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Ms. Elizabeth M. Murphy, Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: Comments on Proposed Dodd-Frank Act Whistleblower Rules (File No. S7-33-10)

Dear Ms. Murphy:

Foster Wheeler appreciates the opportunity to provide comments to the Securities and Exchange Commission (the "Commission") on its proposed rules on the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank" or the "Act") whistleblower provisions.

The Commission has indicated that it is seeking the appropriate balance between motivating whistleblowers to provide it with quality information against the need to ensure that companies maintain strong internal corporate compliance processes. This is a laudable objective, but we are concerned that the Commission's proposed rules do not strike the proper balance and that they favor obtaining information at the expense of undermining effective internal compliance processes. Moreover, the proposed rules do not ensure that the Commission will receive high-quality information; to the contrary, they provide incentives for whistleblowers to provide information to the Commission as quickly as possible, without giving companies' internal compliance personnel the opportunity to address the allegations. Although the proposed rules preserve a whistleblower's status as the original source of information after reporting violations internally, they do not provide any concrete incentives for whistleblowers to report violations through internal compliance programs before bringing them to the Commission. To the contrary, with a minimum five-figure award at stake, whistleblowers are given ample incentives to bypass internal reporting systems, which could considerably weaken compliance programs.

A more appropriate way to achieve the balance that the Commission is seeking would be to require whistleblowers to utilize internal compliance procedures before reporting potential violations to the Commission. We recommend adopting rules modeled after the Sarbanes-Oxley requirements that auditors first report violations internally and the Commission's similar rules defining attorneys' reporting obligations after discovering violations. At a minimum, we suggest

making it mandatory for the Commission to consider whether a whistleblower has utilized internal compliance structures in determining the amount of an award.

I. The proposed rules do not provide incentives for whistleblowers to utilize internal reporting and compliance programs.

The proposed rules do provide some allowance for internal corporate reporting mechanisms, but they do not go far enough in doing so. For example, proposed rule 21F-4(b)(7) provides that a whistleblower will be considered an original source of information — and thus eligible to receive an award — if he or she provides information on a potential violation to internal corporate compliance personnel or another corporate employee expected to report the information, provided that the whistleblower submits the necessary forms to the Commission within 90 days. The Commission explains in its release that "the objective of this provision is to support, not undermine, the effective functioning of company compliance and related systems by allowing employees to take their concerns about potential violations to appropriate company officials first while preserving their rights under the Commission's whistleblower program."[1] However, under proposed rule 21F-4(b)(7), whistleblowers have every incentive to bypass internal company compliance programs and take their information directly to the Commission. Even with the assurance that the Commission will consider the date of the whistleblower's report through internal company systems as the effective date of his or her submission to the Commission, a whistleblower is unlikely to voluntarily risk reporting information that could be worth tens of millions of dollars to anyone at a company that he or she believes is violating the law.[2]

The proposed rules also do not require the Commission to consider whether a whistleblower has utilized internal compliance procedures in determining the size of an award. In its release, the Commission notes that it may consider "whether, and the extent to which, a whistleblower reported the potential violation through effective internal whistleblower, legal or compliance procedures before reporting the violation to the Commission."[3] However, the use of internal reporting systems is not required for a whistleblower to be eligible for an award greater than the statutory minimum of 10 percent, and there is no penalty for whistleblowers who do not utilize internal compliance programs before going to the Commission. Moreover, this suggested factor is not even mentioned in the proposed rules — it is relegated to the release as one of eleven factors that the Commission may (or may not) take into account. In light of the fact that the use of internal compliance systems is not a mandatory factor for the Commission to consider and is not even addressed in the proposed rules, it is unlikely that a whistleblower would find any benefit to using internal compliance systems.

The exclusions provided in the proposed rules are not sufficient to protect internal compliance programs. For example, proposed rule 21F-4(b)(4) excludes certain employees with compliance roles, including attorneys, auditors, and other compliance personnel, from being

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[1] Release No. 34-63237, at 33-34 (hereinafter "Release").

[2] Corporate counsel have noted this concern. For example, Kenneth Grady, general counsel at Wolverine World Wide Inc., has asked "Which do you think is going to win — an internal whistleblower program that relies on trust or one that offers a huge financial bounty?...For a whistleblower, it's a no brainer." Quoted in Ashby Jones and Joann S. Lublin, Critics Blow Whistle on Law, Wall Street Journal, Nov. 1, 2010.

[3] Release at 51.

eligible for awards in most cases. The Commission indicates that the rationale for these exclusions is "the concern that Section 21F not be implemented in a way that would create incentives for persons who obtain information through such functions, as well as other responsible persons who are informed of wrongdoing, to circumvent or undermine the proper operation of the entity's internal processes for responding to violations of law."[4] The proposed rules, however, would allow such persons to be considered whistleblowers if the company does not disclose information obtained through its compliance program to the Commission within a reasonable time or if it proceeded in bad faith. These exclusions are sound in principle, but they do not go far enough to protect corporate compliance programs because they do not create any incentives for non-compliance personnel to use internal reporting mechanisms.

