December 17, 2010

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

Re: *File Number S7-33-10*
Proposed Rules for Implementing the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934

Dear Ms. Murphy:

We are some of the largest global companies in the United States dedicated to the highest standards of integrity and ethics in business. We are pleased to respond to the request for comments from the U.S. Securities and Exchange Commission ("SEC" or "Commission") on Release No. 34-63237 (Proposed Rules for Implementing the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934, File No. S7-33-10, Nov. 3, 2010) ("Proposed Rules").

We support the Commission's goal of "implement[ing] Section 21F in a way that encourages strong company compliance programs."[1] We want to assist in adopting rules that do not have the unintended effect of undermining the effectiveness of, and benefits that follow from, such programs. We believe that the element of the Proposed Rules that has the greatest significance for investors, company compliance programs, and the Commission's goal of receiving high quality tips is the absence of a requirement that a whistleblower first use internal company reporting procedures—no matter how robust his or her employer's compliance program may be. The release accompanying the Proposed Rules ("Proposing Release") sets forth the Commission's rationale: "while many employers have compliance processes that are well-documented, thorough, and robust, and offer whistleblowers appropriate assurances of confidentiality, others lack such established procedures and protections."[2] However, the failure of some entities to implement appropriate processes should not be a rationale for undermining the programs at the many companies that have devoted substantial time and resources to establishing and operating robust compliance and reporting programs. Accordingly, we believe that the Commission can best achieve its goal by requiring employee whistleblowers to first use internal company reporting procedures at

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[1] Release Accompanying the Proposed Rules ("Proposing Release") at 35.

[2] Proposing Release at 34.

companies that have procedures in place that are compliant with Section 301 of the Sarbanes-Oxley Act of 2002, as implemented by Commission rules and exchange listing standards, that extend to all potential securities violations.

While the Proposed Rules include provisions "intended *not to discourage*" whistleblowers at companies with robust compliance programs to first report an alleged violation internally, they do not adequately *encourage* employees to do so.[3] In contrast, the Proposed Rules offer substantial financial incentives for employees to bypass internal mechanisms and go directly to the SEC. That the SEC has imposed recent penalties in the tens and even hundreds of millions of dollars for alleged securities law violations only amplifies these incentives. Thus, the proposed whistleblower program would undermine more than encourage strong company compliance programs, which are an essential and effective tool for uncovering wrongdoing. For companies that have not devoted significant resources to their internal compliance programs, there are no apparent incentives in the Proposed Rules for them to do so.

We set forth below in more detail our comments on the Proposed Rules. In light of our view that the Proposed Rules do not give appropriate consideration to company compliance programs, particularly internal reporting procedures, we first describe several of our existing compliance and reporting programs. We then turn to the context in which these programs have developed, showing how internal compliance systems are rooted in longstanding public policy. Next, we discuss how the Proposed Rules depart from those policies and would undermine not only company compliance programs but also the purposes of the Commission's whistleblower program. We conclude by suggesting modifications to the Proposed Rules that we believe will better serve the Commission's goals while avoiding negative consequences.

I. Compliance And Reporting Programs At Many Companies Are Fully Capable Of Assisting The Commission.

We believe the following discussion of real-world company compliance and reporting programs illustrates the strength of these programs, which, as the Proposing Release acknowledges, exist at many companies across the country.[4] For purposes of this letter, we will refer to these sample companies as Company A, Company B, Company C, and Company D.

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[3] Proposing Release at 4 (emphasis added).

[4] Proposing Release at 34.

A. Company A

Company A makes its employees aware of their responsibility to report alleged violations through its code of conduct, annual certifications, and training. In addition, Company A posts its hotline numbers in all of its business offices and confirms the presence of these posters during every site audit. Moreover, the company's Ombudsman regularly travels around the world to promote the company's values and meets personally with employees to communicate information regarding the hotline and their obligation to report potential violations. Company A also makes clear that it does not tolerate retaliation in any form against employees for raising concerns or making good faith reports of potential violations. All employees are encouraged to speak up, seek guidance, and report any actions that could potentially harm the company, its employees, its shareholders, or its reputation.

The compliance and reporting program at Company A provides five different, well-publicized means for employees to raise their concerns anywhere in the world, including: (1) a toll-free telephone number, which is available 24 hours a day, seven days a week, in more than 20 languages, and which accepts allegations that are submitted anonymously; (2) the Office of the Ombudsman, which reports to the Audit Committee and Chief Compliance Counsel; (3) a specially established email address, which accepts anonymous allegations; (4) a specially established website, which accepts anonymous allegations; and (5) reporting to a manager, Legal, or Human Resources ("HR"). Anonymous reporting is actively encouraged, both through the design of the reporting tools themselves and by management, and the data confirm this fact: Almost 50% of the total fiscal year 2010 allegations were reported anonymously.

Once an allegation is reported, it is categorized according to Company A's risk-based classification system (A, B, or C). "A" is for serious matters that require immediate attention of senior personnel. "B" is for moderate matters, and "C" is for less significant reports, such as those raising certain types of personnel issues. Significant allegations or investigations are promptly reported to the Audit Committee by the General Counsel or Chief Compliance Counsel.

