanction individuals who make abusive whistleblower claims, and it should not hesitate to use that authority. The Commission should not allow a small number of mostly repeat offenders to hijack what has otherwise been a generally effective whistleblower program.

V. The Commission Should Review Its Rules to Encourage Whistleblowers to Report Violations Internally

The Proposing Release suggests amending Exchange Act Rule 21F-2 to reflect the holding of the US Supreme Court in *Digital Realty Trust, Inc. v. Somers*, 138 S. Ct. 767 (2018), that someone who reports a potential securities law violation internally to an employer, but does not report that violation directly to the Commission itself, does not qualify as a "whistleblower" for the purposes of Section 21F of the Exchange Act.[18]

SIFMA has long been concerned that the whistleblower rules should encourage internal corporate compliance reporting systems, which are a critical component of what the Commission

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making payments out of that fund) without any legislative authorization or appropriation would present significant concerns under the Anti-Deficiency Act.

[15] *See generally* Proposing Release at pp. 76-79.

[16] *Id.*

[17] *See, e.g., Touche Ross & Co. v. SEC*, 609 F.2d 570, 578 n.13 (2d Cir. 1979); *accord Sheldon v. SEC*, 45 F.3d 1515, 1518 (11th Cir. 1995); *Checkosky v. SEC*, 23 F.3d 452, 455-56 (D.C. Cir. 1994); *Davy v. SEC*, 792 F.2d 1418, 1421 (9th Cir. 1986); *see also Polydoroff v. ICC*, 773 F.2d 372 (D.C. Cir. 1985) (upholding ICC's inherent authority to sanction individuals who appear before it).

[18] *See generally* Proposing Release at pp. 60-62.

has recognized is the first and most important line of defense against securities law violations.[19] Internal corporate compliance reporting systems are particularly important in the financial services industry, and the industry has spent billions of dollars developing and improving these systems. Indeed, the desirability of encouraging internal reporting to corporate compliance programs was the primary theme of SIFMA's 2010 comment letter on the original whistleblower rules. Whistleblower complaints generally can be resolved most quickly, effectively and efficiently by allowing the company itself to investigate and respond in the first instance (although in many cases the SEC staff then will want to validate the conclusions of the company's internal investigation). The result of the decision in *Digital Realty* – that whistleblowers must report directly to the Commission so as to be treated as a whistleblower – is directly contrary to the goal of encouraging internal reporting.

SIFMA recognizes that the Commission has no alternative but to recognize the Supreme Court's decision in *Digital Realty*. At the outset of the program, the Commission recognized the critical importance of encouraging whistleblowers to use their internal compliance programs.[20] That being said, SIFMA urges the Commission to think broadly about how it can provide additional incentives to encourage the use of internal reporting systems. SIFMA appreciates that in the current whistleblower rules, the Commission has provided explicitly that voluntary internal reporting can increase the amount of an award, and interfering with internal compliance and reporting systems can decrease the amount of an award – provisions that are legally unaffected by the Supreme Court's decision. Practically, however, SIFMA fears that the *Digital Realty* decision will have a major impact on the incentives the Commission intended to create.[21]

To mitigate the harm to compliance programs that may result from *Digital Realty*, SIFMA suggests that the Commission consider an explicit program providing that in appropriate cases, that the Commission staff give a company an opportunity to conduct its own internal investigation of whistleblower allegations (even if in coordination with the staff) and report the results, before the Commission staff takes substantial investigative steps. If a whistleblower goes directly to the Commission without using corporate internal reporting channels (because of *Digital Realty*), in appropriate cases the Commission should allow the company to investigate the potential misconduct in the first instance.[22] Such a policy would encourage strong internal

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[19] *See e.g.*, Adopting Release, Implementing Whistleblower Provisions of Section 21F of the Securities Exchange Act, Exch. Act Rel. No 64545, at p. 90 (May 25, 2011) ("2011 Adopting Release") (https://www.sec.gov/rules/final/2011/34-64545.pdf) ("compliance with the federal securities laws is promoted when companies have effective programs for identifying, correcting, and self-reporting unlawful conduct by company officers or employees").

