

# SEC whistleblower program seeing renewed support under Biden administration

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Whistleblowers have a longstanding and vital role to play in detecting securities fraud. Protections for whistleblowers weakened during the Trump administration, as did efforts to incentivize reporting fraud to the U.S. Securities and Exchange Commission (SEC). The Biden administration has brought hope for revitalized protections and incentives for whistleblowers through recently updated guidance from the SEC and proposed legislation pending before Congress.

## Role of the whistleblower

As corporate insiders, whistleblowers know where and at whom to look to expose well-hidden fraud and harmful business practices. Getting this inside perspective to regulators can kickstart entirely new investigations and drive existing investigations with new leads. For this reason, since July 2010, the SEC has maintained an Office of the Whistleblower, which “strongly encourages the public (including any whistleblowers)” to submit any tips or complaints of securities fraud.

In addition to enforcement actions, whistleblower tips have long provided invaluable behind-the-scenes information that has sparked private securities litigation. Over the past decade, multiple securities lawsuits have stemmed from whistleblower tips and complaints filed with the Whistleblower Office. These private actions provide an important source of recovery for defrauded investors and keep corporate America in check.

## Dodd-Frank Act of 2010

In 2010, in the aftermath of the Great Recession, the Obama-Biden administration signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank). Dodd-Frank’s stated objective was to promote the United States’ financial stability.

To that end, Dodd-Frank expanded the protections afforded to whistleblowers. In a provision titled “prohibition against retaliation,” Dodd-Frank guarantees that “[n]o employer may discharge, demote, suspend, threaten, harass, directly or indirectly, or in any other manner discriminate against, a whistleblower in the terms and conditions of employment” for having reported their employers’ securities law violations to the SEC.

Dodd-Frank further provides that, if an employer is found to have retaliated against a whistleblower, the whistleblower is entitled to reinstatement; two-times the back pay otherwise owed to them, with interest; and compensation for litigation costs and attorney fees.

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Dodd-Frank also contains provisions designed to incentivize whistleblowers to report corporate misconduct through a “whistleblower award program.” The Whistleblower Program’s stated objective is to “motivate people who know of securities law violations to tell the SEC.” Dodd-Frank statutorily requires the SEC to pay an award to whistleblowers who submit “original information” that leads to a successful enforcement action resulting in a sanction or recovery greater than \$1 million. Under Dodd-Frank, qualifying whistleblowers are entitled to no less than 10%, and up to 30%, of monetary sanctions resulting from an SEC or related action.

Many observers have heralded the Whistleblower Program as a success. Enforcement actions from tips provided to the Whistleblower Office have resulted in nearly \$5 billion in monetary sanctions. These tips have helped the SEC and other enforcement agencies stop multiple fraudulent schemes in their tracks. They have also helped return money where it belongs: to defrauded investors.

According to the SEC’s 2021 Annual Report to Congress, since the inception of the program, investors had received or were scheduled to receive more than \$1.3 billion. The SEC has also awarded over \$1.1 billion to 214 whistleblowers since the program started a decade ago.

## Trump-era rollbacks of whistleblower protections

During the Trump presidency, SEC support for whistleblowers stalled. Most notably, in 2018, Trump's appointed SEC Chair proposed three crucial amendments to the SEC's rules governing the Whistleblower Program. The amendments, which were adopted by a 3-2 vote among the SEC commissioners along party lines, reduced protections of whistleblowers and incentives to report fraud.

First, the SEC limited the reach of Dodd-Frank's anti-retaliation provisions to "written communications." As a result, whistleblowers who conveyed their information to the SEC orally — including through SEC interviews — no longer received the protections against retaliation so critical to the success of the Whistleblower Program.

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Second, the SEC amended its criteria for determining whistleblowers' awards to "clarify" that the SEC may consider the "dollar or percentage" of the reward. This marked a departure from past practice. Under Dodd-Frank, qualifying whistleblowers are guaranteed between 10% and 30% of monetary sanctions from an SEC or related action, and the SEC's prior rules did not list the dollar amount the whistleblower would ultimately receive as a consideration in determining the appropriate percentage to award.