Upon receipt of an allegation via any of the methods described above, it is logged into the Case Management System, for which the Office of the Ombudsman has operational responsibility. The Ombudsman assigns a case manager to the allegation who reviews and analyzes the allegation. The case manager then coordinates with an investigator concerning the conduct of the investigation. Importantly, all cases are investigated; there is no *de minimis* exception. Company A believes that identifying small dollar misconduct is important in and of itself, in part because it can help root out unethical employees who might, if not caught, engage in larger scale misconduct in the future or who may already be doing so.

Company A is staffed to a level that helps ensure a thorough and timely investigation and response to all allegations of misconduct. There are nine full-time forensic auditors located around the world whose sole task is to investigate allegations of wrongdoing. To maintain their independence and objectivity, these auditors work for the corporate entity and not for any of the company's business units. These auditors are also supported by internal auditors on loan, or by external resources, on an as-needed basis. Certain significant investigations, such as Foreign Corrupt Practices Act ("FCPA") issues, are overseen by legal counsel, including a former Assistant United States Attorney.

Once the investigation is completed, the investigator prepares a report and, based on the findings, the proper course of action is determined. At that time, the reporting employee is provided with information regarding the investigation and its disposition, either personally or, if the allegation was submitted anonymously, through a specially established website that protects the reporter's anonymity. Similar controls are in place to protect the identity of anonymous reporting employees throughout the course of the investigation. Before a case is officially closed, the Office of the Ombudsman conducts a second review to see that the proper investigation process was followed. Moreover, the Ombudsman attends Audit Committee meetings and provides updates with respect to analyses and trends in the hotline data. Such analyses and data also are presented at Board meetings, which include, among others, the Chief Compliance Counsel and General Counsel.

As the above description indicates, Company A makes significant expenditures to support its compliance efforts. The budget for forensic audit and the Ombudsman alone (excluding the costs of resources such as HR, Security, Legal, Compliance, and others, all of which play varying and significant roles in conducting and supporting internal investigations) exceeds $2.5 million per year. Moreover, in fiscal year 2010, Company A spent many millions more on outside legal and forensic resources for internal investigations to supplement the company's internal resources.

Company A's efforts have led to the implementation of a reporting program that employees understand and use. In fiscal year 2010, Company A received a total of 872 allegations, a figure that is generally consistent with prior years. Almost 70% of those complaints related to personnel issues, 14% related to legal and regulatory issues, and 6% related to financial or accounting issues. Various other issues, from environmental to security matters, round out the total figure.

B. Company B

Company B communicates to employees the opportunity and their responsibility to report potential violations through its Value Statement, Policy on Business Conduct ("PBC"), and Escalation Policy. The Value Statement is reviewed by all new employees

during their orientation, displayed prominently in all company buildings, and referred to regularly in official company documents. The PBC, which comprises the code of conduct and anti-corruption policy, is communicated across the enterprise and supplemented by an employee training program; and each year, all business units and over 400 senior executives certify compliance with the PBC. The Escalation Policy reiterates the company's requirements governing the escalation of any potential or actual violations. These policies apply not only to all of Company B's operating companies and employees, but also to third parties working with or on behalf of the company who are held to those policies through certification and contractual mechanisms.

There are many ways in which employees, third parties, or customers can report alleged violations. Employees may submit reports anonymously through an Employee Hotline telephone number or website. Callers or users of the website are provided with a PIN so they can track the progress of the allegations they have reported, or anonymously be in contact with company investigators. Employees also can (and do) report allegations through other mechanisms within their local business unit or to the company's Audit, Law, Security, or HR organizations.

The Employee Hotline mechanisms are two of the most often used means of communicating allegations to the company. When so reported, the allegation is routed by an independent, external vendor to Corporate Internal Audit, which triages the report to corporate, sector, or operating company personnel on the basis of an established algorithm for investigation. Any allegation that may involve a financial or government compliance issue is posted on the company's Sensitive Issues Log. All Sensitive Issues are investigated by Internal Audit, Law, Office of Compliance, or their designated representatives. Other allegations, such as those relating to HR, environmental health, or safety policies, are routed to the reporting and investigative functions in these organizations. A Triage Committee comprising the Chief Compliance Officer, Internal Audit, the Law Department, Worldwide Security, and HR meets twice per week to review and analyze any new allegations, and to formulate and determine investigation strategies. The Triage Committee also assigns a priority value (High, Medium, or Low) on the initial assessment of the potential severity of the allegation and convenes monthly to review the investigation status of serious allegations. Internal Audit follows up to see that all investigations are completed in a thorough and timely manner, and, on an ongoing basis, the status of certain investigations is disclosed to appropriate regulators.

On a quarterly basis, allegations are reported to the Audit Committee of the Board of Directors. The report includes the allegation, the investigation scope, findings, control weaknesses, and actions taken. The Audit Committee reviews trends of reported allegations, and this information is shared with the external auditors. On a quarterly basis, all issues, trends, and metrics related to allegations of impropriety are reviewed with the Compliance

Committee, which is a management committee that includes the Chief Compliance Officers of each of the company's business sectors. This process provides Company B with the opportunity to enhance its policies, procedures, and controls in light of any pertinent trends or identified weaknesses, as well as provide additional training or heightened supervision where necessary.

The above description reflects a comprehensive and sophisticated internal reporting system that is widely used. Year to date, there have been 720 calls or website entries made into the anonymous Hotline system. This is trending toward an annual call volume of approximately 850 reports, which is consistent with past years. Historically, nearly 80% of the reports made through the Hotline process have been HR related. And year to date, 109 Hotline reports raised Sensitive Issues. Beyond the Hotline, Company B has thus far received 279 allegations that have been posted on the Sensitive Issues Log.

