BLOWING THE WHISTLE ON DODD-FRANK WHISTLEBLOWER REFORM

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I. INTRODUCTION

"Imagine getting 10% for blowing the whistle on Madoff's $50 billion scam. It's a simple thing like that will stop a lot of fraud fast."[1] At first blush this logic may be very convincing, but whistleblowers are driven by more than just monetary incentives.[2] The emotions of Harry Markopolos, the whistleblower who was ignored by the SEC while trying to expose Bernie Madoff's infamous Ponzi scheme, are illustrative:[3]

> If [Madoff] contacted me and threatened me, I was going to drive down to New York and take him out. At that point it would have come down to him or me; it was as simple as that. The government would have forced me into it by failing to do its job, and failing to protect me. In that situation I felt I had no other options. *I was going to kill him*.[4]

Are these the words of a man motivated by money? Recent research shows that many factors incentivize whistleblowers to expose fraud,[5] and may vary depending on context.[6]

In the wake of Bernie Madoff's[7] and Sir Allen Stanford's[8] widely-publicized Ponzi schemes, the Dodd-Frank Wall Street Reform and Consumer Protection Act[9] ("Dodd-Frank") significantly expands

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[1] Robert Chew, *Calling All Whistleblowers! The SEC Wants You*, TIME, Feb. 24, 2009, *available at* http://www.time.com/time/business/article/0,8599,1881318,00.html (quoting Laura Goldman, a whistleblower who has alerted the SEC to 25 cases leading to SEC fraud charges).

[2] Yuval Feldman and Orly Lobel, *The Incentives Matrix: The Comparative Effectiveness of Rewards, Liabilities, Duties, and Protections for Reporting Illegality*, 88 TEX. L. REV. 1151, 1155 (2010) (noting that monetary incentives can sometimes be counterproductive). *See also, e.g. id.* at 1181-82.

[3] Harry Markopolos, *Assessing the Madoff Ponzi Scheme and Regulatory Failures: Hearing Before the H. Comm. on Financial Services*, 111th Cong. 102 (2009) (stating that "[as] early as May 2000, I provided evidence to the SEC's Boston Regional Office that should have caused an investigation of Madoff. I re-submitted this evidence with additional support several times between 2000–2008, a period of nine years. Yet nothing was done"). *See also* Ross Kerber, *The Whistleblower*, THE BOSTON GLOBE, Jan. 8, 2009, *available at* http://www.boston.com/business/articles/2009/01/08/the_whistleblower/.

[4] HARRY MARKOPOLOS, NO ONE WOULD LISTEN: A TRUE FINANCIAL THRILLER 145 (2010). *See also Madoff Whistleblower Slams SEC in New Book*, NY TIMES DEALBOOK BLOG, *available at* http://dealbook.blogs.nytimes.com/2010/02/26/madoff-whistle-blower-slams-s-e-c-in-new-book/.

[5] Feldman and Lobel, *supra* note 2, at 1178-79.

[6] *Id.* at 1155 (stating that "[o]ur findings suggest that a systematic approach to regulation must include an understanding of the fit between the adopted law, the misconduct it addresses, and the individual it aims to incentivize").

[7] U.S. v. Madoff, 586 F.Supp.2d 244-46 (S.D.N.Y. Jan. 12, 2009).

upon existing whistleblower law.[10] In doing so, Dodd-Frank is designed to incentivize whistleblowers to expose securities fraud by expanding anti-retaliation protection and monetary incentives.[11] For example, Dodd-Frank provides a 10-30% bounty to whistleblowers exposing securities fraud.[12] However, a bounty incentive may be a misguided monetary incentive,[13] especially as applied to reporting violations of the Foreign Corrupt Practices Act.[14] Dodd-Frank's negative implications bring to light plausible alternatives to enforce securities fraud through whistleblower reporting and highlight the importance of thoughtful business practices.[15]

This Note analyzes the Dodd-Frank whistleblower provisions and provides recommendations moving forward. Part II briefly outlines relevant whistleblower laws to provide context. Part III discusses likely implications for government, businesses and individual whistleblowers. Next, Part IV provides a proposal which may be implemented through administrative and legislative action. Part V provides practical guidance for business compliance with Dodd-Frank's whistleblower provisions. Finally, Part VI offers concluding remarks.

II. Relevant Whistleblower Laws

A. *Existing Whistleblower Laws*[16]

A relatively recent area of law, whistleblower law has evolved partly in response to financial scandals.[17] In 1978, the Civil Service Reform Act ("CSRA") established the first statutory cause of action

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[8] Julie Creswell, *U.S. Agents Scrutinize Texas Firm*, NY TIMES, Feb. 12, 2009, *available at* http://www.nytimes.com/2009/02/13/business/13stanford.html?_r=2&ref=business. *See also* Laurel Brubaker Calkins and Andrew M. Harris, *Stanford Committed No Crimes: Securities Expert Says*, BLOOMBERG BUSINESSWEEK, Aug. 27, 2010, available at http://www.businessweek.com/news/2010-08-27/stanford-committed-no-crimes-securities-expert-says.html.
[9] Pub.L. No. 111-203, 124 Stat. 1376 (2010).
[10] *See* S. REP. NO. 111-176, at 110 (2009).
[11] *Id.* at 112.
[12] Pub.L. No. 111-203, sec. 922(a), §21F(b)(1),124 Stat. 1376 (2010).
[13] Feldman and Lobel, *supra* note 2, at 1178-79.
[14] See discussion *infra* Part III(A)(2).
[15] See discussion *infra* Parts III-V.
[16] For an objective and thorough discussion of the policy and efficiency of encouraging whistleblowers to report bad conduct, presented in the context of the False Claims Act, see William Kovacic, *Whistleblower Bounty Lawsuits as Monitoring Devices in Government Contracting*, 29 Loy. L.A. L. Rev. 1799, 1821-41 (1996).
[17] The Insider Trading and Securities Fraud Enforcement Act was enacted, in part, to respond to insider trading scandals, including a scandal at Drexel Burnham Lambert Inc. H. REP. NO. 100-910, at 12 (1988). The Sarbanes-

protecting whistleblowers from employer retaliation.[18] While the CRSA was notable in its efforts to protect whistleblowers, its provisions were limited to protecting federal employees[19] and proved largely ineffective.[20]

Accordingly, Congress enacted the Whistleblower Protection Act of 1989 ("WPA"), which greatly expanded whistleblower protection.[21] Among other provisions, the WPA created a separate agency to litigate claims,[22] permitted individuals to file whistleblower claims without government support in some cases,[23] and permitted courts to shift attorneys' fees from whistleblower plaintiffs to defendants.[24] A contemporary act, the Insider Trading and Securities Enforcement Act of 1988, mandated a SEC whistleblower bounty program for tips reporting insider trading.[25] However, the bounty program has proven largely ineffective, making only seven payments totaling $159,537 since its inception.[26]

In 2002, the Sarbanes Oxley Act ("SOX") tremendously expanded the scope of whistleblower protection and also required business controls to deter and detect fraud.[27] Most significant, and in the wake of corporate scandals at Enron and Worldcom,[28] SOX extended whistleblower protection beyond federal employees to employees of publicly held companies.[29] Notably, whistleblower protection for non-government employees effectively adopted public policy to regulate private sector securities fraud to limit the associated public risk.[30] Moreover, SOX granted whistleblowers the right to file a claim in federal

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Oxley Act was passed, in part, to respond to corporate scandals at Enron and Worldcom. STEPHEN KOHN, MICHAEL KOHN, AND DAVID COLPINTO, WHISTLEBLOWER LAW xi (2004).
[18] S. REP. NO. 100-413, at 2 (1989).
[19] *Id.*
[20] *Id.* at 5. Surveys showed that the percentage of federal employees reporting known fraud remained fairly constant in 1980 and 1983. *Id.* Moreover, the number of employees who did not report illegal activity due to fear of reprisal had risen. *Id.*
[21] *See* CRS Summary Pub.L. No. 101-12, 103 Stat. 16 (1989). *See also* S. REP. NO. 100-413, at 2 (1989).
[22] Pub.L. No. 101-12, § 1221, 103 Stat. 16 (1989).
[23] *Id.* § 1221(a).
[24] *Id.* § 1221(g)(1).
[25] Pub. L. No. 100-704, §3(a), 102 Stat. 4677, 15 U.S.C. 78u-1 (1988).
[26] U.S. Securities and Exchange Commission, Office of Inspector General, Office of Audits, *Assessment of the SEC's Bounty Program* (hereinafter *Inspector General Report*), Rep. No. 474, at 5, Mar. 29, 2010.
[27] Pub.L. No. 107-204, § 806, 116 Stat. 745 (2002). *See also* CRS Summary Pub.L. No. 107-204, 116 Stat. 745 (2002). *See also* KOHN, *supra* note 17.
[28] KOHN, *supra* note 17, at xii.
[29] Pub.L. No. 107-204, § 806, 116 Stat. 745 (2002). *See also* KOHN, *supra* note 17, at xiii.
[30] KOHN, *supra* note 17, at xiv.

court if an administrative procedure does not result in a final order within a statute of limitations.[31] SOX also set a low standard for whistleblowers to acquire statutory protection, only requiring that the whistleblower have a "reasonable belief" of fraud.[32] Thus, whistleblowers enjoyed a broad array of federal protection to incentivize the reporting of securities fraud prior to the enactment of Dodd-Frank.[33]

B. *Dodd-Frank Whistleblower Reform*[34]

Dodd-Frank expands whistleblower protection and monetary incentives even further than SOX, in part to respond to the Madoff and Stanford Ponzi schemes.[35] Specifically, the Dodd-Frank provisions expand whistleblower law by:

- Providing *a 10-30% bounty for all tips resulting in SEC[36] or CFTC[37] enforcement actions with monetary sanctions greater than $1,000,000*, which expands upon the SEC's existing insider trading bounty program.

- Providing *protection to employees of all subsidiaries and affiliates of public companies*[38] and "any individual performing tasks related to the offering or provision of a consumer financial product or service."[39]

- Providing a *private right of action in federal court* for whistleblowers regardless of administrative delay.[40]

- *Increasing the statute of limitations* for whistleblower protection actions to 6 years following the alleged violation.[41]

Perhaps as a result of being lost in long legislation, which totals 2319 pages,[42] the Dodd-Frank whistleblower provisions received relatively little media attention during Dodd-Frank's deliberation and

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31 Pub.L. No. 107-204, sec. 806(a), § 1514A(b)(1)(B), 116 Stat. 745 (2002). *See also* KOHN, *supra* note 17, at 5.

32 Pub.L. No. 107-204, sec. 806(a), § 1514A(b)(2)(C), 116 Stat. 745 (2002) (citing 42 U.S.C. § 42121(b)(2)(A)) (stating that "[i]f the Secretary of Labor concludes that there is a reasonable cause to believe that a violation of subsection (a) has occurred, the Secretary shall accompany the Secretary's findings with a preliminary order providing the relief prescribed by paragraph (3)(B)"). *See also* KOHN, *supra* note 17, at 6.

33 *See* KOHN, *supra* note 17, at 6.

34 For a more thorough discussion of the substance of the Dodd-Frank whistleblower provisions, see Drew Harker et al., *Whistleblower Incentives and Protections in the Financial Reform Act*, 127 Banking L.J. 779 (2010).

35 S. REP. NO. 111-176, at 139-140 (2009).

36 Pub.L. No. 111-203, sec. 922(a), § 21F(b)(1), 124 Stat. 1376 (2010).

37 *Id.* sec. 748, § 23(b)(1).

38 *Id.* § 929A.

39 *Id.* § 1057(b). Whistleblowers protected under § 1057 may not waive their statutory rights through arbitration agreements. *Id.* § 1057(d)(1).

40 *Id.* sec. 922(a), § 21F(h)(1)(B)(i). Under SOX, whistleblowers could only proceed to federal court if they could not obtain a final order from an administrative hearing within 180 days. Pub.L. 107-204, sec. 806(a), § 1514A(b)(1)(B), 116 Stat. 745 (2002).

41 Pub.L. No. 111-203, sec. 922(a), § 21F(h)(1)(B)(iii), 124 Stat. 1376 (2010).

are conspicuously absent from the Congressional Research Service Bill Summary of Dodd-Frank.[43] Nonetheless, Dodd-Frank's whistleblower provisions will undoubtedly affect fraud reporting and impose costs on businesses and government agencies.[44]

III. IMPLICATIONS

As an important preliminary note, the implications of Dodd-Frank's whistleblower reform are largely contingent on the extent to which reform actually results in increased whistleblower tips and the quality of such tips. Recently proposed SEC rules may also greatly affect reporting frequency and quality once implemented.[45] Ideally, increased whistleblower reporting will increase fraud detection and build public confidence in U.S. capital markets, which in turn stimulates investment and economic growth.[46] However, it is not certain that the new laws, especially the bounty program, will increase the quality of whistleblower reporting and subsequently detect fraud as intended.[47]

Early reports show that Dodd-Frank is indeed increasing whistleblower tips.[48] But time is needed to assess the quality of these tips.[49] Moreover, avoiding the cost of frivolous or unreliable tips is difficult because the quality of tips is rarely apparent from a whistleblower complaint.[50] This section discusses Dodd-Frank's likely impact on whistleblower reporting and the costs associated with its incentives.