Instead, the SEC considered a range of qualitative factors, including the information's significance and the whistleblower's culpability, and then set the percentage of the award between 10% and 30%, as required by Dodd-Frank. After the rule amendment, however, the SEC gave itself discretion to consider the amount of the award in terms of dollars.

Many experts have commented that, as a result of this change in approach, whistleblowers became less incentivized to come forward with new information during the Trump presidency because, if the SEC determined that the dollar amount was too great, they would not receive the outsized award previously provided to qualifying whistleblowers under Dodd-Frank.

Finally, the SEC further reduced the incentives for whistleblowers to report fraud by amending how it would interpret Dodd-Frank's definition of a "related action." Prior to the amendment, when the SEC or a whistleblower shared information with another agency, the SEC would pay an award to the whistleblower based on the sanctions associated with that related action, even if the other agency had its own whistleblower program.

As a result of the amendment, however, the SEC began providing awards only if (i) the SEC determined that its whistleblower program had the "more direct or relevant connection to the action"; and (ii) the whistleblower had not already received an award from another governmental entity. The SEC's interjection of this limitation on "related actions" made whistleblower awards less certain when another agency used the whistleblower's information.

## Biden administration ushers in restoration of Dodd-Frank incentives and protections

Now under the Biden-Harris administration, the SEC has made a concerted effort to restore Dodd-Frank's protections of whistleblowers and redouble efforts to incentivize the reporting of securities fraud. On July 30, 2021, three months after Biden's newly appointed SEC Chair, Gary Gensler, took office, Gensler issued a statement that he "believe[s] deeply in whistleblower programs" and has "asked staff to examine whether and how the program could be further strengthened to ensure that misconduct within the remit of the SEC is identified, addressed, and stopped."

Weeks later, Gensler published a "Statement in Connection with the SEC's Whistleblower Program," announcing his direction to the SEC staff to review and revise the Trump-era SEC's amendments to the whistleblower program rules. Gensler highlighted in his Statement how "[v]arious members of the whistleblower community," as well as two of his fellow SEC commissioners, "have expressed concern that two of these amendments could discourage whistleblowers from coming forward."

The Democrat-controlled House of Representatives has also recently focused its attention on whistleblowers, and the need to protect and incentivize them. In October 2021, Congressman Al Green, the Chair of the House Financial Services Committee Subcommittee on Oversight and Investigations, introduced the Whistleblower Protection Reform Act of 2021 (WPROA), which is before the House for a vote. Thus far, the WPROA has received considerable public support, including from 19 whistleblower advocacy groups. If adopted, the WPROA would strengthen protections and incentives for SEC whistleblowers under Dodd-Frank and permanently undo the Trump-era SEC's controversial rule amendments discussed above.

The WPROA would also make various other amendments to Dodd-Frank aimed at strengthening whistleblower incentives and protections. Among other things, the WPROA would broaden Dodd-Frank's anti-retaliation protections to individuals who report internally at their company instead of only those who blow the whistle directly to the SEC, as well as individuals who experience retaliation post-employment, including interference with future employment prospects. It would also provide whistleblowers an avenue to recover for emotional distress and harm to reputation caused by employer retaliation.

The WPROA's full adoption and implementation will improve and reinvigorate Dodd-Frank's Whistleblower Program. If adopted, it would help ensure that whistleblowers are properly motivated to come forward and protected when they do.

## More remains to be done

Over the past year, strides have been taken to move the SEC whistleblower program in the right direction. Much more, however, remains to be done. According to a report released by New York University Pollack Center for Law & Business and Cornerstone Research, SEC enforcement actions against public companies

plummeted to a seven-year low during this fiscal year, and not a single public company defendant admitted to guilt.

The SEC's whistleblower program is not enough: The SEC must take strong action when fraud is identified. Only time will tell whether the SEC's and Congress' stated focus on whistleblowers will improve SEC enforcement efforts going forward. For the sake of investors, let's hope they do.

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