[20] *See, e.g.*, Opening Statement of Chairman Mary L. Schapiro, Whistleblower Program (May 25, 2011) (https://www.sec.gov/news/speech/2011/spch052511mls-item2.htm) ("But, perhaps, no issue received more focus during this process than the role of internal compliance programs. As I have often said, internal compliance programs play an extremely valuable role in the fraud prevention arena.").

[21] The most recent SEC Office of the Whistleblower Annual report states that 83% of tips received by the Commission first had been reported internally. 2017 Annual Report at p. 17.

[22] SIFMA recognizes that in some circumstances in which a firm's senior executives are an integral part of an intentional fraudulent scheme, it would not be appropriate to notify the company before the SEC staff began its own

corporate compliance and investigative programs and would maximize the Commission's own investigative resources. The Commission should consider additional and more explicit incentives for internal reporting – whether before or, at least simultaneous with, reporting to the Commission. For example, remediation resulting from a whistleblower's internal complaint could be used as a factor to drive the award up to 30%. Without additional incentives, SIFMA fears the result of *Digital Realty* may be to undermine compliance programs.

SIFMA also suggests the Commission consider addressing the holding in *Digital Realty* with Congress. The case was decided on pure statutory analysis grounds, so Congress maintains the authority to amend the statute in response to the decision. The precise scenario at issue in *Digital Realty* was the controversial issue of anti-retaliation protection. Congress could restore award eligibility to whistleblowers who report through internal compliance programs.[23] Such a step would achieve the SEC's original goal, which SIFMA strongly supports, of encouraging whistleblowers to use internal reporting channels where they are available and effective.

VI. The Commission Should Provide Clearer Guidance About Permissible Terms in Employment and Severance Agreements and Disclosures to Employees During Internal Investigations

Exchange Act Rule 21F-17(a) prohibits employers from taking actions that impede their employees from reporting potential securities law violations to the Commission. SIFMA supports the intent of this rule – clearly (for example) an employee severance agreement that purports explicitly to forbid an employee from reporting potential misconduct to the SEC should not be permitted. The Commission, however, has brought a series of enforcement actions under this rule (all of which were settled, and thus of limited precedential value), and those enforcement actions have created substantial uncertainty in the regulated community about what is permissible conduct.[24] Some of those enforcement actions involve conduct that (on their face – SIFMA recognizes that settlements are negotiated documents) does not appear to involve obvious violations of the rule. SIFMA urges the Commission to provide clear guidance (with an opportunity for the regulated community to provide input on that guidance) about what types of provisions the Commission believes are permissible and not permissible in this area. This area is an example where the regulated community would welcome the Commission's guidance. The

investigation. Although the SEC must always be aware of the potential for these types of situations, SIFMA believes them to be exceptional.

[23] Included as Appendix A is proposed statutory language to accomplish this step. The proposed language would add to Section 21F(a)(6), the statutory definition of "whistleblower", language adapted from the current Exchange Act Rule 21F-4(b)(7), which includes internal whistleblowers within the coverage of the award scheme so long as they subsequently report to the Commission.

[24] *See* Securities and Exchange Commission, Office of the Whistleblower, Enforcement Actions Based on Actions to Impede Reporting (https://www.sec.gov/whistleblower/retaliation#protections).

SEC staff has provided guidance to employees about the anti-retaliation provisions,[25] and SIFMA suggests that the Commission or its staff provide similar guidance to regulated entities.

There are strong and legitimate reasons that firms need to protect confidential information from being disclosed to third parties. For example, the safeguarding provisions of Regulation SP require firms to take reasonable steps to protect the non-public financial information of customers.[26] As a result, financial services firms typically, in employment agreements and severance agreements as well as in employee codes of conduct, restrict employees' ability to disclose nonpublic customer financial information to third parties, or to retain that information when they leave their firm. Similarly, for the legitimate purpose of preserving intellectual property rights protected by federal and state law, financial services firms generally forbid their employees from misappropriating the firm's trade secrets, or from misappropriating firm information protected by copyright, trademark, patent and other intellectual property doctrines. In many cases, the firms might lose some or all of those intellectual property protections if they do not take reasonable steps to protect that information, including by informing employees of the firm's rights (and the employee's lack of rights) to that information.[27]