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[42] Pub.L. No. 111-203, 124 Stat. 1376 (2010). In contrast, Sarbanes-Oxley was only 66 pages long. *See* Pub.L. No. 107-204, 116 Stat. 745 (2002).
[43] *See* CRS Summary Pub.L. No. 111-203 (Jul. 29, 2010). *But see* Jessica Holzer and Fawn Johnson, *Larger Bounties Spur Surge in Fraud Tips*, WALL ST. J. (Sep. 7, 2010). *See also* Sue Reisinger, *Firms Face a Sudden Rush of Whistleblower Claims*, WALL ST. J., Sep. 9, 2010.
[44] *See* discussion *infra* Part III.
[45] SEC Release No. 34-63237, Proposed Rules for Implementing the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934 (heinafter *SEC Proposed Rules*), at 104, Nov. 3, 2010, *available at* http://www.sec.gov/rules/proposed/2010/34-63237.pdf.
[46] S. REP. NO. 111-176, at 2-4 (2009). *See also id.* at 112.
[47] *See* discussion *infra* Part III(A)(1).
[48] Holzer and Johnson, *infra* note 43.
[49] *Id.*
[50] Amy Kolz, *Serial whistle-blower Joseph Piacentile makes millions helping the government uncover fraud. That's how the False Claims Act is supposed to work. Or is it?*, THE AMERICAN LAWYER (June 1, 2010), *available at* http://www.law.com/jsp/tal/PubArticleTAL.jsp?id=1202457711736&slreturn=1&hbxlogin=1.

A. *A Closer Look at Reporting Securities Fraud and Dodd-Frank*

Dodd-Frank provides both anti-retaliation incentives (e.g. direct access to federal court) and monetary incentives (e.g. the bounty program) designed to increase whistleblower reporting.[51] Unfortunately, Dodd-Frank does not adequately address existing administrative issues with managing whistleblower tips. Moreover, monetary incentives may primarily encourage unreliable tips if outrage over morally culpable behavior already incentivizes whistleblowers to voluntarily report actual securities fraud.

1. *The Problem: Managing Whistleblower Tips*

It is better administrative tip management, rather than increased monetary incentives, that are needed to efficiently improve securities law compliance.[52] A 2010 Inspector General Report implicitly recognized as much by offering many managerial recommendations for improving the SEC's existing insider trading bounty program.[53] Taken in this light, it is not whistleblower incentives of any type, but rather administrative management that should be reformed to enforce securities laws.

A recently exposed Ponzi scheme is a prime example of the need for better administrative whistleblower tip management and the potential ineffectiveness of monetary incentives.[54] In the case, a trader, Ty Schlobohm, obtained information exposing a hedge fund's Ponzi scheme.[55] However, Mr.

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[51] Pub.L. No. 111-203, sec. 922(a), 124 Stat. 1376 (2010). Generally speaking, there are three distinct types of whistleblower incentives: anti-retaliation laws, affirmative duties to report and monetary incentives. Feldman and Lobel, *supra* note 2, at 1160.
[52] *See Inspector General Report, supra* note 26.
[53] *Id.*
[54] There is plentiful anecdotal evidence of the SEC and CFTC mishandling valid tips about fraud. As a second example, in the context of the SEC, the SEC mishandled Harry Markopolos's repeated tips about the Madoff Ponzi scheme. An earlier response to the Markopolos tips would have limited the degree of Madoff's fraud. Moreover, Markopolos's motive for attempting to expose Madoff's fraud was not a whistleblower award, but rather to create fair competition among hedge funds competing for business. MARKOPOLOS, *supra* note 4, at 54. Thus, while better handling of the Markopolos tip would have been effective, monetary whistleblower incentives would not have exposed the Madoff scheme because Markopolos voluntarily provided the tip. Markopolos, *supra* note 3, at 2 (Rep. Kanjorski stating "Mr. Markopolos was justifiably relentless in ringing alarm bells. Unfortunately, our regulators failed to follow his roadmap and heed his warnings. As a result, thousands of investors were hurt."). A third example of mishandling tips, this time in the CFTC context, regards tips about manipulating silver commodity prices. Susan Pullium and Carolyn Cui, *Act Now*, *CFTC is Urged*, WALL ST. J., Oct. 27, 2010, *available at* http://online.wsj.com/article/SB10001424052702303341904575576203310056046.html.
[55] Edward Wyatt, *Whistle. Then Worry and Wait.* NY TIMES, October 9, 2010, *available at* http://www.nytimes.com/2010/10/10/business/10whistle.html?pagewanted=1&_r=3&emc=eta1.

Schlobohm's initial report was ignored by the Commodities and Futures Trading Commission ("CFTC"), which incorrectly concluded that it did not have jurisdiction over the case.[56] It was not until Mr. Schlobohm reported the tip to the Department of Justice ("DOJ") that the government began to act.[57] The FBI eventually took the lead in the criminal investigation, and the DOJ action resulted in guilty pleas of mail fraud and tax evasion.[58]

The SEC and CFTC's civil investigation began after the criminal investigation and is still pending, ironically, despite a less extensive civil burden of proof than in the criminal context.[59] Furthermore, the DOJ investigator noted that "[c]ategorically, at no time did we interfere with the [SEC/CFTC's] ability to move."[60] It is also doubtful that monetary incentives such as the Dodd-Frank bounty program[61] would have affected Mr. Schlobohm's behavior.[62] In fact, Mr. Schlobohm stated that he did not report the fraud in hope of a reward and has even suggested that he might reject any award or give it to the victims of the fraud.[63]

The successful result of the criminal investigation in Mr. Schlobohm's case considered in tandem with the slow pace and uncertain results of the SEC/CFTC civil investigation demonstrate the need for improved SEC and CFTC administrative efficiency.[64] Had the SEC or CFTC been as responsive initially as the DOJ and FBI were, the fraud could have been detected in a timely manner and investors may have saved significant amounts of money.[65] With Mr. Schlobohm's case in mind, it is apparent that

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[56] *Id.*
[57] *Id.*
[58] *Id.*
[59] *Id.*
[60] *Id.*
[61] It is not clear in this case whether the Dodd-Frank whistleblower provisions are applicable to this situation because the investigation began prior to Dodd-Frank's enactment. *Id.* *But see* Pub.L. No. 111-203, § 924(b), 124 Stat. 1376 (2010).
[62] *Id.*
[63] *Id.*
[64] One lawyer representing the victims noted that "it is inexcusable that the authorities did not move in more quickly to stop people from investing more money." *Id.*
[65] *Id.* The criminal investigation in this case allowed fraud to persist in order to build enough evidence to bring a successful criminal case. *Id.* A civil investigation may not have required as much evidence, brought a civil action sooner, and effectively concluded the investor fraud sooner.

whistleblower incentives cannot be successfully implemented without the ability to adequately manage whistleblower tips.

2. *The Congressional Solution: A Bounty Program*

Even if administrative management is sufficient to benefit from whistleblower incentives, Dodd-Frank's bounty program is an unnecessary and misguided securities fraud deterrent. Regulation should implement "a fit between the adopted law, the misconduct it addresses, and the individual it aims to incentivize."[66] Unfortunately, monetary incentives can be ineffective or even counterproductive and decrease reporting of illegal activity.[67] More significant, however, is that the context of fraud is critical to reporting. That is, individuals are more likely to report illegal activity if they are particularly outraged by morally reprehensible conduct.[68] As such, monetary incentives are more effective regarding conduct that is not viewed as morally reprehensible.[69]

Congressional arguments analogizing the new SEC bounty program to the IRS's recently reformed bounty program supported enacting the Dodd-Frank whistleblower provisions. However, the two bounty programs may not be analogous because securities fraud reporting is not necessarily analogous to tax fraud reporting.[70] Tax fraud may not be viewed as morally reprehensible[71] because it harms diffuse victims indirectly through the government.[72] In contrast, securities fraud may be viewed as morally reprehensible[73] because it is likely to involve morally culpable conduct directly harming

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[66] Feldman and Lobel, *supra* note 2, at 1155.
[67] Monetary incentives can result in a "crowding out effect," whereby informants are discouraged from reporting illegal activity because the presence of external rewards discounts moral incentives and intrinsic motivation to report. *Id.* at 1178-79. In the presence of monetary incentives, reporting of illegal activity can be viewed as a "transaction rather than a charitable act." *Id.* at 1179.
[68] *Id.* at 1192.
[69] *Id.* at 1193-94.
[70] *Id*. (making a positive analogy between the new SEC bounty program and the recently reformed IRS bounty program). *See also* Tax Relief and Health Care Act of 2006, Pub. L. No. 109-432, § 406, 120 Stat. 2922, 2958 (2006).
[71] Feldman and Lobel, *supra* note 2, at 1204 (stating that tax fraud is generally not viewed as morally culpable).
[72] Dan Markel, *Executing Retributivism: Panetti and the Future of the Eighth Amendment*, 103 NW. U. L. REV. 1163, n. 161 (2009).
[73] Michael Sirkin, *The Deterrence Paradox: How Making Securities Fraud Class Actions more Difficult for Plaintiffs will more Strongly Deter Corporate Fraud*, 82 TEMP. L. REV. 307, 308 (2009) (stating that strong cases of securities fraud involve morally culpable conduct). *See e.g.* Brent Horton, *How Corporate lawyers Escape*

individual investors who have difficulty defending against fraud.[74] Further, if securities fraud has more potential to involve morally culpable conduct and enrage potential whistleblowers than tax fraud, potential whistleblowers are more likely to report securities fraud voluntarily regardless of any monetary incentive.[75]

In addition, voluntary disclosure may result from corporate management making a business decision. Many tips incentivized by Dodd-Frank are expected to report Foreign Corrupt Practices Act ("FCPA") violations.[76] However, empirical evidence in the Sarbanes-Oxley era has shown that corporations voluntarily disclose a significant portion of FCPA claims.[77] Moreover, Dodd-Frank may have the effect of decreasing voluntary corporate reporting. Expressly, increased monetary incentives may encourage whistleblowers to report externally to the SEC rather than report internally, which could ultimately result in voluntary corporate disclosure.[78] Even if there are a significant amount of undetected FCPA claims, it is unclear whether whistleblowers understand fact-driven FCPA law well enough to provide reliable tips.[79] Thus, at least in the case of FCPA tips, monetary incentives may not be as effective as intended or as in the tax fraud setting.

Sarbanes-Oxley: Disparate Treatment in the Legislative Process, 60 S.C. L. REV. 149, 162 (2008) (stating that Enron's security fraud was morally reprehensible).

[74] David A. Wilson, *Outsider Trading—Morality and the Law of Securities Fraud*, 77 GEO. L.J. 181, 215 (1988). *See also* KOHN, *supra* note 17, at xv (citing Congressional intent to enact "U.S. laws [that] encourage and protect those who report fraudulent activity that can damage innocent investors in publicly traded companies."). *Id.* Additionally, Kohn notes that pre-SOX securities fraud "caused investors and pensioners to lose billions of dollars in scandal-plagued companies. *Id.* at xii. By citing such Congressional intent and noting the effect on individuals, Kohn is implicitly recognizing that securities fraud can have a direct effect on individuals.

[75] *See* Feldman and Lobel, *supra* note 2, at 1193-94.

[76] Harker et al., *supra* note 34. *See also* Holzer and Johnson, *supra* note 43.

[77] Robert Tarun, *How Corporate Lawyers Escape Sarbanes-Oxley: Disparate Treatment in the Legislative Process*, 60 S.C. L. REV. 149 (2010). It should be noted that an SEC official has refuted the extent to which voluntary disclosure leads to filing FCPA enforcement actions. *Id.* Also, voluntary FCPA disclosure is due, in part, to increased corporate oversight required by SOX as well as DOJ incentives which potentially minimize punishments for corporation's voluntarily disclosing FCPA violations. *Id.* However, it is unclear whether the DOJ incentives actually minimize punishment for FCPA violations. Bruce Hinchey, *Punishing the Penitent: Disproportionate Fines in Recent FCPA Enforcements and Suggested Improvements*, *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1650925.

[78] *Id.*

[79] See discussion *infra* Part III(B)(2). *But see SEC Proposed Rules*, *supra* note 45, at 112 (noting a proposed SEC mechanism whereby whistleblowers can seek guidance from corporate compliance staff as to whether certain conduct constitutes securities fraud and still be eligible for a bounty).

Also, the IRS analogy is not very persuasive because there is conflicting evidence as to the success of the IRS bounty program. Under the IRS program, whistleblower rewards take years to be issued.[80] Indeed, as of January 2010, the IRS had not yet paid a bounty under the program reformed in 2006.[81] The Chief Counsel of the IRS has even stated that the bounty program is a "disaster waiting to happen"[82] and a "ticking time-bomb"[83] because the whistleblower program could result in complaints about overzealous auditors.[84] Nonetheless, advocates of the IRS bounty program point to the billions of dollars in tax revenue the IRS stands to gain under the program[85] and the reliable information provided by whistleblowers.[86]

A more compelling argument in support of the new SEC bounty program, not cited in a Senate Report about Dodd-Frank,[87] analogizes it to the False Claims Act ("FCA").[88] The FCA analogy is more compelling because *qui tam* actions brought by private citizens on behalf of the United States[89] has more clearly led to successful enforcement actions.[90] However, the FCA may still be distinct from securities fraud for the same reasons tax fraud is distinct from securities fraud. Expressly, securities fraud is more likely than fraudulently claiming federal funds to involve morally culpable conduct, which may outrage

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[80] David Kocieniewski, *Whistleblowers Become Investment Option for Hedge Funds*, NY TIMES (May 19, 2010), *available at* http://www.nytimes.com/2010/05/20/business/20whistleblower.html?pagewanted=1&_r=1. Interestingly, hedge funds have invested in whistleblower awards by "agreeing to buy a percentage of [future payouts to IRS whistleblowers] in exchange for a smaller amount upfront to the whistleblowers. *Id.*

[81] *IRS Whistleblower Office Closer to First Aware Determinations Under New Law*, TAX NOTES TODAY, 2010 TNT 15-8 (Jan. 25, 2010).