C. Company C

Company C believes that the keys to an effective reporting system for alleged violations are: (1) requiring that potential violations be reported; (2) publicizing that requirement; (3) facilitating compliance with that requirement by making available multiple reporting channels for employees to submit reports; (4) encouraging reporting by permitting anonymous reports, protecting the confidentiality of those who request it, and strictly prohibiting retaliation against reporting employees; (5) providing annual training that covers the obligation to report; (6) requiring annual affirmations of compliance from all employees; (7) investigating and tracking reports thoroughly; and (8) ensuring that senior management and the board are informed and engaged in the process.

To that end, Company C's Code of Conduct includes a requirement that employees report all violations of internal policy, law, or regulation applicable to the company's business. Employees also are required to report if they suspect that a violation may have occurred. The Code provides that anonymous reporting is permitted, that confidentiality will be respected, and that retaliation for good faith reporting is prohibited, even where the report is ultimately determined to have been unfounded.

Company C makes its employees aware of their obligations under the Code in a variety of ways. All employees are required to take annual Code of Conduct training, which highlights the reporting requirement. All employees also must provide an annual affirmation that they have read, understand, and will comply with the Code of Conduct, including the reporting requirement. All new hires are required to take Code training and to provide a similar affirmation. In addition, a reporting function is featured on all internal company web pages, so employees have ready access to information on how to make a report. Through the annual affirmation process, attorneys also affirm compliance with the requirements of the up-

the-ladder reporting obligations under the SEC's rule, and finance professionals affirm compliance with Company C's Code of Ethics for Finance Professionals.

The Code lists several channels through which reports can be made. Company C maintains a number of internal hotlines that are accessible throughout the world. All of these hotlines are staffed by members of the company's internal investigations unit, many of whom are former law enforcement agents, including agents who served in the United States Secret Service and Federal Bureau of Investigation. Employees also are encouraged to discuss concerns with managers, with HR representatives, and with their internal legal and compliance staff, where appropriate. The Code specifies reporting to the head of Company C's Internal Audit Department if an issue relates to a senior officer, and it also includes contact information for the Chairman of the Audit Committee of the Board of Directors for reports relating to accounting or financial reporting practices.

Company C maintains databases in which reported violations are recorded and tracked. Reports that involve significant issues are raised with appropriate senior business and risk managers and members of the legal department. Where warranted, the Audit Committee is promptly notified of significant issues by the head of internal audit or the General Counsel. The investigations unit, with the assistance of the legal department and internal audit, establishes an investigation plan for each report received, and the investigation is tracked to completion in the database. Where an investigation determines that a violation in fact has occurred, appropriate action is taken. Company C's Internal Audit Department periodically tests that reports and investigations are being handled in accordance with the company's policies.

Reported violations and investigation results are reviewed quarterly by a group of senior managers that includes the General Counsel, the heads of the internal audit, global compliance, and HR departments, and the head of the internal investigations unit. The Audit Committee of the Board of Directors receives quarterly reports of investigations that relate to accounting or financial reporting matters, as well as an annual report on the Code of Conduct training and affirmation. The Audit Committee also receives a number of other reports, including updates on investigations.

D. Company D

Compared to the other companies described above, Company D is a smaller company in terms of number of employees and revenue. In fiscal year 2010, Company D received 134 inquiries and reports of alleged violations of law or company policy. Approximately 70% of the allegations reported related to HR issues, as well as other issues unrelated to securities law violations.

Company D communicates its values and the responsibility to report potential violations in its Conduct Policy, which is provided in nine languages. The Conduct Policy is supported by either live training, which was conducted this year at all company locations with the assistance of the legal department, or by a combination of live and computer-based training. The training emphasizes employees' responsibility to "speak up" and covers the different ways in which employees can report potential or actual misconduct (discussed below). Employees are required to complete a computer-based knowledge test on the Conduct Policy and to certify annually their compliance with it. These measures are designed to help ensure that employees understand their obligations under the Conduct Policy. In addition, the company's reporting mechanisms are publicized through signage at all company locations, as well as on the company's internal and external websites.

Employees can report their concerns or any potential violations through a number of mechanisms, including a toll-free telephone number ("Helpline") that is available 24 hours a day, seven days a week, in numerous languages. The Helpline, which is operated through a third-party service, accepts allegations that are submitted anonymously. In addition, employees may call, email, fax, or visit the Chief Compliance Officer or a Regional Compliance Officer; register an allegation on a specially established website that permits anonymous allegations; and report any concerns to a manager, legal, or HR.

Company D actively encourages anonymous reporting. In fiscal year 2010, 50% of all allegations were reported anonymously. The identity of individuals filing reports, whether anonymous or not, is handled with strict confidentiality. Further, anyone who submits a report, provides information, or otherwise participates in an investigation is protected by an explicit non-retaliation policy, which is published in the company's Conduct Policy.