When conducting internal investigations of potential misconduct or in anticipation of potential litigation, firms also have legitimate attorney-client privilege and attorney work-product protections recognized by the US Supreme Court in cases such as *Upjohn Co. v. United States*, 449 U.S. 383 (1981), and *Hickman v. Taylor*, 329 U.S. 425 (1947). The preservation of these protections, however, depends in part on the firm adequately informing employees who are asked to participate that the investigation is confidential and privileged and that the employees should treat it as such.[28]

In short, there are a variety of situations in which firms regulated by the SEC can and should inform employees that certain information belongs to the firm and not to the employee, and that the employee cannot (either during or after their employment) disclose that information to third parties. These warnings are not intended to chill the ability of current or former employees to disclose potential violations of the securities laws to the SEC or other regulators. Yet some of the SEC's enforcement actions in the anti-retaliation area have alleged (again, in negotiated

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[25] *See* Securities and Exchange Commission, Office of the Whistleblower, Protections Against Retaliation, Frequently Asked Questions (https://www.sec.gov/whistleblower/retaliation#protections).

[26] *See* 17 C.F.R. § 248.30.

[27] In *Anheuser-Busch InBev SA/NV*, Exch. Act Rel. No. 78957 (Sept. 28, 2016), the Commission sanctioned a company for using form confidentiality provisions in severance agreements which did not mention communications with the SEC, but had been designed to prevent employees from disclosing confidential customer information or trade secrets. The order found that one employee had interpreted the agreement to apply to communications with the SEC, but did not allege that the company had intended to prevent communications with the SEC.

[28] *See, e.g., KBR, Inc*. Exch. Act Rel. No. 74619 (Apr. 1, 2015) (sanctioning issuer for confidentiality warning during internal investigation, despite the fact that the instructions did not direct the employees not report misconduct to the SEC, and lack of any evidence that any employee in fact was deterred from reporting to the SEC or that the company sought to use the warning to prevent employees from reporting to the SEC).

settlements which lack precedential value) that general warnings of the duty not to disclose confidential information could in some way, to employees who are not legally sophisticated, chill those employees' ability to disclose potential misconduct to the SEC in violation of Exchange Act Rule 21F-17(a).[29]

SIMFA believes that this area – the conflict between firms' legitimate desire to protect customer and firm information, and employees' legitimate desire to be able to report whistleblower concerns – is an example where the regulated industry would happily follow whatever guidance the SEC would provide. But because to date the SEC has not provided clear guidance consistent with its rules, firms have been left to grapple with uncertainty when drafting basic documents such as employment agreements, severance agreements, employee handbooks or codes of conduct, and warnings for internal investigations.

SIFMA urges the Commission or its staff to provide guidance about contract terms and policy provisions that they believe do and do not comport with Exchange Act Rule 21F-17(a). Ideally, the Commission or its staff should provide an opportunity for notice and comment on this guidance, so that the regulated community may provide input to the Commission on the types of warnings that should be permissible (or even required), and are not likely to mislead employees about their whistleblower rights and protections, given firms' need to protect confidential information. Uncertainty in this area poses a significant cost to the regulated community, which is exactly what careful regulatory guidance can prevent. SIFMA believes that providing greater certainty in this area would promote better compliance on the part of the regulated industry, and would protect both firms and employees from inadvertent violations.

VII. The Commission Should Review Whether Its Rule Provisions Concerning Culpable Whistleblowers Are Contributing to Additional Violations

In our 2010 comment letter, SIFMA argued that culpable employees – employees who had participated in a securities law violation – should not be eligible to profit from that violation through making a whistleblower complaint. SIFMA's view was based on the common sense notion that crime should not pay – the Commission should not provide financial incentives through which individuals can profit from their own misconduct. In its final version of the whistleblower rules, the SEC took a different view. The current Exchange Act Rule 21F-16 provides that if an individual "substantially directed, planned, or initiated" the misconduct, then sanctions imposed for that misconduct will not count toward the $1 million threshold for a "covered action," but for other individuals, Exchange Act Rule 21F-6(b) provides that culpable misconduct will count only as a potential negative factor in calculating the amount of their award (subject to the 10% statutory floor). As the Adopting Release for the original whistleblower