[82] Kocieniewski, *supra* note 80.

[83] Jeremiah Coder, *Tax Analysts Exclusive: Conversations: Donald Korb,* TAX NOTES TODAY, 2010 TNT 11-7 (Jan. 19 2010).

[84] *Id.*

[85] Feldman and Lobel, *supra* note 2, at 1168.

[86] Erika Kelton, Phillips & Cohen LLP, *Letters to the Editor: Korb Wrong about Whistleblower Program, Writer Says,* TAX NOTES TODAY, 2010 TNT 15-20 (Jan. 25, 2010).

[87] *See generally* S. REP. NO. 111-176.

[88] 31 U.S.C. § 3730(d). As with the SEC bounty program, awards resulting from *qui tam* actions under the FCA may reach up to 30% of the enforcement proceeds. 31 U.S.C. 3730(d)(2). For a thorough description of relator/whistleblowers and the FCA, see Kovacic, *supra* note 16, at 1818-19.

[89] 31 U.S.C. § 3730(d)(4) (1994). While not a bounty program *per se*, *qui tam* actions under the FCA nonetheless encourage relator/whistleblowers to report fraud by bringing actions on behalf of the United States government.

[90] Thomas Harris, *Alternate Remedies & the False Claims Act: Protecting Qui Tam Relators in Light of Government Intervention and Criminal Prosecution Decisions*, 94 CORNELL L. REV. 1293, 1302 (2009). *But see* Kovacic, *supra* note 16, at 1841-42 (stating that there is a lack of empirical evidence to evaluate the effectiveness of FCA *qui tam* actions).

potential whistleblowers, result in voluntary reporting, and obviate the need for monetary incentives.[91] As is the case with tax fraud, noted above, one argument in support of this view is that FCA violations affect a more diffuse group (i.e. the government) than securities fraud. Thus, a bounty is more appropriate for FCA violations than securities fraud.

Finally, the legislative history of the Dodd-Frank whistleblower provisions suggests that Congress may not have been very thoughtful in reforming the SEC's bounty program.[92] First, the report the Senate cited to support the proposition that whistleblowers are instrumental in detecting and reporting fraud does not address securities fraud *per se*, but rather all occupational fraud, which is overinclusive and underinclusive of the SEC bounty program's scope.[93] Second, there is little indication that Congress considered some negative ramifications of providing whistleblowers with additional monetary incentives.[94] Rather, Congress appears to have followed a common misconception that monetary incentives will always increase reported illegal activity[95] without providing authority. Third, a Senate Report cites a White House press release as the impetus for the Dodd-Frank whistleblower provisions.[96] However, the White House press release does not call for a reformed SEC bounty program, which is a major part of Dodd-Frank whistleblower reform.[97] More thoughtful policy may have garnered initial executive support. Accordingly, the SEC bounty program may not result in significant fraud reporting, detection or enforcement.

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[91] *See* Feldman and Lobel, *supra* note 2, at 1193-94.
[92] *See generally* S. REP. NO. 111-176 (2009).
[93] S. REP. NO. 111-176, 110 (2009) (citing Markopolos, *supra* note 3 (citing Association for Certified Fraud Examiners, *2008 Report to the Nation on Occupational Fraud & Abuse*, *available at* http://www.intercedeservices.com/downloads/2008-rttn.pdf)). Expressly, only some securities fraud occurs in the occupational context and only some occupational fraud is securities fraud.
[94] *But see* S. REP. NO. 111-176, at 244 (2009).
[95] Feldman and Lobel, *supra* note 2, at 1190 (noting empirical research in which survey participants "[revealed] a perception that a stranger's decision to report [illegal activity] is more likely to be externally driven" as opposed to being driven by moral considerations). *See* 156 Cong. Rec. S4076 (daily ed. May 20, 2010) (Senator Shelby stating that "the guaranteed massive minimum payouts and limited SEC flexibility ensures that a line of claimants will form at the SEC's door").
[96] *See* S. REP. NO. 111-176, at 110-11 (2009).
[97] *Fact Sheet: Administration's Regulatory Reform Agenda Moves Forward; Legislation for Strengthening Investor Protection Delivered to Capitol Hill,* U.S. Department of the Treasury, Press Release, Jul. 10, 2009, *available at* http://www.financialstability.gov.

B. *Costs Associated with the Dodd-Frank Whistleblower Provisions*

As a general matter, there are certain to be additional costs from Dodd-Frank's whistleblower provisions simply due to increased whistleblower reporting.[98] As a result, attorneys will benefit from both businesses and whistleblowers that need representation as well as businesses in need of compliance advice. In addition, specific methods of incentivizing whistleblowers under Dodd-Frank carry with them other costs.

Three types of laws incentivize whistleblower reporting: anti-retaliation protection, monetary incentives, and affirmative duties to report.[99] As noted, Dodd-Frank adopts additional anti-retaliation measures (e.g. a private right of action in federal court) and monetary incentives (e.g. the bounty program).[100] Each incentive type will cause businesses and government agencies to incur considerable costs.

1. *Costs Resulting from Anti-Retaliation Protection*

Anti-retaliation protection costs are exemplified by the fact that whistleblower protection extends to government agencies and publicly traded companies, but not private businesses.[101] Implicit in the absence of whistleblower protection for employees of privately held businesses is the public policy determination that private business fraud does not pose a threat to society which warrants imposing the costs associated with federal whistleblower protection.[102]

Perhaps the most significant cost of Dodd-Frank's anti-retaliation protection is the direct access to federal courts provided to whistleblowers, which may lead to expanded and expensive litigation. Previously, under Sarbanes-Oxley, whistleblowers were granted access to federal courts only if there was

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98 Holzer and Johnson, *supra* note 43. *See also* Reisinger, *supra* note 43.
99 Feldman and Lobel, *supra* note 2, at 1160.
100 Pub.L. No. 111-203, sec. 922(a), 124 Stat. 1376 (2010).
101 Frank Cavico, *Private Secotr Whistleblowing and the Employement-At-Will Doctrine: A Comparative Legal, Ethical, and Pragmatic Analysis*, 45 S. TEX. L. REV. 545, 546-47 (2004). The exclusion of private company employees from whistleblower protection is in contrast to more encompassing federal anti-discrimination laws. *Id.*
102 *See* KOHN, *supra* note 17, at xiv (noting that whistleblower protection for employees of publicly held companies serves the public interest). Harsh results to employees of privately-held companies are avoided through secondary employer liability, which may be the result of state policy decisions to protect private employees from whistleblower retaliation. First, there is secondary liability under state blues sky laws. Cavico, *supra* note 101, at 550. Second, common law tort actions provide secondary liability. *Id.* at 550-52. Specifically, many state statutes allow wrongfully discharged employees to recover damages from their employer in tort. *Id.* at 579.

administrative delay such that a final order was not issued within a 180 day statute of limitations.[103] Additional costs result because litigation in federal courts often includes expensive discovery, litigation, and appeals processes.[104] In contrast, administrative hearings are not governed by the rules of evidence[105] and may be amended or streamlined to accommodate an executive's budget concerns.[106]

Also, Dodd-Frank prohibits pre-dispute arbitration agreements or waiver of statutory whistleblower protection.[107] Arbitration and waiver can be effective tools to combat the business burdens resulting from expanded whistleblower protection.[108] By eliminating these cost-cutting options,[109] Dodd-Frank forces parties into expensive litigation in federal court.

Finally, extending protection to whistleblowers reporting any type of securities fraud exacerbates moral hazard.[110] Since whistleblower protection applies to whistleblowers even if they are providing invalid tips, employees fearing discipline or termination may report false tips solely to obtain whistleblower protection that may prevent an employer from terminating an employee.[111] Broadening whistleblower protection may therefore have the adverse effect of requiring businesses to retain employees they would otherwise terminate. Also, agencies must process frivolous tips resulting from moral hazard. In light of the foregoing, Dodd-Frank's broadening of anti-retaliation whistleblower protection poses a considerable burden.

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[103] Pub.L. No. 107-204, sec. 806(a), § 1514A(b)(1)(B), 116 Stat. 745 (2002). *See also* KOHN, *supra* note 17, at 5.
[104] Robert Bone, *Improving Rule 1: A Master Rule for the Federal Rules*, 87 DENV. U. L. REV. 287, 296 (2010) (stating that increasing federal litigation expense has given rise to a movement in alternative dispute resolution).
[105] *Schuler v. Comm'r of Soc. Sec.*, 109 F. Appx. 97, 102 (6th Cir. 2004) (citing *Cline v. Secretary of Health, Education & Welfare*, 444 F.2d 289, 291 (6th Cir. 1971)).
[106] Andrew Page, *What's the Cost of Living in Oregon These Days? A Fresh Look at the Need for Judicial Protections in the Death with Dignity Act*, 22 REGENT L. REV. 233, 253 (2009).
[107] Pub.L. No. 111-203, sec. 922(c)(2), § 1514(A)(e)(2), 124 Stat. 1376 (2010).
[108] Robert Rhoad et al., *Whistling While They Work: Limiting Exposure in the Face of the PPACA's Invitation to Employee Whistleblower Lawsuits*, 22 No. 6 HEALTH LAW 19 (2010).
[109] Pub.L. No. 111-203, sec. 922(c)(2), § 1514(A)(e)(2), 124 Stat. 1376 (2010).
[110] Feldman and Lobel, *supra* note 2, at 1177 (stating that "overprotection may encourage bad-faith reporting and exaggerated, or even false, accusations"). "It can also diminish the positive ties and organizational citizenship behavior (OCB) of institutional players." *Id.*
[111] Pub.L. 111-203, sec. 922(a), § 21F(h)(1), 124 Stat. 1376 (2010). Section 922(a) only requires that an employee report information, not that the employee report accurate information, to obtain whistleblower protection. *See id.*

2. *Costs Resulting from Monetary Whistleblower Incentives*

The Dodd-Frank bounty program imposes heavy costs on business compliance and agency administration. In a similar context, the IRS Chief Counsel remarked that a mandate to reform its fraud detection bounty program was "forced on the IRS.[112] Specific costs of the new SEC bounty program include: (1) a flood of poor quality tips; (2) compliance burdens such as encouraging employees to report fraud externally rather than internally; (3) an inflexible SEC fraud enforcement strategy; (4) fraud detection measures that may not be cost-effective; and (5) excessive and unnecessary litigation.

First and foremost, the bounty program is likely to incentivize frivolous, misleading, exaggerated, or otherwise unreliable tips.[113] One reason is that employees may not understand the criteria needed to obtain a whistleblower bounty and will report poor or incomplete information "just in case" they have sufficient information.[114] A misunderstanding may result from ambiguous rules implementing Dodd-Frank or insufficient notice of the bounty requirements.

In addition, employees may unintentionally contribute to the administrative backlog of tips if they do not understand complicated legal standards for securities fraud.[115] For example, employees may report fraud regarding the Foreign Corrupt Practices Act ("FCPA")[116] despite, or perhaps because, FCPA violations are not always clear due to ambiguous law.[117] Indeed, it is expected that many tips under the new bounty program will report potential FCPA fraud.[118] Unfortunately, there is little FCPA case law because enforcement actions usually result in settlement.[119] As a result, FCPA actions are usually pursued under sometimes conflicting agency interpretations that do not have the force of law.[120]

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[112] Coder, *supra* note 83.
[113] *Id.*
[114] *SEC Proposed Rules*, *supra* note 45, at 39.
[115] *See e.g.* Kolz, *supra* note 50.
[116] 15 U.S.C. §§ 78dd-1, et seq.
[117] Professor Mike Koehler, Butler University, *The Financial Reform Bill's Whistleblower Provisions and the FCPA* (July 20, 2010), *available at* http://fcpaprofessor.blogspot.com/2010/07/financial-reform-bills-whistleblower.html.
[118] Holzer and Johnson, *supra* note 43. *See also* Reisinger, *supra* note 43.
[119] Koehler, *supra* note 117.
[120] *Id.*

Moreover, many FCPA violations are already voluntarily reported by whistleblowers.[121] Taken in this light, whistleblowers may flood the SEC with reports 'just in case' they have sufficient information and it is not clear that questionable reporting justifies an award.

Second, Dodd-Frank indirectly encourages employees to report fraud externally to the government and undermine corporate compliance rather than internally to corporate management.[122] Employees stand to earn a considerable reward under the bounty program if they report fraud to the SEC, which may not be available if the fraud is handled internally.[123] Reporting internally is further discouraged due to a potential race to provide the SEC with "original information" worthy of an award.[124] Whistleblowers may report externally to the SEC, rather than internally to management, to avoid delay and mitigate the risk of foregoing or sharing an award due to another whistleblower reporting sooner, collecting the award, and rendering the information non-original. A whistleblower may not be eligible for an award if not possessing original information, possibly due to another informant reporting the same information sooner.