Each allegation that is reported is logged into Company D's case management system, which is handled by the Compliance Office. Once an allegation is logged into the system, the Chief Compliance Officer assesses the allegation and coordinates the assignment of the matter to an investigator. The investigator then contacts the reporter, if known, and conducts the investigation. Where an allegation is reported anonymously, any communication with the reporter is handled through the third-party Helpline provider, noted above. At the conclusion of an investigation, the investigator prepares a report, which is reviewed and analyzed by the Compliance Office. Cases are recommended for closure as substantiated, unsubstantiated, or closed with recommendations (i.e., a case in which the allegation is not substantiated, but the value of certain process improvements is detected). The business and other groups within Company D are briefed on the results of the investigation, and follow-up actions are determined. In addition, the Chief Compliance Officer reports all allegations and inquiries, and their eventual resolutions, to the Audit Committee of the Board of Directors through quarterly oral and typically in-person briefings

and written reports. Certain allegations, such as those involving a senior officer or securities issue, would be elevated for an expedited briefing to the Audit Committee Chair. Among other things, these briefings and reports include analyses pertaining to trends and, where applicable, suggested policy improvements. The reporting employee also is notified at the conclusion of the investigation, either personally or, if the allegation was submitted anonymously, through the third-party Helpline provider.

Company D investigates all allegations that it receives, including reports of comparatively minor matters. The Compliance Office is well staffed and is able to conduct thorough and timely internal inquiries. Investigations are conducted by lawyers or forensic accountants in the Compliance Office, other in-house lawyers, auditors from the Internal Audit Department, or shared-services HR, environmental, and health and safety professionals. Moreover, external resources are available to supplement investigations, where necessary.

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The companies whose internal reporting processes are described above—and many others like them—work together with governmental efforts to detect and prevent securities law violations, and to provide remediation where appropriate. Clearly, the Commission's implementation of the whistleblower provisions in Section 21F of the Exchange Act should foster, not frustrate, this partnership.

II. Public Policy Has Long Supported Internal Compliance And Reporting Systems.

Company compliance programs contribute to the establishment of, and reinforce, a strong "tone at the top," which is widely regarded as a central component to fostering a companywide culture of ethical behavior.[5] A culture of compliance encourages employees to report matters of concern, including questionable conduct and possible violations of the securities laws, and cultivates a system by which companies can stop wrongdoing promptly and take appropriate remedial action expeditiously. Such reporting permits companies to identify and investigate potential misconduct, discipline offending employees, and enhance their internal policies, procedures, and controls.

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[5] *See, e.g.*, Ethics Resource Center, National Business Ethics Survey: An Inside View of Private Sector Ethics 9 (2007).

Accordingly, public policy has long supported company compliance programs. Senior leaders at the SEC repeatedly have emphasized the importance of such programs. In fact, so settled is this view that during her opening statement regarding the Proposed Rules, Chairman Mary Schapiro announced that "our goal is not to, *in any way*, reduce the effectiveness of a company's existing compliance, legal, audit and similar internal processes for investigating and responding to potential violations of the securities laws."[6]

The SEC's Enforcement Cooperation Initiative further emphasizes the importance that the Commission places on company compliance procedures. The Commission's initiative was designed to "establish[] incentives for individuals and companies to fully and truthfully cooperate and assist with SEC investigations and enforcement actions."[7] Thus, the initiative is premised upon, and encourages the development of, in-house compliance programs that include a robust set of processes relating to internal investigations and disclosure.

Beyond Commission efforts to promote company compliance systems, the U.S. Federal Sentencing Guidelines provide for a reduced sentence if a convicted organization had in place an effective compliance and ethics program. Section 8B2.1(a) of the Guidelines requires that to be considered "effective," an organization's compliance and ethics program must: (1) "exercise due diligence to prevent and detect criminal conduct"; and (2) "otherwise promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law." Section 8B2.1(b) delineates seven specific steps that a corporation must take to "minimally" meet the two general requirements above, including "establish[ing] standards and procedures to prevent and detect criminal conduct," taking reasonable steps to "communicate its standards and procedures throughout the organization," and "ensur[ing] that its compliance program is followed." Importantly, companies also must "have and publicize a system, which may include mechanisms that allow for anonymity or confidentiality, whereby the organization's employees and agents may report or seek guidance regarding potential or actual criminal conduct without fear of retaliation." Further underscoring the importance of company compliance programs, the SEC and federal

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[6] Chairman Mary L. Schapiro, Opening Statement at the SEC Open Meeting: Whistleblower Program (Nov. 3, 2010) (emphasis added).

[7] Press Release, SEC Announces Initiative to Encourage Individuals and Companies to Cooperate and Assist in Investigations (Jan. 13, 2010).

prosecutors look at the effectiveness of such programs at particular companies, generally using the Guidelines, in determining whether to take enforcement or prosecutorial action.[8]

Promotion of vigorous internal compliance programs also is central to the Sarbanes-Oxley Act. Section 301 requires the audit committee of public companies to establish procedures for the receipt, retention, and treatment of complaints and the confidential submission by employees of those complaints. Moreover, Section 307 directs the SEC to issue rules, which it has done, requiring an attorney at a public company to report "up the ladder" any evidence of material violations of the securities laws and, if those higher officials do not appropriately respond, requiring the attorney to report the evidence to the audit committee.[9] And, Section 404 requires companies to disclose in their annual reports information detailing their internal procedures for maintaining an adequate reporting system. This builds upon the requirement in the FCPA that public companies "devise and maintain a system of internal accounting controls."[10]

III. The Current Proposal Risks Undermining Company Compliance Programs And Frustrating The Commission's Goals.

We are concerned that the Proposed Rules risk undermining the operation and effectiveness of internal company compliance programs by creating substantial financial incentives—and no positive disincentive—for employees to bypass internal reporting procedures (including anonymous and confidential hotlines). Such a result would be contrary to the Commission's goal of "implement[ing] Section 21F in a way that encourages strong company compliance programs"[11] and, as reflected above, would represent a departure from longstanding Commission guidance and policies underlying the Federal Sentencing Guidelines, the Sarbanes-Oxley Act, and the FCPA.