[29] In no way does SIFMA endorse or defend the steps alleged to have been taken in some other enforcement actions, such as *Homestreet, Inc*., Exch. Act Rel. No. 79844 (Jan. 17, 2017), in which the company was alleged to have used severance or indemnity agreements actively to impede whistleblowers from communicating with the SEC.

rules acknowledged, the culpable participant provisions were among the most controversial portions of the rules.[30]

There are legitimate questions whether the current rules regarding culpable whistleblowers are working as intended, because of the lack of public information available regarding this aspect of the program. When wrongdoers themselves go to the Commission rather than to internal compliance programs, there is a substantial cost on firms imposed by the very people whose conduct may be at issue. Indeed, regulated entities are concerned that low-level conduct of which they are not made aware deprives them of immediate opportunities to remediate before the conduct gets worse, with the potential result that the wrongdoer can benefit.[31] This is not what SIFMA thinks Congress or the Commission meant to encourage.

SIFMA suggests that the Commission review and report publicly on whether the culpable participant portions of the whistleblower rules are working as intended. The current Proposing Release does not address this issue at all. Section 21F(h)(2) of the Exchange Act and Exchange Act Rule 21F-7 require that the Commission keep whistleblower submissions confidential, even at the award stage. As a result, there is no public transparency concerning whether the Commission is making awards to culpable whistleblowers, whether the Commission is making downward departures as anticipated pursuant to Exchange Act Rule 21F-6(b), whether making culpable participants eligible for awards is allowing the SEC staff to find misconduct that would otherwise remain undetected, or whether the culpable participant provisions are in fact providing an incentive for individuals to join in misconduct or to allow misconduct to continue.

SIFMA continues to believe that allowing individuals to be rewarded for misconduct in which they took part creates a very dangerous set of incentives. Because of the lack of public transparency in the whistleblower award process, SIFMA cannot evaluate how serious that problem may be – therefore we believe it is incumbent upon the Commission to review that issue. There should be objective metrics that can reveal how this aspect of the program is operating, while protecting the identity of individual whistleblowers. If the Commission will not report on its awards to culpable whistleblowers, then Congress should consider oversight hearings. Financial awards to people who participate in violations of the securities laws have the potential to erode public trust in the fair administration of those laws, and the Commission or Congress should provide assurance that the current rules rewarding culpable employees are not subject to abuse.

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SIFMA appreciates the opportunity to submit this comment letter on these important issues. We would be happy to meet with the Commission staff to discuss the issues in this letter. Please contact me at [redacted] or Bernard V. Canepa, Vice President and Assistant General

[30] *See* 2011 Adopting Release at p. 192.

[31] *See* Exch. Act Rel. No. 84125 (Sept. 14, 2018), in which a whistleblower received an award (although the amount of the award was reduced), despite having unreasonably delayed in reporting the misconduct to the Commission with the result that the misconduct grew larger and the amount of the sanction increased.

Counsel at [redacted], or our outside counsel at Sidley Austin LLP, W. Hardy Callcott at [redacted], or Stephen Cohen at [redacted], if you have any questions or would like to discuss these issues further.

Respectfully submitted,

Ira D. Hammerman
Executive Vice President and General Counsel

cc: Chairman Jay Clayton
Commissioner Kara M. Stein
Commissioner Robert L. Jackson
Commissioner Hester M. Peirce
Commissioner Elad L. Roisman

Appendix A:

Suggested statutory amendment to restore whistleblower award eligibility to internal whistleblowers. Add, at the end of Section 21F(a)(6) of the Exchange Act:

> If an individual provides information pursuant to an entity's internal whistleblower, legal, or compliance procedures for reporting allegations of possible violations of law, and the individual, within 120 days, submits the same information to the Commission, then, for purposes of evaluating the individual's claim to an award under Section 21F(b) of this chapter, the Commission will consider that the individual provided information as of the date of the individual's original disclosure, report or submission made pursuant to those internal procedures.