External fraud reporting imposes costs on businesses which are not present when fraud is corrected by internal reporting and detection. If the SEC steps in to enforce fraud, companies face SEC penalties, legal costs of corporate defense, and forgo potential leniency due to voluntary reporting. Also, damage to an organization's reputation may result from an SEC action, which may discourage clients from engaging in business and investors from contributing capital.

More generally, the external reporting issue highlights the cost of small business compliance with Dodd-Frank, which is a result of both anti-retaliation and monetary incentives. Specifically, Dodd-Frank

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[121] Tarun, *supra* note 77. *See also* Hinchey, *supra* note 77. Voluntary reporting may be a result of the outrage that can be associated with securities fraud, in contrast to tax fraud. See discussion, *supra* Part III(A)(2).

[122] *SEC Proposed Rules*, *supra* note 45, at 104. *See also* Bruce Carton, *Pitfalls Emerge in Dodd-Frank Whistleblower Provisions*, SECURITIES DOCKET, Sep. 9, 2010, *available at* http://www.securitiesdocket.com/2010/09/09/pitfalls-emerge-in-dodd-frank-whistleblower-bounty-provision.

[123] *Id. See also* Pub.L. No. 111-203, sec. 922, §21F(b)(1), 124 Stat. 1376 (2010). *But see SEC Proposed Rules, supra* note 45, at 112 (proposing a mechanism whereby whistleblowers may report internally and still receive a bounty).

[124] Carton, *supra* note 122. Whistleblowers are only entitled to awards under the new bounty program if they provide original information. Pub.L. No. 111-203, sec. 922(a), § 21F(b)(1), 124 Stat. 1376 (2010). *See also SEC Proposed Rules, supra* note 45, at 31-47 (defining "original information").

burdens small business insomuch as they must implement and maintain internal controls designed to avoid whistleblower retaliation liability.[125] Although Dodd-Frank exempts businesses with market capitalization smaller than $75M from SOX 404 regulatory requirements,[126] the whistleblower provisions may effectively leave in place the burden of closely scrutinizing internal controls, which is a burden similar to SOX 404.[127] Additional training or controls to prevent whistleblower retaliation may even be necessary due to the threat of increased whistleblower reporting and protection.[128] For example, subsidiaries of public companies may require management training to avoid whistleblower retaliation and all businesses may need new policies to encourage internal reporting.[129]

Reasoning in the SEC's proposed rules is evidence that the whistleblower provisions create a compliance burden. The SEC explains that it will not require whistleblowers to report fraud internally before reporting to the SEC because corporate compliance systems may not be "robust" at all businesses.[130] Putting aside the rebuttal that poor compliance systems do not preclude external reporting, the SEC's reasoning emphasizes that the new provisions cover businesses with poor internal compliance systems that must be improved to comply with the new laws. Ironically, this result contravenes Dodd-Frank's policy objective to relieve small businesses from the internal control burdens such as those in Section 404.[131] As a final consideration, compliance burdens may also be an unnecessarily duplicative

[125] *See* MICHAEL DELIKAT & RENEE PHILLIPS, CORPORATE WHISTLEBLOWING IN THE SARBANES-OXLEY ERA § 10:1 (2010) (outlining measures businesses can implement to comply with SOX). Internal controls designed to avoid whistleblower retaliation are increasingly important with an increasing number of whistleblowers likely to result from additional whistleblower incentives. *See* Holzer and Johnson, *supra* note 43. Moreover, Dodd-Frank expands the coverage of whistleblower protection to affiliates and subsidiaries of public companies, which will trigger the need for compliance among these businesses. *See also* Pub.L. No. 111-203, § 929A, 124 Stat. 1376 (2010).
[126] Pub.L. No. 111-203, § 989G(a), 124 Stat. 1376 (2010).
[127] Roberta Romano, *Does the Sarbanes-Oxley Act Have a Future?*, 26, YALE J. ON REG. 229, 239-43 (noting that business must implement controls and incur costs to comply with SOX).
[128] Pub.L. No. 111-203, § 989G(b), 124 Stat. 1376 (2010).
[129] See discussion *infra* Part V(A).
[130] *SEC Proposed Rules*, *supra* note 45, at 34.
[131] *See* Pub.L. No. 111-203, § 989G(a), 124 Stat. 1376 (2010). *See* DELIKAT & PHILLIPS, *supra* note 125. As Dodd-Frank increases whistleblower incentives and protection, prudent business practices will maintain internal controls to avoid whistleblower retaliation liability. *See id.*

function in light of other fraud detection measures already in place including external audits, internal audits, and existing internal controls.[132]

Third, Dodd-Frank implicitly mandates SEC fraud enforcement strategy rather than deferring to administrative expertise to set the enforcement agenda.[133] Dodd-Frank does so by creating administrative costs that limit resources available to pursue alternative enforcement methods. Specific new costs facing the SEC include costs associated with operating a new office,[134] investigating additional whistleblower tips,[135] enforcement actions based upon those tips,[136] and paying mandatory whistleblower bounties.[137] Because of these costs, the SEC has fewer resources at its disposal to set its enforcement strategy at its discretion.

One alternative SEC enforcement strategy is using test cases to signal to the market or "draw a line in the sand" stating that their fraud enforcement is focused on deterring a particular fraud type.[138] As part of a markedly distinct strategy, Dodd-Frank mandates that the new SEC office to implement the bounty program[139] create a report to assess whether whistleblower tips are handled with administrative efficiency.[140] Thus, in contrast to the test case strategy, the SEC is expected to pursue each case reported by a whistleblower, regardless of whether it is part of their strategy of identifying test cases.

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[132] Michael K. Shaub and James F. Brown, Jr., *Whistleblowing management accountants: a US view in* GERALD VINTEN, WHISTLEBLOWING: SUBVERSION OR CORPORATE CITIZENSHIP 107 (1994) (noting accountants role in maintaining internal controls, internal auditors role in monitoring managerial accountants, and external auditors role in attesting to fair presentation of financial statements). *See also* Association for Certified Fraud Examiners, *2008 Report to the Nation on Occupational Fraud & Abuse, available at* http://www.intercedeservices.com/downloads/2008-rttn.pdf . Although the ACFE report examines all occupational fraud, securities fraud is a subset of occupational fraud which may be detected by these measures.

[133] Carton, *supra* note 122 (citing Richard Wallace, Esquire).

[134] *See* Pub.L. 111-203, § 924(d), 124 Stat. 1376 (2010).

[135] Holzer and Johnson, *supra* note 43 (noting that additional whistleblower tips are expected as a result of Dodd-Frank). *See also* Reisinger, *supra* note 43.

[136] Michael Lowman, *SEC Compliance Best Practices Leading Lawyers on Working with the SEC, Structuring Effective Compliance Programs, and Evaluating Securities Developments*, 2010 WL 894704 at 2 (Mar. 2010).

[137] Dodd-Frank requires that whistleblowers provide original information leading to successful SEC or CFTC enforcement actions with proceeds greater than $1,000,000 receive, *at a minimum*, 10% of the proceeds as an award. Pub.L. 111-203, sec. 922(a), § 21F(b)(1)(A), 124 Stat. 1376 (2010).

[138] Lowman, *supra* note 136, at 2 (stating that "[i]f there are certain people they feel are gatekeepers ... the agency will take marginal dollar value cases if they can advance a message they believe will advance the SEC's enforcement program). *See also* Carton, *supra* note 122.

[139] Pub.L. 111-203, § 924(d), 124 Stat. 1376 (2010).

[140] *Id.* § 922(d).

The Congressional enforcement directive is especially unfortunate because test cases can be very effective and require many resources. To demonstrate expense, the SEC recently spent hundreds of thousands of dollars pursuing a small insider trading case that only resulted in a $110 client gross profit specifically to deter insider trading involving unregistered broker/dealers.[141] The SEC was willing to incur the high costs because it expects that other cases of insider trading will be deterred by the threat of enforcement.

Another case illustrates the magnitude and importance of test cases. Days prior to Dodd-Frank's enactment, the SEC reached a $550M settlement with Goldman Sachs as a result of an SEC investigation.[142] The case was designed, at least in part, to signal to the market that the SEC was strengthening enforcement efforts against deceptive collateralized debt obligation sales.[143] Significantly, it is probable that the SEC incurred extremely high out-of-pocket expenses pursuing the settlement.[144] By pursuing this individual case, the SEC was addressing the subprime mortgage crisis that had a devastating effect on the economy. Had Dodd-Frank been in place prior to the Goldman settlement, the SEC may have also been required to pay a large and unnecessary whistleblower bounty ($55M-$165M) or litigate against whistleblowers claiming a bounty.[145] Taken in this light, Dodd-Frank's costs will mandate SEC enforcement strategy and limit resources available for the SEC to pursue test cases at its discretion.

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[141] Lowman, *supra* note 136.

[142] Andrew Martin, *S.E.C. puts Wall St. on Notice*, NY TIMES, Apr. 19, 2010, *available at* http://dealbook.blogs.nytimes.com/2010/04/19/s-e-c-puts-wall-st-on-notice.

[143] *Id. See also* Carton, *supra* note 122.

[144] Although SEC enforcement expenses are not publicly available, the SEC unquestionably spends considerable amounts for out-of-pocket expenses and attorney time related to enforcement actions. Lowman, *supra* note 136. Regarding the $550M Goldman Sachs-SEC settlement, the long duration of the investigation which lasted over a year, the large size of the alleged fraud which resulted in a $550M settlement and the complexity of the alleged fraud involving sophisticated collateralized debt obligations, all indicate that the SEC incurred significant expenditures during the investigation. Lindsay Fortado and Christine Harper, *Goldman Sachs Fined $27 Million for Not Reporting Probe*, BLOOMBERG NEWS, Sep. 9, 2010, *available at* http://www.bloomberg.com/news/2010-09-09/goldman-sachs-fined-27-million-by-u-k-for-failing-to-report-tourre-probe.html (noting that the SEC has been investigating the Goldman Sachs Abacus deal since August 2008). Patricia Hurtado and Christine Harper, *SEC Settlement with Goldman Sachs for $550 Million Approved by U.S. Judge*, BLOOMBERG NEWS, Jul. 21, 2010, *available at* http://www.bloomberg.com/news/2010-07-20/goldman-sachs-settlement-with-sec-for-550-million-approved-by-u-s-judge.html.

[145] As an alternative to whistleblower leads, poor investment performance often leads to regulatory investigation of securities fraud. *See* Carrick Mollenkamp et al., *iSEC Probes Soured Deals*, WALL ST. J, Apr. 19, 2010 (noting that the SEC is investigating securities fraud in underperforming funds). *See also* Gretchen Mortgenson and Landon

Fourth, Dodd-Frank's requirement to award whistleblowers *at least* a 10% bounty is both overreaching and misplaced.[146] Specifically, the 10% floor is overreaching because it may not be cost-effective. That is, the marginal utility of providing a whistleblower with, for example, $7M rather than $5M, may not be a meaningful incentive to report fraud. Further, there is little evidence in the legislative history of Dodd-Frank that Congress contemplated whether costs associated with managing additional whistleblower tips and litigating whistleblower claims might exceed the residual amount of fraud enforcement proceeds deposited in the Investor Protection Fund once bounties are paid from the Fund.[147] If that is the case, Dodd-Frank may not be cost-effective.

Moreover, the 10% floor is misplaced because it may not provide certainty as intended.[148] Whistleblower bounties are anything but certain due to the possibility that other whistleblowers will subsequently provide information entitling them to a portion of the bounty.[149] As noted above, ambiguity about the reporting standard or securities law can also decrease certainty.[150] Thus, although whistleblower bounties are likely to be unnecessarily high with little marginal utility, they ironically may not provide certainty as intended.

Finally, the new bounty program is likely to lead to unnecessary litigation. One reason is because Dodd-Frank entitles whistleblowers to appeal the amount of a bounty awarded by the SEC.[151] Under the new bounty program, bounties are determined on an *ad hoc* basis using subjective factors, but must be

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Thomas, *A Glare on Goldman, From U.S. and Beyond*, NY TIMES, Apr. 18, 2010, *available at* http://www.nytimes.com/2010/04/19/business/19investors.html (noting that members of Congress have been requesting that the SEC investigate mortgage securities deals due to government investment in financial institutions like A.I.G.).

[146] S. REP. NO. 111-176, at 111 (2009) (stating that the "critical component of the whistleblower program is the minimum payout that any individual could look towards in determining whether to take the enormous risk of blowing the whistle in calling attention to fraud"). *See also* Pub.L. 111-203, sec. 922(a), § 21F(b)(1)(A), 124 Stat. 1376 (2010).

[147] *But see* S. REP. NO. 111-176, at 244 (2009) (stating the "minority view" of the Dodd-Frank bill).

[148] *Id.* at 111.

[149] Pub.L. No. 111-203, sec. 922(a), §21F(b)(1), 124 Stat. 1376 (2010). *See also SEC Proposed Rules, supra* note 45, at 48.

[150] *SEC Proposed Rules, supra* note 45, at 112 (stating that whistleblowers may be mistaken about securities laws).