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[8] United States Attorneys' Manual, Title 9 (1997) (directing Assistant United States Attorneys to consider the same factors as those in the Guidelines when making charging decisions).

[9] Implementation of Standards of Professional Conduct for Attorneys, 68 Fed. Reg. 6296-01 (Feb. 6, 2003).

[10] 15 U.S.C. § 78m.

[11] Proposing Release at 35.

If employee whistleblowers bypass their companies' compliance and reporting programs because they are incentivized to go directly to the SEC, then the value and effectiveness of these programs will be significantly diluted—leading to a "less effective" system of securities regulation.[12] We recognize that the Proposed Rules include certain provisions that are intended to address these concerns, and we appreciate the Commission's efforts in that regard, but they do not go far enough. Specifically, Proposed Rule 21F-4(b)(7) provides that a whistleblower's report to the SEC will relate back to the date of the whistleblower's internal report to a corporate legal, compliance, audit, or similar function, provided that the whistleblower contacts the SEC within a certain amount of time of having reported internally. However, while this measure would *allow* for internal reporting, it provides no requirement or *incentive* for employees to report internally. Moreover, whether employees first report an alleged violation through their company's compliance program is not a consideration that the Commission is required to take into account in determining the amount of the award; it is, instead, only one of 11 "permissible considerations."[13]

A whistleblower program that encourages employees to circumvent internal processes, and report alleged violations directly to the SEC, would deprive companies of the ability to promptly identify and investigate instances of potential misconduct, and to determine the depth and breadth of wrongdoing. Moreover, it would be inconsistent with the provision in many companies' codes of conduct that requires employees to report internally any potential or actual violations of law or company policy. A program that does not require internal reporting also would deprive companies of the ability to act promptly in order to prevent misconduct. For example, given the $1,000,000.01 threshold to trigger the possibility of receiving a bounty payment, employees who otherwise would internally report conduct that may involve monetary amounts that they consider *de minimis* might instead hold on to the information, perhaps indefinitely (in which case the company would never learn of the information) or until the potential misconduct and investor harm escalate by several orders of magnitude. Additionally, we are concerned that the Proposed Rules would discourage employees from going to their supervisors or other company resources with questions as to possible conduct that might or might not be a violation of law or company policy.

The unintended, adverse consequences likely would not end there. Of particular significance to the Commission, the current version of the whistleblower program could

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[12] Proposing Release at 112.

[13] Proposing Release at 49.

impair the Commission's goal of encouraging whistleblowers to provide high quality tips. According to David Rosenfeld, Associate Director of the SEC's New York Regional Office, "the SEC is being 'inundated' with tips and complaints because of the pending whistleblower bounty program. . . . We expect tons of these whistleblower complaints." Mr. Rosenfeld further stated, "Some will be excellent, and some will be out there. It will take 'considerable resources and time' to sort out the viable tips."[14] Mr. Rosenfeld's observation that "some will be out there" is consistent with the empirical data, which confirm that most whistleblower complaints are not related to securities law violations but, rather, HR issues.[15] As noted above, in fiscal year 2010, almost 70% of whistleblower complaints at Company A involved personnel issues; and historically, nearly 80% of Hotline-reported complaints at Company B are HR related. Driven by the pursuit of bounty payments from the SEC—and possibly coupled with a lack of familiarity with the securities laws—employees may send the full gamut of whistleblower complaints to the Commission.

This result would be contrary to the Commission's intent as reflected in the Proposing Release, which recognizes the need to "provide a mechanism by which some of those erroneous cases may be eliminated before reaching the Commission, without otherwise adversely affecting the incentives on the part of potential whistleblowers."[16] Indeed, in recent testimony before Congress, Robert Khuzami reiterated that the SEC needed to be "mindful of competing interests" in implementing the program: "(i) a desire to encourage whistleblowers to provide the Commission with high-quality tips regarding potential violations of the federal securities laws, and (ii) *a need to avoid creating undue burdens* on the Commission and the constituencies that we protect and regulate that could result from groundless whistleblower submissions."[17]

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[14] Yin Wilczek, *SEC to Take Advantage of New Powers to File Aiding, Abetting Charges, Official Says*, BNA Corporate Accountability Report (Nov. 12, 2010).

[15] *See, e.g.*, 2009 Corporate Governance and Compliance Hotline Benchmarking Report: A Comprehensive Examination of Organizational Hotline Activity from the Network 9, 14 (2009).

[16] Proposing Release at 113.

[17] Robert Khuzami, Testimony Concerning Investigating and Prosecuting Fraud After the Fraud Enforcement and Recovery Act, Senate Committee on the Judiciary (Sept. 22, 2010) (emphasis added).