II. The proposed rules will weaken internal compliance programs.

In its release, the Commission notes that it considered "requiring potential whistleblowers to utilize in-house complaint and reporting procedures," but rejected this approach because some employers do not have sufficient compliance processes. If the Commission is concerned that some companies do not have sufficient compliance processes, we believe that the proposed rules will only exacerbate the problem. Moreover, the Commission's proposed rules do not provide any incentives for companies to strengthen their internal compliance programs. To the contrary, the proposed rules may well weaken compliance programs, many of which the Commission describes as "well-documented, thorough, and robust."

Because they do not impose requirements or provide incentives for whistleblowers to report violations internally, the proposed rules will undermine internal compliance programs.[5] As noted above, the proposed rules create incentives for whistleblowers to take their concerns directly to the Commission without utilizing internal compliance programs. Companies that have committed considerable time and resources to implementing and maintaining such programs will find that those programs may no longer be providing vital feedback regarding conduct that is occurring within the company. One important function of compliance programs is monitoring employee conduct and adjusting internal controls and training programs as necessary. The Commission clearly has a role to play in cases where a violation has actually occurred, and these issues are appropriately addressed through enforcement proceedings. However, internal compliance personnel are in a much better position than the Commission to address conduct that does not yet rise to the level of a violation and the proposed rules effectively cut off the major source of information for these programs, thereby undermining internal responses. Indeed, the proposed rules seem to create an incentive for an employee who

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[4] Release at 24.

[5] A range of commentators have suggested that the proposed rules will undermine compliance programs. For example, the Wall Street Journal quoted David Hirschmann of the U.S. Chamber of Commerce as stating that "The SEC has long advocated for corporate compliance programs, but this whistleblower-bounty program would essentially eviscerate them." Jessica Holzer and Ashby Jones, SEC Proposes Rules for Bounty Program, Wall Street Journal, Nov. 4, 2010, *available at* http://online.wsj.com/article/SB10001424052748703506904575592533100919998.html#articleTabs%3Darticle (last accessed Dec. 2, 2010). The New York Times quoted Harvey L. Pitt, a former chairman of the S.E.C., as stating that Dodd-Frank "contains the seeds for undermining corporate governance and internal compliance systems." Edward Wyatt, For Whistle-Blowers, Expanded Incentives, N.Y. Times, Nov. 14, 2010, *available at* http://www.nytimes.com/2010/11/15/business/15whistle.html?ref=securities_and_exchange_commission (last accessed Dec. 7, 2010).

is aware of a compliance issue to sit on the information until the problem ripens into a violation serious enough to justify a higher award. This may result in an increased number of serious violations — problems that could have been addressed early when they were small and manageable may fester and become major violations.

Allowing whistleblowers to take their complaints directly to the Commission without giving the company an opportunity to review the allegations would potentially narrow the scope of internal compliance programs and put them into a purely reactive mode. Internal compliance programs are appropriately scaled to resolve a variety of whistleblower complaints, some of which may be based on simple misunderstandings of the facts or the law. These programs are able to handle such complaints without expending unnecessary resources. On the other hand, if these matters are automatically forwarded to the Commission, then companies could suddenly find themselves faced not with an easily resolved complaint but with an investigation by the Commission, which will require far more time and effort to resolve — even for complaints that are unsubstantiated.

Internal compliance programs also play a prophylactic role. In addition to addressing actual and potential violations, they also enable compliance personnel to monitor and address areas of risk before actual violations occur. Internal compliance personnel and outside counsel use information obtained through compliance systems to create new employee training programs and implement other initiatives to promote compliance with securities laws. If the flow of information from employees is disrupted, then compliance programs will become less dynamic and therefore less effective in addressing any actual control issues within the company. As a result, the proposed rules could actually lead to an increased number of violations.

III. Recommendation: Require whistleblowers to use internal compliance programs before reporting potential violations to the Commission or, at a minimum, require the Commission to consider this as a factor in determining the amount of an award.

The Commission could address the concerns discussed above and strike the balance it is seeking by making a whistleblower's use of internal corporate compliance procedures a condition of eligibility for an award. Such a requirement would further the Act's overarching purpose of protecting investors[6] by ensuring that internal compliance programs will continue to function as the first line of defense against securities violations that could be harmful to investors.

We recommend that the Commission adopt rules modeled after section 10A of the Securities Exchange Act[7] and the Commission's rules pertaining to attorneys who represent issuers of securities.[8] Under Section 10A, if a registered public accounting firm conducting an audit required under the Securities Exchange Act discovers a potentially illegal act, the accounting firm is required to notify the company's audit committee or board of directors.[9] If

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[6] For example, the Senate Banking Committee Report indicates that "enhancing consumer and investor protections" is one of the main purposes of the Act. S. Rep. No. 111-176, at 2.
[7] *See* 15 U.S.C. § 78j-1.
[8] *See* 17 C.F.R. § 205.3.
[9] 15 U.S.C. § 78j-1(b)(1).