[151] Pub.L. No. 111-203, sec. 922(a), §21F(f), 124 Stat. 1376 (2010).

within 10-30% of the penalty collected as a result of the tip.[152] Subjective criteria make award amounts an easy target to dispute. Further, appeals are incentivized because successful appeals could yield lofty rewards representing a portion of high penalties in SEC fraud actions.[153]

Dodd-Frank also invites litigation to define key terms including "original information."[154] Without a clear definition of original information, a whistleblower's burden of proof is ambiguous and litigation is needed to specify the level of detail required to obtain a whistleblower award.[155] For example, whistleblowers with less conclusive evidence of fraud, or perhaps just a hunch, may file claims seeking an award.[156] Moreover, secondary whistleblowers providing information about fraud that has already been reported may file a claim seeking a portion of the whistleblower award.[157] Admittedly, the SEC's proposed rules provide some guidance to limit uncertainty and curb litigation,[158] but discretionary standards nonetheless provide potential for considerable litigation over the amount of a Dodd-Frank bounty.

IV. PROPOSAL

There are a myriad of ways to amend or implement Dodd-Frank's whistleblower provisions to achieve the purpose of the Act while substantially reducing its costs. A threshold issue is whether the appropriate recourse is legislatively amending Dodd-Frank or administrative action, including management efficiency and rulemaking. Unfortunately, the current political environment suggests that it

[152] *Id. See also SEC Proposed Rules*, *supra* note 45, at 49-51. Some have also criticized the Dodd-Frank bounty program for eliminating the SEC's discretion to award bounties in amounts less than 10% of the fraud penalty. S. REP. NO. 111-176, at 244 (2009).
[153] Dodd-Frank entitles whistleblowers to bounties only if a SEC or CFTC action results in monetary sanctions greater than $1,000,000. Pub.L. No. 111-203, sec. 922, § 21F(a)(1), 124 Stat. 1376 (2010).
[154] Pub.L. No. 111-203, sec. 922, § 21F §(b)(1), 124 Stat. 1376 (2010). *See also id.* sec. 922(a), § 21F(a)(3).
[155] Telephone Interview with Dan Sandman, U.S. Steel Vice Chairman and Chief Legal & Administrative Officer and General Counsel (Ret.), (Oct. 15, 2010).
[156] *See e.g.* Kolz, *supra* note 50. Kolz describes the case of Joseph Piacentile, a whistleblower who does not report fraud as an employee or business partner, but instead in reliance of potentially unreliable secondhand information resulting from his own investigations. *Id.* As there is little or no disincentive to deter unreliable whistleblower tips, one lawyer has noted that "even if [Piacentile] hits a couple, his batting average is terrible." *Id. But see SEC Proposed Rules*, *supra* note 45, at 39.
[157] *SEC Proposed Rules*, *supra* note 45, at 48. *See also* Pub.L. No. 111-203, sec. 922, § 21F §(b)(1), 124 Stat. 1376 (2010). *See also e.g.* Kolz, *supra* note 50.
[158] *SEC Proposed Rules*, *supra* note 45, at 31-42. Pub.L. No. 111-203, § 924(a), 124 Stat. 1376 (2010).

is unlikely Dodd-Frank will be amended.[159] Nonetheless, administrative remedies exist and legislative remedies are available should the political environment change.

A. *Prospects for Legislatively Amending Dodd-Frank*

Notwithstanding any plausible reform proposals, it is unlikely that Congress will amend the Dodd-Frank whistleblower provisions. One factor indicating that Congress will not amend Dodd-Frank is the influence of the trial lawyer lobby. Admittedly, it is difficult to measure a particular special interest's influence because it is difficult to know the specific purpose behind political contributions.[160] Exacerbating this difficulty are political contributions made not just by political organizations, but trial lawyers individually, their families, and law firms.[161] Notwithstanding this difficulty, the American Association for Justice, which is the preeminent trial lawyer lobbying association, is a heavy Democratic contributor and regarded as influential upon Congress and the Obama administration during Dodd-Frank's enactment.[162]

If incentives suggest the purpose behind contributions, the trial lawyer lobby is certainly a likely promoter of whistleblower awards because attorneys stand to gain considerably from whistleblower

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[159] *But see* Jeff Zeleny, *GOP Captures House, but not Senate*, NY TIMES, Nov. 2, 2010, *available at* http://www.nytimes.com/2010/11/03/us/politics/03elect.html. Majority control of the U.S. House of Representatives will shift from Democrats to Republicans in 2011, which may affect the viability of legislative reform. *Id.*

[160] *See* WILLIAM N. ESKRIDGE, JR. ET AL., CASES AND MATERIALS ON LEGISLATION: STATUTES AND THE CREATION OF PUBLIC POLICY 305 (4th Ed. 2007) (noting uncertainty, in the context of bribery, regarding situations that "fall somewhere along the spectrum between clearly legitimate arrangements and patently corrupt deals"). Contributions to a candidate or organization may be a result of a donor's wish to support a variety of issues or candidates for past or future behavior. *Id.* at 304. For information about the American Association for Justice Political Action Committee contributions and expenditures, visit http://www.opensecrets.org/pacs/lookup2.php?strID=C00024521&cycle=2010.

[161] Chris Rizo, *Group says trial lawyers actually gave $35 Million to political causes*, LEGALNEWSLINE.COM (March 15, 2010), *available at*: http://www.legalnewsline.com/news/226145-group-says-trial-lawyers-actually-gave-35-million-to-political-causes.

[162] David Ingram, *Trial Lawyers Sticking With Democratic Party*, THE NAT'L L. J., Oct. 19, 2010, *available at* http://www.law.com/jsp/article.jsp?id=1202473540921&Trial_Lawyers_Sticking_With_Democratic_Party. *See also* David Freddoso, *Will Obama administration give trial lawyers a $1.6 billion tax break?*, THE WASHINGTON EXAMINER, Jul. 14, 2010, *available at* http://www.washingtonexaminer.com/opinion/blogs/beltway-confidential/will-obama-administration-give-trial-lawyers-a-16-billion-tax-break-98413014.html. *But see* Kara Rowland, *Trial Lawyer Lobby Sinks $6.2M in Debt*, THE WASHINGTON TIMES (September 28, 2009), *available at* http://www.washingtontimes.com/news/2009/sep/28/trial-lawyers-lobby-is-62-m-in-debt/ (noting that the trial lawyer lobby may have had limited influence on Dodd-Frank if they only have limited financial resources).

litigation.[163] The SEC bounty program is expected to be a significant boon to trial lawyers just as *qui tam* actions under the False Claims Act earn trial lawyers handsome fees.[164] Moreover, trial lawyers benefit not only from legal fees taking a portion of lucrative whistleblower bounties, but also benefit in negotiations with employers on behalf of terminated employees claiming whistleblower protection.[165] Thus, the presence of trial lawyers' interest stands as a potential bar to more thoughtful whistleblower reform and desirable policy.

Another factor indicating that Congress will not amend Dodd-Frank is the prospect that amendment will open the door to amending other Dodd-Frank provisions or other legislation enacted by the 111th Congress, including the Patient Protection and Affordable Care Act ("PPACA").[166] To illustrate, consider that Congress recently declined to amend the PPACA to eliminate a new 1099 reporting requirement, which is designed to close the tax gap and pay for health care reform.[167] The PPACA 1099 reporting requirement requires that all businesses prepare 1099s for goods and services purchased from vendors which cumulatively exceed $600 during the course of the taxable year.[168]

However, the 1099 reporting requirement may not have been carefully contemplated. There is a considerable compliance burden placed on small business.[169] Also, it is not clear that the 1099 requirement will increase income reporting as intended because businesses may not comply and, even with business compliance, it will be administratively difficult for the IRS to process the information in a

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[163] Harker et al., *supra* note 34, at 780-81 (noting that trial lawyers may benefit handsomely from the Dodd-Frank whistleblower provisions).
[164] Harris, *supra* note 90.
[165] William Olsen, *Major Whistleblower Provisions in Financial Regulation Bill*, CATO INSTITUTE (Jul. 16. 2010), *available at:* http://www.cato-at-liberty.org/major-whistleblower-provisions-in-financial-regulation-bill/.
[166] Pub.L. 111-148, 124 Stat. 119 (2010).
[167] Alexander Bolton, *Senate Defeats Plan to Strip Filing Requirement from Health Care Law*, THE HILL, Sep. 14, 2010, *available at* http://thehill.com/homenews/senate/118637-senate-defeats-effort-to-strip-1099-requirement-from-health-law.
[168] Pub.L. 111-148, § 9006, 124 Stat. 119 (2010). "Current law dictates that only services provided in excess of $600 must be reported via form 1099 and that corporations (with the exception of attorneys) are exempt from receiving 1099s." Amy Mignogna, *Concern over new 1099 reporting requirement gaining momentum*, CPA VOICE at 7 (Aug. 2010). Notably, credit card transactions are exempt from this requirement. *Id.*
[169] Robert Pear, *Many Push for Repeal for Repeal of Tax Provision in Health Law*, NY TIMES, Sep. 11, 2010, *available at* http://www.nytimes.com/2010/09/12/health/policy/12health.html?_r=1. Democratic support for repealing the requirement suggests that it may not have been carefully contemplated in light of the fact Democratic votes were the primary source of support to enact the PPACA. *Id.*

useful way.[170] Notwithstanding the negative implications of the 1099 requirement, Congress rejected proposals to eliminate or amend the requirement, in part due to reluctance to open the door to amend other legislation and in part due to an inability to replace expected tax revenue.[171] As applied to Dodd-Frank, it is unlikely that Congress will amend the new whistleblower provisions because it would open the door to amending other controversial and distantly related Dodd-Frank provisions.

B. *Administrative Action*

Administrative action is a plausible way to remedy the costs of the Dodd-Frank bounty program because it avoids the uncertain legislative process. The SEC and CFTC may achieve Dodd-Frank's purpose and limit associated costs by: (1) adopting practices to better manage whistleblower tips; and (2) carefully implementing Dodd-Frank through rulemaking.

1. *Administrative Efficiency: Improving Tip Management*

As noted at the outset, whistleblower reform cannot achieve its policy ends if there are not administrative structures in place to properly manage whistleblower tips. That is, no incentive to report fraud, monetary or otherwise, will address the underlying problems if the enforcement agency does not act on fraud reports. With this in mind, administrative reform in the way the SEC manages whistleblower tips and its bounty program should have been implemented and assessed prior to enacting Dodd-Frank's more sweeping and costly changes.[172] If assessment of administrative reform demonstrated improved fraud enforcement, many of the Dodd-Frank provisions may prove overreaching or even unnecessary because Dodd-Frank's purpose would have already been achieved. Put another way, it is possible, perhaps even likely, that existing voluntary whistleblower reports are sufficient to achieve Dodd-Frank's purpose of exposing Ponzi schemes and structured finance fraud, but that agencies have not been responsive enough to use the tips.[173]

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[170] Amy Mignogna, *Federal tax proposals heat up over summer months*, CPA VOICE, at 11 (Sep. 2010).
[171] Pear, *supra* note 169 (stating that "[t]he White House is nervous about a repeal, fearing that it could set a precedent for rolling back other unpopular features of the law.").
[172] *See Inspector General Report*, *supra* note 26, at vi-vii.
[173] See discussion *supra* Part III(A).

A March 2010 Inspector General Report provides proposals to reform the SEC's existing bounty program, many of which are applicable to managing whistleblower tips even in the absence of a bounty program. [174] Alternatively, even if enacting a broad bounty program encompassing all securities fraud, all the recommendations may be implemented without increasing the amount of whistleblower awards. Interestingly, Dodd-Frank calls for another Inspector General report to assess the new whistleblower provisions despite the presence of the aforementioned report.[175] As the Dodd-Frank whistleblower provisions were enacted prior to the implementation and assessment of existing recommendations, it is questionable whether a new Inspector General Report will garner attention necessary to result in administrative reform and improved enforcement.

Nonetheless, the existing Inspector General Report reveals that the SEC's insider trading bounty program had basic deficiencies and provides the following corresponding recommendations:[176]

- The SEC's bounty program has made few payments to date and should be *more publicized*.[177]
- Information on the SEC's website about applying for a bounty is misleading.[178] As such, there should be *a standardized form to report illegal activity* and policies for following up with whistleblower tips.[179]
- Existing criteria (pre-Dodd-Frank) for awarding bounties is overly vague. There should be *more objective criteria for determining whistleblower award amounts*.[180]
- The SEC does not update whistleblowers with the status of their case and should *communicate with whistleblowers more* to encourage reporting additional information.[181]
- Bounty applications are handled on an *ad hoc* basis and better tracking of applications should result in *more timely review*.[182]
- Bounty applicant's files sometimes contain incomplete information and the SEC should *require a bounty file with specific information*.[183]

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[174] *See Inspector General Report*, *supra* note 26, at vi-vii.
[175] Pub.L. 111-203, § 922(d), 124 Stat. 1376 (2010).
[176] *Inspector General Report*, *supra* note 26, at 4-22.
[177] *Id.* at 8.
[178] *Id.*
[179] *Id.* at 11.
[180] *Id.* at 12-13. It should be noted that Dodd-Frank provides several factors for determining the amount of whistleblower awards. Pub.L. No. 111-203, sec. 922(a), § 21F(c)(1), 124 Stat. 1376 (2010).
[181] *Inspector General Report*, *supra* note 26, at 13-15.
[182] *Id.* at 15-19.
[183] *Id.* at 19-20.