IV. Recommendations

We believe that the Commission can most effectively implement the whistleblower program by working with public companies that have robust compliance and reporting programs, such as companies exemplified by Companies A through D, and in creating meaningful incentives for other companies to implement individually tailored and similarly robust programs. The recommendations that follow are intended to permit the continued effective functioning of those compliance programs, which would allow whistleblower tips to be processed more rapidly and investor harm to be addressed more swiftly, while "enhanc[ing] the utility of the information reported to the Commission."[18] To avoid confusion, we suggest that in adopting the final rules, the Commission apply them to cover all complaints that the SEC has received since passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act").[19]

A. The Commission Should Require—Not Merely Allow—An Individual At A Company With Robust Complaint And Reporting Procedures To First Report A Potential Violation Internally.

Section 922 of the Dodd-Frank Act defines "whistleblower" as an individual or individuals who provide information to the SEC "in a manner established, by rule or regulation, by the Commission." Accordingly, the Commission could require that an employee whistleblower first report an alleged violation in accordance with his or her company's compliance and reporting program in order to meet the definition of a whistleblower. We believe the Commission should modify Proposed Rule 21F-2 by requiring such initial internal reporting where a whistleblower's employer has internal reporting procedures that meet the requirements of Section 301 of the Sarbanes-Oxley Act, as implemented by Rule 10A-3(b)(3) of the Securities Exchange Act and related exchange listing standards. In this regard, the SEC could provide a space on its complaint form for a whistleblower to indicate whether he or she has informed the company of the information, even if it was anonymously.

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[18] Proposing Release at 5.

[19] In this regard, if the Commission determines, as we suggest, that it will require initial internal reporting at companies with robust complaint and reporting procedures, it should provide those companies with any whistleblower complaints that it has received with respect to them since passage of the Dodd-Frank Act.

Pursuant to Section 301, publicly listed companies must establish procedures for: "[t]he receipt, retention, and treatment of complaints received by the listed issuer regarding accounting, internal accounting controls, or auditing matters; and [t]he confidential, anonymous submission by employees of the listed issuer of concerns regarding questionable accounting or auditing matters." Section 301 refers to "accounting, internal accounting controls, or auditing matters," but the Commission could state that in order for a whistleblower to be required to first report internally through company procedures, such procedures must be applicable to all securities law violations. As reflected above, Companies A through D—and many other companies—already have hotlines and other processes in place that address all securities violations, as well as other violations of law and company policy.

This approach addresses the Commission's concern that "while many employers have compliance processes that are well-documented, thorough, and robust, and offer whistleblowers appropriate assurances of confidentiality, others lack such established procedures and protections."[20] Rather than effectively penalize the many companies that have invested substantial efforts and resources into establishing strong compliance and reporting programs, the Commission should require whistleblowers to first use the robust internal processes at the companies that have them. The regulatory standard in the Sarbanes-Oxley Act, as implemented by SEC rules and exchange listing standards, is a ready measure for determining whether such procedures are "well-documented, thorough, and robust." Moreover, such an approach will encourage other companies to adopt robust procedures, including procedures that offer whistleblowers assurances of confidentiality.

B. In Determining The Amount Of The Award, The Commission Should Be Required To Consider Whether An Individual First Reported Internally.

The SEC should promote internal reporting procedures in its final rules implementing the 10% to 30% bounty payment range. Sections 922(b)(1) and (c)(1) of the Dodd-Frank Act leave the determination of the amount of the award to the discretion of the Commission under regulations to be prescribed by the Commission. Proposed Rule 21F-6 sets forth the Commission's proposed criteria for determining the amount of the payment. We urge the Commission to modify the rule in two respects. First, the SEC should provide that in order for an employee to be eligible for a bounty above 10%, he or she must have satisfied all applicable reporting obligations under the company's procedures, including (for example) its code of conduct. Second, the SEC should make clear that internal reporting *will* be

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[20] Proposing Release at 34.

considered a significant plus factor in determining the amount of the payout to the whistleblower, and failure promptly to report internally *will* be treated as a significant negative factor. We believe that consistent with its recognition of the importance of internal compliance programs, the SEC should provide specific incentives to encourage whistleblowers to report internally.

C. Under No Circumstances Should Culpable Whistleblowers Be Allowed To Receive A Bounty.

While the Proposed Rules seek to prevent wrongdoers from financially benefitting from essentially blowing the whistle on their own misconduct, the current proposal expressly contemplates that a whistleblower may be a participant in a securities fraud scheme or otherwise engage in other culpable conduct and still receive an award. We recognize that culpable whistleblowers may have access to potentially helpful information, but believe that countervailing public policy considerations argue against making such individuals eligible for bounty payments. Moreover, other tools are available to incentivize culpable individuals to report information to the Commission, such as offering immunity from prosecution. Incentivizing individuals to violate the securities laws in pursuit of bounty payments, and providing awards to individuals who do so, are contrary to the Commission's goal of promoting "greater deterrence" through implementation of the whistleblower program.[21] The Commission should modify Proposed Rules 21F-4(b)(4) and 21F-8(c)(3) accordingly, and eliminate Proposed Rule 21F-15.

D. Under No Circumstances Should An Individual With Compliance Or Similar Functions Be Eligible To Become A Whistleblower.

In order not to further undermine company compliance programs, we believe it is essential that individuals directly involved in these efforts not be eligible to receive bounty payments. While the Proposed Rules go part way in this direction, they contain an exception that we believe is inappropriate.