the accounting firm is not satisfied with the company's response, it is required to submit a report to the board of directors.[10] The company is required to provide notice to the Commission and furnish a copy of the notice to the accounting firm within one business day of receiving such a report. If the accounting firm does not receive such notice within one business day, it is required to provide a copy of its report to the Commission.[11] Similarly, the Commission's rules applicable to attorneys who represent issuers of securities require attorneys to report evidence of material violations of securities laws to the company's chief legal officer.[12] If the chief legal officer determines that a violation is occurring or has occurred, he or she is required to cause the issuer to "adopt an appropriate response." If he or she determines that there has not been a violation, the chief legal officer must notify the reporting attorney of this conclusion.[13] If the reporting attorney is not satisfied with the chief legal officer's response, he or she is required to report the violation to the company's board of directors, or the appropriate committee thereof.[14]

The frameworks provided by Section 10A of the Securities Act and Rule 205.3 could be easily adapted to apply to internal reporting requirements for whistleblowers under Dodd-Frank. We recommend the following system:

- Require whistleblowers to report complaints through their company's internal compliance program before raising the issue with the Commission. (If the company has no mechanism through which to report violations, then this condition will not apply.)

- Require the company to make a determination of whether the complaint is well-founded within 90 days of receiving such a complaint.

- After the 90 days, the company should be required to inform the whistleblower of its determination and any remedial action being taken. If the whistleblower disagrees with the company's finding or believes the remedial action being taken is not sufficient, he or she may submit his or her complaint to the Commission. When the whistleblower submits the complaint to the Commission, he or she should be required to certify, under penalty of perjury, that he or she has given careful consideration to the company's response but still has reason to believe that there has been a violation.

- If the company reports the violation to the Commission before the end of the 90-day period, it should be required to disclose the name of the whistleblower who brought the original complaint. And if the information provided to the company by the whistleblower was original information, then the whistleblower should still be eligible for the bounty.

- If the information provided by the whistleblower leads to a successful enforcement action, the Commission should take the company's response to the

[10] 15 U.S.C. § 78j-1(b)(2).
[11] 15 U.S.C. § 78j-1(b)(3), (4).
[12] 17 C.F.R. § 205.3(b)(1).
[13] 17 C.F.R. § 205.3(b)(2).
[14] 17 C.F.R. § 205.3(b)(3).

complaint into account. Cooperation credit could be given when a company forwards the complaint to the Commission. This would provide companies with an incentive to take well-founded complaints seriously.

This suggested framework provides incentives for employers to maintain robust internal compliance programs and is consistent with Dodd-Frank, which vests the Commission with substantial discretion in determining eligibility for awards.[15] Exercising that discretion, the Commission has already provided several restrictions on eligibility for an award which, while not included in Dodd-Frank, are consistent with the Act.[16]

We also recommend that proposed rule 21F-6 be modified to require the Commission to consider the extent to which a whistleblower used an internal compliance program in determining the amount of an award. As discussed above, this factor is currently only included in the accompanying release; it is not mentioned in the proposed rules. As was true with the proposed internal reporting requirement, requiring the Commission to consider the whistleblower's use of internal compliance programs would be consistent with Dodd-Frank. Section 922(c)(1) of the Act provides that the amount of an award "shall be in the discretion of the Commission." In addition to the three specific criteria listed, Dodd-Frank requires the Commission to consider "such additional relevant factors as the Commission may establish by rule or regulation" in determining the amount of an award.[17] This is clearly an invitation by Congress for the Commission to establish other mandatory or discretionary criteria. Moreover, if the Commission clearly states that it will consider a whistleblower's use of internal compliance programs in determining the amount of an award, whistleblowers will have some incentive to utilize internal compliance programs. This would help to ensure that internal compliance programs — which the Commission describes as "play[ing] a role in preventing and detecting securities violations that could harm investors" — do not fall into a state of disrepair. Keeping these programs viable will protect investors from securities violations, which is one of the primary goals of Dodd-Frank.

Conclusion

The proposed rules fail to achieve an appropriate balance between encouraging potential whistleblowers to provide quality information to the Commission and ensuring the preservation of internal compliance programs. Under the proposed rules, there is a significant monetary incentive for whistleblowers to bypass internal corporate reporting mechanisms and report information as quickly as possible to the Commission. By contrast, there are no countervailing requirements or incentives for whistleblowers to utilize internal compliance structures. This skewing of incentives may undermine the very compliance programs that the Commission is

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[15] The Commission's broad discretion in determining eligibility is evident throughout section 922 of the Act. For example, a person must provide information to the Commission "in a manner established, by rule or regulation, by the Commission." Dodd-Frank, § 922(a)(6). Similarly, the Act provides that "[n]o award under [section 922,] subsection (b) shall be made . . . to any whistleblower who fails to submit information to the Commission in such form as the Commission may, by rule, require." *Id.* at § 922(c)(2). Moreover, "[a]ny determination made under [ ] section [922 of the Act], including whether, to whom, or in what amount to make awards, shall be in the discretion of the Commission." *Id.* at § 922(f).

[16] *See* Proposed Rule 21F-8.

[17] Dodd-Frank, § 922(c)(1)(B)(IV).

seeking to protect. The changes that we recommend will help to preserve the crucial role that internal compliance systems play in securities enforcement while maintaining incentives for whistleblowers to provide the Commission with timely information about potential violations.

Yours sincerely

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