- The SEC should *implement best practices from other agencies*.[184]

Indeed, the SEC's proposed rules provide measures that are designed to improve information management, including clear reporting procedures,[185] standardized forms,[186] and communication procedures.[187] While the SEC has expressed concern that these measures are procedural hurdles that may be overly burdensome and deter whistleblower reporting,[188] these measures provide critical assurances to serious whistleblowers and should be adopted. Notwithstanding any new SEC rules, Dodd-Frank's sweeping reform of whistleblower law may have been unnecessary in light of several basic recommendations to better manage and utilize existing whistleblower reports to enforce fraud.

2. *Administrative Rulemaking*

Despite potentially heavy costs that may result from the Dodd-Frank bounty program, carefully written SEC rules can limit such costs and maintain the essence of Dodd-Frank moving forward.[189] Specifically, rules can be written to implement a narrow interpretation of key terms including "original information"[190] and "whistleblower,"[191] which are used to establish when whistleblower bounties are warranted.[192]

A rule implementing the bounty program could take multiple forms. One way is to write a rule that is consistent with the existing definition of key terms in Dodd-Frank, but providing greater detail to narrow the scope.[193] In fact, the SEC's proposed rules take this approach.[194] Another way is to write a rule to provide potential whistleblowers with specific and objective criteria required to obtain a

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[184] *Id.* at 20-22.
[185] *SEC Proposed Rules*, *supra* note 45, at 60.
[186] *Id.* at 62.
[187] *Id.* at 84.
[188] *Id.* at 116.
[189] Pub.L. No. 111-203, sec. 922(a), § 21F(j), 124 Stat. 1376 (2010). Dodd-Frank gives the SEC 270 days, until April 21, 2011, to write rules implementing the bounty program. *Id.* § 924(a). Charles Koch, Jr., ADMIN. L. & PRAC. § 4.1 (3d ed. 2010) (stating that "rulemaking is foremost a policymaking device").
[190] Pub.L. No. 111-203, sec. 922(a), § 21F(a)(3), 124 Stat. 1376 (2010).
[191] *Id.* sec. 922(a), § 21F(a)(6).
[192] *Id.* sec. 922(a), § 21F(b)(1).
[193] Koch, *supra* note 189.
[194] *See e.g. SEC Proposed Rules, supra* note 45, at 31-47 (defining "original information").

whistleblower bounty. In a similar vein, safe harbor rules in securities regulation provide certainty to shield an underwriter, for example, from liability.[195]

The policy behind a rule outlining objective whistleblower bounty criteria benefits both the whistleblower and the taxpayer. First, such a rule provides whistleblowers with certainty and encourages reporting just as Dodd-Frank's 10% floor on whistleblower bounties is designed to do the same.[196] Second, a rule taking this shape deters frivolous tips made as a result of hunches about fraud or a misunderstanding of the law because it puts whistleblowers on notice that vague reports will not garner awards.

Regardless of the method used to interpret key terms and implement the bounty program, a rule should preserve the purpose of Dodd-Frank and be narrowly-tailored to avoid costs. In addition to the recently proposed SEC rules,[197] rules that may achieve the purpose of Dodd-Frank and limits costs include: (1) a heightened "pleading" standard; (2) standing requirements; and (3) limiting the type of fraud which may lead to a whistleblower award.

a. *"Pleading" with Particularity*

A heightened pleading/reporting standard may be incorporated into the definition of original information such that incomplete information and hunches will not lead to an award. Indeed, the SEC's proposed rules provide some guidance to whistleblowers as to what requirements must be met to earn a bounty and, as a result, will reduce unreliable tips made due to a misunderstanding of the law.[198] Specifically, the proposed rules require that whistleblowers: cause the SEC to open an investigation; provide information "significantly contributing" to the success of the enforcement action; and provide evidence which will "lead to a successful enforcement action."[199]

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[195] *See e.g.* Regulation D, 17 C.F.R. §230.501 *et seq.*
[196] *See e.g.* Andrew Ross Sorkin, *So What is Insider Trading?* NY TIMES DEALBOOK BLOG, Oct. 25, 2010, *available at* http://dealbook.blogs.nytimes.com/2010/10/25/sorkin-so-what-is-insider-trading/?ref=business (noting the benefit of certainty and clear rules in the insider trading context).
[197] *See generally SEC Proposed Rules*, *supra* note 45.
[198] *Id.* at 38-39.
[199] *Id.*

However, the proposed rules do not go far enough. A heightened pleading/reporting standard should be even more specific than the proposed rules and require whistleblowers to identify culpable individuals, the motive for fraud, where the fraud occurred, and the specific behavior constituting fraud.[200] In addition, a rule could require that whistleblowers provide specific types of reliable evidence.

From a procedural standpoint, the heightened pleading standard to prove fraud in federal court under Fed. R. Civ. P. 9(b) should extend to the whistleblower reporting context.[201] *Qui tam* actions brought by whistleblowers under the FCA and on behalf of the U.S. government, a similar context, require heightened pleading.[202] Moreover, in the securities litigation context, Dodd-Frank requires claims against credit rating agencies to plead intent with particularity.[203] It is reasonable to extend heightened pleading/reporting as a requirement for whistleblower bounties because pleading with particularity is required to enforce the securities laws in federal court and therefore measurably benefit from the tip.[204]

From an efficiency standpoint, heightened pleading may limit many costs of the bounty program. First, frivolous tips based upon hunches or without evidence may be deterred as clearly outside the scope of the bounty program. Second, whistleblowers may be incentivized to gather and provide more complete information before reporting fraud, which will reduce agency investigatory costs. Third, the business accused of fraud would be in a better position to defend against whistleblower claims because they will have a better understanding of the fraud allegations against them.[205] Bounties should therefore be awarded only to those whistleblowers making fraud allegations with particularity.

b. *Standing Requirement to Obtain Whistleblower Bounty*

Another requirement that could limit the costs of the bounty program through rulemaking is a standing requirement. Ideally, a standing requirement will minimize the cost of frivolous tips made by

[200] Fed. R. Civ. P. 9(b). *See also Stradford v. Zurich Ins. Co,* 2002 WL 31027517, at 3 (S.D.N.Y. 2002) (noting that "[Fed. R. Civ. P. 9(b)] requires that the time, place, and nature of the [alleged] misrepresentations be disclosed to the party accused of fraud").
[201] Fed. R. Civ. P. 9(b).
[202] *United States v. Eastman Kodak Co., et al.*, Civil Action No. 95-12545-PBS (D. Mass. May 31, 2000).
[203] Pub.L. No. 111-203, § 933(b)(2)(B), 124 Stat. 1376 (2010).
[204] The SEC uses a similar line of reasoning to justify a whistleblower's evidentiary burden. *See SEC Proposed Rules*, *supra* note 45, at 39-40.
[205] *Stradford*, 2002 WL 31027517, at 3 (noting that "the primary purpose of Rule 9(b) is to afford a litigant accused of fraud fair notice of the claim and the factual ground upon which it is based.").

profit-minded persons reporting hunches and make ineligible whistleblowers who are otherwise required to report. Indeed, the SEC's proposed rules place several restrictions on whistleblower standing, including rules that preclude bounties for information obtained under pre-existing duties or by individuals with conflicting responsibilities.[206] For example, auditors reporting fraud pursuant to their duties under Section 10A are not eligible for a whistleblower bounty.[207]

However, SEC rules should restrict standing even further. The word "whistleblower" could be limited to employees and those in contractual privity with the wrongdoer (e.g. business partners and vendors).[208] Employees and parties in contractual privity with the wrongdoer should be eligible for bounties because their relationship to a wrongdoer puts them in a position to obtain inside information and their professional responsibilities do not necessarily compel disclosure.[209]

The story of one professional whistleblower heeds a cautionary tale.[210] Professional whistleblower Joe Piacentile ("Dr. Joe")[211] *and his attorneys*[212] have amassed a small fortune making FCA claims based on information obtained from private investigations.[213] To obtain information, Dr. Joe often poses as business partners or employees.[214] While Dr. Joe sometimes obtains and reports information leading to an award, the overwhelming majority of his tips do not lead to enforcement actions.[215] In light of Dr. Joe's often poor but nonetheless frequent tips, he imposes unnecessary costs on businesses unaware of his misrepresentations and on agencies conducting fraud investigations.

Public policy should not support granting professional whistleblowers standing to obtain bounties. First, investigations should not be outsourced to professional whistleblowers because agencies

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[206] *SEC Proposed Rules*, *supra* note 45, at 19-20.
[207] *Id.* at 22.
[208] Pub.L. No. 111-203, sec. 922(a), § 21F(a)(6), 124 Stat. 1376 (2010). In contrast, the SEC's proposed rules limit standing by defining the term "independent knowledge," which is required for a bounty, to except information obtained by certain persons or in certain situations. *SEC Proposed Rules*, *supra* note 45, at 19.
[209] S. REP. NO. 111-176, at 110 (2009).
[210] Kolz, *supra* note 50.
[211] Mr. Piacentile is known as "Dr. Joe" by the *qui tam* bar. *Id.*
[212] *Id.* (noting that many lawyers from the "relatively clubby" *qui tam* bar have represented Dr. Joe). *See also* discussion *infra* Part IV(B).
[213] Dr. Joe has made at least $17 million in whistleblower awards. *Id.*
[214] *Id.*
[215] *Id.*

are presumably better investigators due to experience, resource availability, and reasonable compensation (i.e. do not require whistleblower bounties). Dodd-Frank outsources enforcement to whistleblowers only under the assumption that whistleblowers are in a better position to obtain relevant information.[216] Put simply, professional whistleblowers do not support Dodd-Frank's policy objectives because they are not naturally in a better position to obtain material inside information than existing government agencies.

Second, professional whistleblowers may cause whistleblower awards to be shared and detract from the awards of more legitimate whistleblowers.[217] One strategy employed by Dr. Joe is to obtain vague information and strive to be the first whistleblower to report fraud. By doing so, Dr. Joe can "piggyback" on information provided by other whistleblowers even if his information, standing alone, would not have been sufficient to lead to an enforcement action. Candidly, Dr. Joe is a rare instance of a professional whistleblower and many of the specifics of his tips are left under seal with courts. Nonetheless, Dr. Joe's story illustrates the need to narrow whistleblower standing to avoid mischief.

c. *Awarding Bounties for Reporting Only Certain Types of Securities Fraud*

Dodd-Frank was designed to address the problems with U.S. capital markets[218] and its whistleblower provisions were specifically included in response to notorious Ponzi schemes.[219] A broad whistleblower program incentivizing whistleblowers to report all securities fraud therefore goes beyond the scope of Dodd-Frank's policy objectives. By incentivizing tangentially related fraud, some whistleblower reports will have abstract benefits but nonetheless incur heavy costs.[220] For example, whistleblowers reporting violations of the FCPA's anti-bribery provisions will be doing little to protect U.S. capital markets, but nonetheless impose costs on businesses and the SEC.[221] Past securities legislation has avoided this oddity by tailoring whistleblower bounty programs to the specific fraud they

[216] S. REP. NO. 111-176, at 110 (2009).
[217] Pub.L. No. 111-203, sec. 922(a), § 21F(j), 124 Stat. 1376 (2010). *See also* Kolz *supra* note 50 (stating that the FCA requires relator bounties to be awarded as a group).
[218] S. REP. NO. 111-176, at 2-4 (2009).
[219] *Id.* at 110.
[220] *SEC Proposed Rules*, *supra* note 45, at 110.
[221] *See e.g.* Edward Wyatt, *Oil and Gas Bribery Case Settled for $236 Million*, NY TIMES, Nov. 4, 2010, *available at* http://www.nytimes.com/2010/11/05/business/global/05bribe.html?ref=business.

were meant to deter. Specifically, the Insider Trading and Securities Enforcement Act of 1988 was enacted in response to insider trading scandals and accordingly instituted a bounty program limited to insider trading.[222]

To address Dodd-Frank's policy anomaly, the SEC could define "original information" in such a way that only reporting the type of securities fraud Dodd-Frank was intended to address would warrant a whistleblower award. Legislative history clearly shows that original information was intended to mean "new" or "novel."[223] However, in addition to new or novel, rules can be written to interpret original information as also meaning "origin" or "beginning,"[224] as in the origins of the financial crisis Dodd-Frank is intended to address.[225] Applying this interpretation, a rule could limit whistleblower bounties to novel reports of structured finance fraud, Ponzi schemes, or financial reporting under the FCPA and SOX 404.