Proposed Rule 21F-4(b)(4)(iv) excludes from the definition of "independent knowledge" or "independent analysis" information that was communicated to a person with legal, compliance, audit, supervisory, or governance responsibilities with the reasonable expectation that he or she would take steps to cause the company to respond appropriately to the alleged violation. Similarly, Proposed Rule 21F-4(b)(4)(v) excludes information obtained by any person solely through a company's process for conducting internal legal,

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[21] Proposing Release at 5.

compliance, audit, or similar reviews. However, the Proposed Rules provide that any of the above individuals may qualify for a bounty if the company did not disclose the information to the Commission within a "reasonable time" or proceeded in "bad faith."

The Commission should eliminate this exception and make clear that the above-referenced individuals are not eligible for a bounty. Section 922(c)(2)(C) of the Dodd-Frank Act explicitly prohibits the SEC from making an award to external auditors, and a similar rationale applies to persons with legal, compliance, audit, supervisory, or governance responsibilities, or individuals who learn of information through those channels. Such individuals are integrally related to receiving or transferring relevant information, or ferreting out or investigating potential wrongdoing. The Proposed Rules could encourage attorneys, independent auditors, compliance personnel, and others to misuse their positions of trust and to provide information obtained through their positions to the SEC in order to benefit financially as a whistleblower. If this were to occur, the corporate compliance function would be undermined significantly.

This is not a remote possibility. The Proposed Rules do not define "reasonable time" or "bad faith," and the Proposing Release offers little guidance. It states that the amount of time that is reasonable may vary greatly from one inquiry to another, and the contours of what may constitute bad faith are left almost entirely undefined. A person with legal, compliance, audit, supervisory, or governance responsibilities who is contemplating the prospect of a large bounty payment easily could exploit this ambiguity. The Commission should not allow—much less encourage—these categories of individuals to become whistleblowers.

E. The Commission Should Deny An Award To Anyone Who Obtained Information Through A Privileged Relationship Or In Violation Of A Protective Order.

The Commission recognizes in the Proposing Release that whistleblower awards could create incentives for attorneys or others to breach the attorney-client privilege by submitting tips disclosing privileged communications.[22] The Commission has attempted to address this concern through the proposed definition of "independent knowledge," which excludes information obtained through communications protected by the attorney-client privilege. According to the Commission, "The benefit of this proposed definition is that it helps preserve and protect the integrity of the attorney-client privilege and removes financial

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[22] Proposing Release at 113.

incentive[s] encouraging individuals to breach the privilege."[23] A similar rationale applies to the Commission's exclusion from the definitions of "independent knowledge" and "independent analysis" any information that was gained through the performance of an engagement required under the securities laws by an independent public accountant.

We believe this policy applies to exclude any information that is obtained through communications that are subject to common law evidentiary privileges recognized under the laws of any state, including, but not limited to, the spousal privilege, physician-patient privilege, and clergy-congregant privilege. As with the attorney-client privilege, the public policies on which these privileges are based will be undermined if the whistleblower award program encourages individuals to violate the confidentiality of their relationships by creating monetary incentives to disclose information they obtain through privileged communications.

In addition, the Commission should exclude information provided in violation of a judicial or administrative order. Under Proposed Rule 21F-4(b)(4)(ii), attorneys cannot use civil discovery findings in private litigation as the basis for a whistleblower complaint, but clients in such proceedings are not so limited.[24] Moreover, while complaints cannot be based on information acquired in violation of federal or state criminal law, the Proposed Rules are silent as to whether or not information disclosed to the SEC in violation of a court order, such as a protective order under Federal Rule of Civil Procedure 26(c), may form the basis of a valid whistleblower submission.[25] Accordingly, the Commission should add another exclusion to Proposed Rule 21F-4(b)(4), clarifying that it will respect judicial and administrative determinations to protect specific information.

Relatedly, Commission staff should not be allowed, as Proposed Rule 21F-16(b) authorizes, to communicate directly with whistleblowers who are directors, officers, members, agents, or employees of a company that has counsel, without notifying the company's counsel. Consistent with our concern above, the proposed approach could significantly erode the protections of the attorney-client privilege as it provides no limitations

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[23] Proposing Release at 113.

[24] Proposing Release at 21, 129.

[25] Proposing Release at 31, 130.

on the subject matter of staff communications with a whistleblower. Elsewhere, the Proposed Rules evince a clear intent to protect privileged information.[26]

F. Absent Special Circumstances, The SEC Should Share Whistleblower Tips With Companies So They Can Conduct The Initial Investigation And Report Their Findings To The Commission.

The Proposing Release indicates that the Commission intends to continue its practice of working with companies to conduct internal reviews, specifically stating that, in certain instances, it will refer whistleblower complaints to the employer for review and a report of findings:

> We expect that in appropriate cases, consistent with the public interest and our obligation to preserve the confidentiality of a whistleblower, our staff will, upon receiving a whistleblower complaint, contact a company, describe the nature of the allegations, and give the company an opportunity to investigate the matter and report back. The company's actions in these circumstances will be considered in accordance with the Commission's Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions.[27]

This is a prudent approach to handling many whistleblower claims, and one that the SEC should employ whenever possible. Accordingly, we believe Proposed Rule 21F-4(b)(7) should be modified to reflect a policy of sharing whistleblower tips received by the agency with the company so that, absent special circumstances, the company can conduct the initial investigation of the alleged violation and report the result of its inquiry to the Commission. As noted earlier, a large percentage of whistleblower complaints that companies receive relate to personnel matters or other matters not likely to be of interest to the Commission. Thus, companies can assist the Commission in helping to focus its resources on "high quality tips." Moreover, companies have greater knowledge of their internal operations and can move quickly to commence an investigation. Equally important, companies need to be informed about whistleblower complaints so they can take appropriate measures to revise their procedures, strengthen internal controls, provide training, and otherwise prevent the recurrence of wrongdoing.