Candidly, a rule adopting this interpretation could be overruled by courts applying *Chevron* on the ground that it is not consistent with legislative intent or against Dodd-Frank's plain meaning.[226] Nonetheless, the SEC has indicated that they have authority to define the scope of Dodd-Frank through rulemaking.[227] Also, as an alternative bar, the public may voice concerns about a limiting rule through public comment.[228]

Regardless, a rule limiting the type of fraud within the bounty program is a potential way for the SEC to deter tips about unrelated fraud. Moreover, it is a way for the SEC to pursue an enforcement

[222] The existing SEC insider trading bounty program was enacted in response to scandals at Drexel Burnham Lambert Inc. and other banks. H. REP. NO. 100-910, at 12 (1988).
[223] S. REP. NO. 111-176, at 111 (2009).
[224] Definition of "Original," FREE MERRIAM-WEBSTER DICTIONARY, *available at* http://www.merriam-webster.com/dictionary/original.
[225] *Id.* at 2-4. *See also* Pub.L. No. 111-203, § 931(d), 124 Stat. 1376 (2010).
[226] *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). Under the *Chevron* doctrine, administrative rules are upheld if they are: (1) consistent with congressional intent; and (2) reasonable. *Id.* at 842-43. As applied to the present case, the interpretation would probably be considered reasonable in light of administrative expertise and political accountability. *Id.* at 834-44. However, there may be an issue as to whether interpreting original information as "origin" is against Congressional intent. Specifically, the text and legislative history establish that original information means "new" or "novel," but it is not clear whether the "origin" interpretation is inconsistent with the "new" or "novel" interpretation.
[227] *SEC Proposed Rules*, *supra* note 45, at 105. *But see id.* at 109 (stating that "many of the key elements of the whistleblower program have been established by the statute").
[228] Koch *supra* note 189 at § 4.33.

strategy based upon their independent judgment. If the SEC elects to pursue an independent enforcement strategy by simply ignoring whistleblower tips, they are subject to criticism though Dodd-Frank's mandated Inspector General Report.[229] Moving forward, SEC rulemaking can address Dodd-Frank's likely costs, even if only applied piecemeal with some of the stated recommendations.

C. *Legislative Action*

Although it is unlikely that Dodd-Frank will be amended in the current political environment, legislative action could significantly curtail Dodd-Frank's costs in a different environment. Specifically, prospective legislative changes include: (1) requiring that whistleblowers report fraud internally before reporting to the government; (2) adopting dollar value caps on whistleblower bounties; and (3) attorneys' fee-shifting to whistleblowers making frivolous claims.

1. *Require Internal Reporting*

To counteract the new bounty program's undesirable incentive for whistleblowers to forgo internal reporting, noted above, Congress may adopt a provision requiring that whistleblowers report internally before reporting to the SEC or CFTC.[230] Elsewhere in the securities laws, it is required that illegal activity be reported internally before reporting to the SEC. For example, Section 10A of the Exchange Act requires that auditors report fraud to company management before reporting to the board of directors, which must inform the SEC.[231] In addition, shareholder derivative rights of action echo similar policy rationale by generally requiring either a demand on the board of directors or a determination by a special litigation committee before properly proceeding to court.[232] Likewise, Dodd-Frank should have required whistleblowers to report internally before going to the SEC.

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[229] Pub.L. No. 111-203, § 922(d), 124 Stat. 1376 (2010).
[230] Carton, *supra* note 122.
[231] Section 10A of the Securities Exchange Act of 1934, 15 U.S.C. § 78j-1(b).
[232] *Grimes v. Donald*, 673 A.2d 1207 (Del.Sup.Ct. 1996) (stating that "[a] stockholder filing a derivative suit must allege either that the board rejected his pre-suit demand that the board assert the corporation's claim or allege with particularity why the stockholder was justified in not having made the effort to obtain board action."). *See also id.* (citing *Aaronson v. Lewis*, 473 A.2d 805, 812 (1984) (stating that "[t]he demand requirement is a recognition of the fundamental precept that directors manage the business and affairs of the corporation.")).

As a corollary, corporations should be permitted to require internal reporting and bring counterclaims against whistleblowers violating such policies.[233] An important tool for corporations to prevent fraud is ethics codes requiring employees to serve a gatekeeping function and report bad conduct.[234] Arguably, complicity to fraud is just as culpable as committing fraud itself.[235] As such, it could be unnecessarily difficult for corporations to enforce internal compliance systems if they cannot require ethical conduct from employees.[236] To effectively endorse internal policies, counterclaims should be permitted against whistleblowers who report externally in violation of internal policies requiring internal reporting.

Furthermore, if internal reporting were required, high whistleblowers awards may have the adverse effect of discouraging potential whistleblowers who would otherwise report fraud.[237] Such is the case because by allowing fraud to persist, the size of the fraud will likely increase, and with it, the size of the SEC penalty and whistleblower award.[238] To combat this disincentive, whistleblower awards should be based upon the size of the fraud when the whistleblower initially became aware of the fraud.[239]

While the SEC's proposed rules address the external reporting issue, they fall short of *requiring* internal reporting.[240] The proposed rules attempt to *encourage* internal reporting by providing a mechanism whereby a whistleblower may still be eligible for a bounty after internal reporting[241] and identifying internal reporting as a factor that will lead to a higher bounty.[242] However, these incentives are not attractive to some whistleblowers who: may not want to prolong the potentially emotional whistleblowing process;[243] may be skeptical of corporate interests to detect fraud;[244] and may not be

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[233] Kovacic, *supra* note 16, at 1843-44.
[234] *Id.* at 1844.
[235] *Id.*
[236] *Id.*
[237] *Id.* at 1845-46.
[238] *Id.*
[239] *Id.*
[240] *SEC Proposed Rules*, *supra* note 45, at 24-28.
[241] *Id.* at 112.
[242] *Id.* at 51.
[243] Cavico, *supra* note 101, at 545.
[244] Whistleblowers may decide not report internally due to the potential conflict of interest between corporate interests and whistleblower interests to detect fraud or collect a whistleblower award.

aware of internal reporting incentives any more than they are aware of the securities laws under which they may report hunches about fraud.[245]

Curiously, the proposed rules also grant the SEC discretion to allow corporate compliance even after a whistleblower makes a tip,[246] which is inconsistent with Dodd-Frank's policy to provide certainty to whistleblowers.[247] Under the rule, reporting would be anything but certain and even deceive whistleblowers making the emotional decision to report fraud.[248] If a whistleblower reports fraud and the SEC subsequently allows a business to remedy a securities violation with little penalty, the whistleblower may not receive the bounty that incentivized reporting in the first place. Moreover, the main justification offered by the SEC for the administrative discretion is not a policy justification, but rather one based upon past practices.[249] As presented, the proposed rule is an impractical attempt to tow the line between business and whistleblower interests. An internal reporting *requirement* to properly provide whistleblowers with certainty is appropriate, whether enacted by rule[250] or Congressional directive.

2. *Dollar Value Bounty Caps/Floors and Non-Pooled Bounties*

Dodd-Frank encompasses policy objectives to provide certainty to whistleblowers seeking bounties and presumably strives to do so in a cost-effective manner as well.[251] However, as noted above, the required 10-30% bounty may not provide certainty as intended or, even if doing so, may not be cost-effective.[252] To remedy these concerns, Congress may adopt provisions that guarantee bounties within a stated dollar range regardless of whether subsequent whistleblowers earn awards as well.

Addressing the marginal utility of large monetary whistleblower incentives, Senator Kyl proposed a $5-$20 million cap on whistleblower bounties on the Senate floor.[253] Sen. Kyl reasoned that bounties above a high dollar amount are not likely to incentivize additional reporting because bounties may be

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[245] *See supra* note 45, at 112.
[246] *SEC Proposed Rules*, *supra* note 45, at 34-35.
[247] *Id.* at 115.
[248] Cavico, *supra* note 101, at 545.
[249] *SEC Proposed Rules*, *supra* note 45, at 35.
[250] The SEC has indicated that it believes it has the ability to enact a rule requiring internal reporting. *See id.* at 34.
[251] S. REP. NO. 111-176, at 110 (2009).
[252] See discussion *supra* note Part III(B).
[253] Cong. Rec. S4517 (daily ed. Apr. 23, 2009).

virtually indistinguishable to most whistleblowers.[254] In response to Sen. Kyl, Sen. Leahy noted legislative deference to discretionary judicial approval of whistleblower bounties to refute such a cap.[255] However, the judiciary does not have discretion to impose a cap below 10% of enforcement proceeds and any floor on whistleblower bounties necessarily limits administrative discretion.[256] Thus, the 10% floor may not be cost-effective if there is little marginal utility and Congress should adopt dollar value caps on whistleblower bounties.

Moreover, the required whistleblower bounty range will only provide whistleblowers with certainty if they know that the award will not be pooled and split among multiple whistleblowers, as Dodd-Frank allows.[257] An obvious criticism to this approach, voiced by the SEC proposed rules, is that bounties may be exorbitant and even exceed penalties collected if not pooled.[258] However, this result can be curtailed or avoided by adopting high reporting standards through rulemaking, as suggested above. Further, the certainty provided to whistleblowers may justify this counterintuitive result if only occurring in rare cases. In a similar vein, test cases pursued by the SEC have justified excessive costs in individual cases to benefit the overall enforcement strategy. Thus, Congress should provide certainty to whistleblowers by disallowing pooled awards.

3. *Fee-Shifting: Exposing Whistleblowers to Risk to Deter Frivolous Tips*

It may be appropriate to expose whistleblowers to risk to deter unreliable whistleblower tips.[259] Unreliable tips may be a result of employees reporting unreliable hunches about fraud, employees seeking statutory whistleblower protection, and employees retaliating against supervisors for perceived slights.[260]

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[254] *Id.* It should also be noted that whistleblowers may not be aware of whether their reporting will result in a successful enforcement action and thus do not have an accurate estimation of a potential award. *See e.g.* Wyatt, *supra* note 54.
[255] Cong. Rec. S4517 (daily ed. Apr. 23, 2009).
[256] *See id.*
[257] *See* Pub.L. No. 111-203, sec. 922, § 21F(b)(1), 124 Stat. 1376 (2010).
[258] *See SEC Proposed Rule*, *supra* note 45, at 48.
[259] Sandman, *supra* note 155. *See also* Kovacic, *supra* note 16, at 1850.
[260] Sandman, *supra* note 155. *See also e.g.* Kolz *supra* note 50.

Giving whistleblowers some "skin in the game"[261] to deter frivolous tips may ease the SEC's management burden while preserving the benefits of whistleblower incentives.

Currently, whistleblowers are exposed to little or no risk to disincentivize frivolous tips. Under the "American bounty hunter" system, plaintiff's are free to bring claims without exposure to the risk they will be responsible for the defendant's attorneys' fees if their action is unsuccessful.[262] In fact, the only penalty in Dodd-Frank for reporting intentionally unreliable tips is seemingly inconsequential ineligibility for whistleblower awards.[263]

One way to expose potential whistleblowers to risk and thereby deter frivolous reporting is to adopt the English fee-shifting system in which a litigation loser pays the winner's legal fees. Under the English system, whistleblowers may be reluctant to make frivolous claims because they face monetary penalties.[264] As a result, the SEC would reduce the burden of handling some frivolous tips.

Candidly, issues arise surrounding a risk-based system. First, whistleblowers concerned that their tips will be characterized as frivolous and result in liability may be reluctant to file valid claims. Second, whistleblowers are already exposed to significant risk due to the career-risk involved with reporting if there is no anonymous method of reporting.[265]

Nonetheless, Congress implemented fee-shifting provisions for *qui tam* actions brought under the False Claims Act.[266] Under the FCA, the defendant's legal fees are shifted to the whistleblower[267] if the suit was "clearly frivolous, clearly vexatious, or brought primarily for purposes of harassment."[268] Although the high standard has resulted in few defendants successfully shifting fees to whistleblowers,[269]

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[261] Sandman, *supra* note 155.
[262] Professor Dale Oesterle, J. Gilbert Reese Chair in Contract Law, The Ohio State University Moritz College of Law, Class Lecture in Law 607.01L: Business Associations (Feb. 22, 2010).
[263] Pub.L. No. 111-203, sec. 922(a), § 21F(i), 124 Stat. 1376 (2010).
[264] Sandman, *supra* note 155. *But see* Kovacic, *supra* note 16, at n. 185 (noting that there is debate over whether fee-shifting deters frivolous suits).
[265] Cavico, *supra* note 101, at 545 (stating that "practical, ethical and legal ramifications" make "blowing the whistle one of the most difficult decisions an employee will have to make").
[266] Kovacic, *supra* note 16 at 1850 (citing 31 U.S.C. § 3730(d)(4) (1994)).
[267] Persons reporting illegal activity are referred to as "relators" rather than "whistleblowers" under the False Claims Act. *See* Kovacic, *supra* note 16.
[268] *Id.* at 1850 (citing 31 U.S.C. § 3730(d)(4) (1994)).
[269] *Id.*

the presence of FCA fee-shifting may still deter frivolous claims and there appear to be few costs associated with the FCA fee-shifting rule.

In light of the issues noted above and the framework of the FCA fee-shifting rule, any whistleblower liability for frivolous claims should be limited to cases of clearly defined fraud under an objective standard. An objective and high standard will provide certainty and limit the risk of deterring reliable whistleblowers claims due to a fear of penalties. Unfortunately, this framework may deter only the most egregious situations of unreliable tips. Nonetheless, the above analysis demonstrates the potentially high benefits and low costs associated with this proposal. Thus, Congress should adopt the English system to deter unreliable tips and preserve SEC resources.

V. BUSINESS COMPLIANCE

Employees uncovering fraud must balance a duty to society with organizational loyalty.[270] Dodd-Frank is designed to tip the scales in favor of a duty to society by offering whistleblowers substantial and more certain awards for reliable tips.[271] However, in doing so, Dodd-Frank also encourages employees to promptly report fraud externally in a race to secure an award for providing the SEC with "original information."[272] As such, the essence of Dodd-Frank's whistleblower provisions complicates business compliance. Notwithstanding any efforts to influence administrative rulemaking through public comment[273] or legislative action through lobbying, corporations can promote compliance by taking steps: (1) to prevent fraud and encourage internal detection; (2) to avoid whistleblower retaliation once fraud

[270] MILTON SNOEYENBOS ET AL., BUSINESS ETHICS 388 (3d ed. 2001). *See also* ROBERTA ANN JOHNSON, WHISTLEBLOWING: WHEN IT WORKS AND WHY 26 (2003).
[271] S. REP. NO. 111-176, at 111 (2009). *See also* Pub.L. 111-203, sec. 922(a), § 21F(b)(1)(A), 124 Stat. 1376 (2010).
[272] Carton, *supra* note 122.
[273] Public comments on the SEC's proposed rules to implement the Dodd-Frank may be made by following instructions available at: http://sec.gov/cgi-bin/ruling-comments?ruling=s73310&rule_path=/comments/s7-33-10&file_num=S7-33-10&action=Show_Form&title=Proposed%20Rules%20for%20Implementing%20the%20Whistleblower%20Provisions%20of%20Section%2021F%20of%20the%20Securities%20Exchange%20Act%20of%201934.

has been detected; and (3) to comply with special circumstances that arise under the Foreign Corrupt Practices Act ("FCPA"). [274]

A. *Preventing Fraud and Encouraging Internal Detection*

Management systems may be put in place to encourage and manage internal fraud reporting in a way that limits potential liability. As an initial matter, policies should be in place to notify employees of wrongful behavior and procedures should be available to report corporate wrongdoing internally.[275] A critical component to a code of conduct is informing employees what behavior is considered wrongful and prohibiting retaliation against employees reporting fraud.[276] Prohibited wrongful conduct may include: "insider trading, environmental crimes, bribery/payment violations, intellectual property infractions, accounting improprieties, discrimination/harassment, and other offenses."[277] Further, employees should be permitted to report fraud to particular individuals who can report retaliation complaints.[278] A hotline may also be implemented for employees to anonymously and/or confidentially report fraud.[279]

Further, proper internal controls and communication systems can serve as "a corporate safety net" against fraud and render whistleblowing virtually unnecessary.[280] In fact, companies have been relatively successful in defending against SOX whistleblower retaliation claims.[281] As such, businesses should review their internal controls for fraud detection to encourage internal reporting, thereby preserving organizational reputation and limiting fraud prevention costs.[282]

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[274] This section is designed to be a general overview of steps to comply with internal control requirements and avoid whistleblower retaliation liability, which may be contingent on a particular jurisdiction's law. For a more in-depth discussion and analysis, see DELIKAT & PHILLIPS, *supra* note 125 and Dowling, *infra* note 276.
[275] DELIKAT & PHILLIPS, *supra* note 125.
[276] Donald C. Dowling, International HR Best Practice Tips: Conducting Internal Employee Investigation Outside the U.S., 19 INT'L HR J. 1, 2 (2010).
[277] *Id.*
[278] DELIKAT & PHILLIPS, *supra* note 125. Such individuals may include "designated managers, in-house counsel and/or human resources personnel." *Id.*
[279] Dowling, *supra* note 276.
[280] Marlene Winfield, *Whistleblowing as corporate safety net, in* GERALD VINTEN, WHISTLEBLOWING: SUBVERSION OR CORPORATE CITIZENSHIP 25 (1994).
[281] DELIKAT & PHILLIPS, *supra* note 125.
[282] FREDERICK ELLISTON ET AL., WHISTLEBLOWING 135 (1985) (stating that external fraud reporting can "embarrass the company by washing their dirty laundry in public). *See also* Thompson Hine LLP, *Competition, Antitrust &*

Employers should also maintain performance records about employees.[283] If an employee is disciplined or terminated after reporting wrongdoing, the employer may be able to successfully defend against employee retaliation claims.[284] By pointing to records of poor performance prior to fraud reporting, employers may cast doubt on a causal link between disciplinary measures and fraud reporting.[285]

Notably, training is also necessary to educate employees about wrongful conduct, reporting procedures, and investigation procedures.[286] As employees are often reluctant to report fraud because of the uncertainty regarding potential retaliation and condemnation by their peers,[287] Dodd-Frank is designed to provide some certainty to whistleblowers by putting a 10% floor on whistleblower awards.[288] In a similar vein, disclosing information about the investigation process, including procedures and confidentiality (discussed in Part B *supra*), may encourage employees to report fraud internally.[289]

B. *Avoiding Whistleblower Retaliation*

Procedures should be in place and management should be trained to prevent retaliation against employees reporting fraud.[290] Under Dodd-Frank, even employees reporting unauthenticated fraud are protected against retaliation and employers should avoid even the appearance of whistleblower retaliation.[291] Procedures should be designed to retain management rights such that a reporting employee is no better or worse off as a result of reporting.[292] Employers must therefore balance retaining management rights and avoiding whistleblower liability.

White-Collar Crime and Business Litigation Update: Dodd-Frank Expands Securities Whistleblower Incentives (Jul. 30, 2010), *available at* http://www.thompsonhine.com/publications/publication2134.html.
[283] DELIKAT & PHILLIPS, *supra* note 125.
[284] *Id.*
[285] *Id.*
[286] *Id.*
[287] Cavico, *supra* note 101.
[288] S. REP. NO. 111-176, at 111 (2009).
[289] Dowling, *supra* note 276.
[290] DELIKAT & PHILLIPS, *supra* note 125.
[291] *Id.*
[292] *Id.* § 10:2.

Once wrongdoing or fraud has been reported, it is critical to swiftly implement initial measures. Misconduct must be discontinued[293] and immediate discipline should be implemented if fraud or other misconduct is clear.[294] Regardless of disciplinary measures, the employee engaging in alleged fraud should be counseled about proper behavior.[295] Also, if the reporting employee so desires, s/he should be separated from working alongside the employee engaging in alleged misconduct.[296]

Furthermore, every effort must be made to confidentially communicate with all the parties involved, including the reporting employee, the employee engaging in alleged misconduct and any witnesses. Initially, involved employees should be notified of investigation procedures and assured that communication is confidential, where appropriate.[297] Management should check in periodically with the reporting employee during the investigation to ask about any retaliation concerns.[298] Other witnesses should be notified of the investigation and given *Upjohn* warnings, which explain that the attorney works for the employer and may have corresponding confidentiality obligations.[299]

Other safeguards include accumulating and maintaining records. To prepare for potential litigation, records about the alleged fraud and the involved employees should be accumulated.[300] Moreover, internal and external auditors should be consulted to ensure that financial statements are not inaccurate due to any hidden losses or inappropriate payments.[301] For example, and as addressed in the next section, inaccurate financial reporting may violate the FCPA.[302]

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[293] Dowling, *supra* note 276, at 6.
[294] *Id.* at 2.
[295] DELIKAT & PHILLIPS, *supra* note 125, at § 10:2.
[296] *Id.* Measures should be taken to ensure that the employee does not consider any change in working conditions to be retaliatory in nature. *Id.*
[297] *Id.* For each instance of reported fraud, it is important to appoint an investigation team, define the scope of the investigation (i.e. legal and factual issues to be investigated) and draft an investigation plan outline steps to be taken. *Id.* at 3.
[298] DELIKAT & PHILLIPS, *supra* note 125, at § 10:2. If the reporting employee has valid retaliation concerns, prompt remedial action should be taken. *Id.*
[299] Dowling, *supra* note 276, at 4 (citing *Upjohn v. U.S.*, 449 U.S. 383, 101 S. Ct. 677, 66 L. Ed. 2d 584 (1981)).
[300] *Id.*
[301] *Id.* at 5.
[302] *Id.*

C. *Complying with the Foreign Corrupt Practices Act*

Compliance with the FCPA is increasingly important in today's regulatory environment for two reasons. First, the SEC is expected to adopt an enforcement strategy which prioritizes FCPA enforcement.[303] Second, it is expected that Dodd-Frank will incentivize whistleblowers to provide many tips regarding violations of the FCPA, which will spur SEC enforcement.[304]

The FCPA prohibits bribery[305] and requires that issuers within the scope of the Securities Act maintain records, books, and accounts to a reasonable level of detail.[306] These requirements are designed to disclose illegal transactions and prevent the falsification of records.[307] FCPA tips may increase not only due to whistleblowers seeking lucrative awards, but also due to increased illegal activity as a result of companies driven to engage in illegal activity to remain competitive during the recent economic crisis.[308]

As such, businesses should implement internal controls to comply with the FCPA. Particularly important to the FCPA context are having policies in place specifically forbidding acts prohibited by the FCPA[309] and training employees about prohibited activity.[310] With respect to financial reporting, internal controls should be in place to ensure that transactions are authorized, monitored if deemed to be high risk, properly recorded, and in accordance with generally accepted accounting principles.[311] If there is any doubt regarding whether a particular activity complies with the FCPA, the Department of Justice will review the proposed conduct and provide an opinion on legality.

[303] Lowman, *supra* note 136, at 4.
[304] Harker et al, *supra* note 34. *See also* Carton, *supra* note 122. *See also* Reisinger, *supra* note 43.
[305] Philip H. Hilder, Hilder & Associates PC, *Foreign Corrupt Practices Act Compliance Issues: Leading Lawyers on Responding to Recent FCPA Enforcement Actions, Maintaining an Effective Compliance Program, and Navigating Risk in Emerging Markets*, 2010 WL 2828307, at 5 (Jul. 2010).
[306] 15 U.S.C. §§ 78dd-1, et seq. *See also* Hilder, *supra* note 305, at 6.
[307] Hilder, *supra* note 305, at 6.
[308] *Id.* at 5.
[309] Lowman, *supra* note 136, at 9 (noting that recent FCPA enforcement actions have resulted in senior management being liable for FCPA violations they did not know were illegal despite the presence of a corporate policy forbidding such conduct). *See also* Hilder, *supra* note 305, at 7. Such activity should clearly outline permissible corporate payments for gifts and entertainment. *Id.* at 8.
[310] Lowman, *supra* note 136, at 9. *See also* Hilder, *supra* note 305, at 7.
[311] Hilder, *supra* note 305, at 6.

Moreover, monitoring can be an effective tool to detect illegal activity and avoid or limit FCPA liability.[312] Specifically, internal audits involving a team of forensic auditors including outside counsel are another effective fraud detection strategy.[313] Risk assessment should be performed, especially regarding consultants, agents, distributors, and subcontractors working in countries with a history of corruption.[314] Further, due diligence should be performed before entering into international mergers, acquisitions or joint ventures.[315] Finally, if activity violating the FCPA is detected, companies should consider self-reporting violations to potentially curb liability.[316] Accordingly, businesses should implement practices to avoid or limit liability under Dodd-Frank's whistleblower provisions.

VI. CONCLUSION

Dodd-Frank, totaling 2319 pages, enacts sweeping changes to our financial regulatory system including provisions that provide whistleblowers with anti-retaliation protection and monetary incentives to report securities fraud.[317] Surprisingly, or perhaps unsurprisingly in light of the sheer length of Dodd-Frank, there is little indication in the legislative history of Dodd-Frank that Congress objectively considered whistleblower motives/incentives and the negative implications which may result.[318] Moving forward, negative implications should be addressed by agencies through management and rulemaking, by Congress through legislative amendment, and by businesses through internal policies and controls.[319]

Against this background, the Dodd-Frank whistleblower provisions demonstrate a risk inherent in long legislation encompassing broad substantive areas. Specifically, that broadly reaching legislation will result in less-than-thoughtful legislation and undesirable policy that is difficult to amend. To be sure, the Dodd-Frank whistleblower provisions will impose costs on businesses and agencies and benefit trial

[312] *Id.*
[313] Lowman, *supra* note 136, at 9-10.
[314] *Id.*
[315] *Id.* at 8. *See also* Hinchey, *supra* note 77.
[316] *Id.*
[317] See discussion *supra* Part II(B).
[318] *But see* S. REP. NO. 111-176, at 244 (2009).
[319] See discussion *supra* Part II and Part III.

lawyer interests.[320] What are less certain are the benefits to society—namely confidence in the U.S. capital markets.[321] Therefore, while only time will tell whether the Dodd-Frank whistleblower provisions fulfill their policy ends[322] through regulations and potential legislative amendment,[323] lawmakers should be cognizant of the risks inherent with long and broadly reaching legislation.

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[320] See discussion *supra* Part III(B).

[321] See discussion *supra* Part III(A). The SEC posits that whistleblower law costs are outweighed by the confidence they create in U.S. capital markets by deterring fraud, which consequently incentives investing. *SEC Proposed Rules*, supra note 45, at 120.

[322] *See e.g.* Harker et al., *supra* note 34, at 780 (stating that "the program could be a boon to law enforcement in connection with laws such as the Foreign Corrupt Practices Act").

[323] *Id.* at 779. It is expected that agencies will be heavily lobbied as they write rules and regulations to implement Dodd-Frank. Amanda Becker, *Financial overhaul has been signed, but lawyers' work on law is far from over*, THE WASHINGTON POST, Jul. 26, 2010, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2010/07/23/AR2010072304359.html. Ronald D. Oral, *Bank lobbyist expects 'mistakes' with new rules*, THE WALL STREET JOURNAL DIGITAL NETWORK: MARKETWATCH, *available at* http://www.marketwatch.com/story/bank-lobbyist-expects-mistakes-with-new-rules-2010-10-14 (Oct. 14, 2010) (stating that short time horizons to write the rules implementing Dodd-Frank may result in administrative rule-writing mistakes).