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[26] *See, e.g.*, Proposing Release at 20-21.

[27] Proposing Release at 34-35.

G. The Commission Should Give Employee Whistleblowers The Benefit Of A 180 Day "Look Back" Period.

Under Proposed Rule 21F-4(b)(7), if an employee whistleblower reports a potential violation to internal legal, compliance, or audit personnel at the company and, within 90 days thereafter, reports the potential violation to the SEC, the SEC will deem the information to have been provided to the SEC as of the date of the whistleblower's earlier report. We believe that 90 days is too short for all but the most basic internal investigations. The 90 day "look back" period provides companies with less control than before over whether and when to self-report potential violations, and how quickly to complete an internal inquiry. This raises particularly difficult issues in the FCPA context, where investigations often involve complicated cross-border data privacy issues, as well as large-scale document collections (and translations) and employee interviews in countries throughout the world. To help address these concerns, we believe that up to 180 days should be permitted under the look-back period for the internal review to proceed. This more reasonable time frame would help facilitate the effective operation of internal investigations, as well as maximize the utility of internal inquiries by reducing the prospect of incomplete or compressed investigations.

Consistent with our recommendation that employee whistleblowers be required to first report internally at companies with procedures that comply with the Sarbanes-Oxley Act, a 180 day window would allow such companies to conduct their internal inquiries and, where appropriate, report their findings to the SEC. In such circumstances, the company would inform the SEC that the report came from a whistleblower and provide the SEC with the internal reporting date. If the company does not report back to the employee within 180 days or informs the employee that the allegation does not warrant reporting to the SEC, the employee could determine to provide the information to the SEC, with the employee's whistleblower status relating back to the date of the internal report.

H. Whistleblowers Should Be Required To Attest That They Have A Good Faith Reasonable Belief That A Securities Law Violation Has Occurred.

Under Section 806 of the Sarbanes-Oxley Act, whistleblowers are protected only if they have a reasonable belief that their complaint relates to a securities law violation.[28] In its implementing rules, the SEC should make clear, either in Proposed Rule 21F-4, -8, or -9, that a whistleblower has not provided information "in accordance with" Section 922(h)(1)(A)(i) of the Dodd-Frank Act if the whistleblower lacks a good faith reasonable belief that a

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[28] 18 U.S.C. § 1514A(a)(1).

securities law violation has occurred. This measure would build upon the procedural requirements in the Proposed Rules that are designed to deter false submissions, including a requirement that the information be submitted under penalty of perjury, and a requirement that an anonymous whistleblower be represented by counsel who must certify to the Commission that he or she has verified the whistleblower's identity. In addition, such a requirement would further contribute to the Commission's goal of receiving high quality tips, thereby "promot[ing] greater deterrence by enhancing the efficiency and effectiveness of the Commission's enforcement program."[29]

* * *

We appreciate this opportunity to share our views with you, and would be happy to provide you with further information or feedback to the extent you would find it useful. If you have any questions, please contact Douglas Chia, Assistant General Counsel & Corporate Secretary at Johnson & Johnson, by phone at (732) 524-3292 or email at dchia@its.jnj.com, or Matthew Tanzer, Vice President and Chief Compliance Counsel at Tyco International Ltd., by phone at (609) 720-4346 or email at mtanzer@tyco.com.

Respectfully submitted,

Donna Dabney
Vice President, Secretary and
Corporate Governance Counsel
Alcoa Inc.

Gary M. Rowen
Chief Compliance Officer
Celanese Corporation

Maria C. Hermida
Chief Ethics Officer
Citigroup

Allan Tananbaum
Vice President and Deputy General Counsel,
Compliance and Litigation
Ingersoll-Rand plc

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[29] Proposing Release at 5.

Jo S. Levy
Global Director, Legal Compliance
Intel Corporation

Gary W. Fair
Vice President, Corporate Internal Audit
Johnson & Johnson

Jeffrey B. Reitman
Global Head of Compliance
JPMorgan Chase & Co.

Robert L. Herst
Vice President & Chief Compliance Officer
Kraft Foods Inc.

Douglas Lankler
Executive Vice President,
Chief Compliance Officer
Pfizer Inc.

Ann M. Kappler
Chief Legal Officer, Corporate Services
Prudential Insurance Company of America

Matthew O. Tanzer
Vice President and
Chief Compliance Counsel
Tyco International Ltd.

cc: The Honorable Mary L. Schapiro, Chairman
The Honorable Kathleen L. Casey, Commissioner
The Honorable Elisse B. Walter, Commissioner
The Honorable Luis A. Aguilar, Commissioner
The Honorable Troy A. Paredes, Commissioner
Mr. David M. Becker, General Counsel and Senior Policy Director
Ms. Meredith B. Cross, Director, Division of Corporation Finance
Mr. Robert Khuzami, Director, Division of Enforcement