$4.5M SEC Whistleblower Award Underscores Incentives to Report Internally

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On May 24, 2019, the SEC awarded $4.5M to a whistleblower whose disclosures to his employer and regulators about a kickback scheme in Brazil led to a $30M enforcement action. According to the SEC’s press release announcing the award, this is the first award in which the whistleblower got credit for information that a company provided to the SEC following an internal investigation prompted by a whistleblower’s internal disclosure.

The whistleblower, a former orthopedic surgeon, initially provided an anonymous tip about the kickback scheme to his employer Biomet, which spurred the company to investigate the tip. Biomet self-reported the whistleblower’s tip to regulators and shared the results of its investigation, which formed the basis for an enforcement action. Within 120 days of disclosing the kickback scheme to Biomet, the whistleblower also reported the violation to the SEC, thereby rendering him eligible for an award based on the information that Biomet disclosed to the SEC from its internal investigation.

A Wall Street Journal article reports that the award stems from a 2017 enforcement action in which Biomet agreed to pay approximately $30 million to resolve parallel SEC and Department of Justice investigations into repeat violations of the Foreign Corrupt Practices Act (FCPA). In 2012, Biomet entered into a deferred prosecution agreement (DPA) and paid $22 million in penalties due to its subsidiaries and agents bribing publicly-employed physicians in Argentina, Brazil, and China for nearly a decade to win business. The SEC and DOJ took enforcement action in 2017 because Biomet “continued to interact and improperly record transactions with a known prohibited distributor in Brazil” and paid bribes to Mexican customs officials to import and smuggle unregistered and mislabeled dental products.

SEC Whistleblower Program Incentivizes Internal Whistleblowing

This $4.5M whistleblower award underscores two ways in which the SEC whistleblower rules incentivize internal whistleblowing. First, Rule 21F-6(a)(4) authorizes an increase in the award percentage where the whistleblower reported the possible securities violations through internal whistleblower, legal or compliance procedures. Second, under Rule 21F-4(c)(3), a whistleblower can get credit for information disclosed by a company to the SEC where the information results from an internal investigation of the whistleblower’s disclosure to the company, as long as the whistleblower also discloses the information to the SEC within 120 days of providing it to the company.

Significantly, a whistleblower is eligible for an award when the employer-provided information led to a successful enforcement action even if the information that the whistleblower originally provided to the employer would not have satisfied the “led to” requirements in the rules. Therefore, reporting internally and initiating an effective internal investigation can increase the probability of receiving an award, especially where the employer is motivated to address the misconduct. In this matter, Biomet was operating under a DPA with a compliance monitor and was required to promptly address any FCPA violation. Accordingly, Biomet had a strong incentive to investigate and self-disclose the whistleblower’s tip about an ongoing FCPA violation.

But in certain circumstances, internal whistleblowing can be futile, such as where a whistleblower works at a company at which senior management initiated and profited from a fraudulent scheme or where there is a
substantial risk that the company will try to cover-up the violation (e.g., by destroying evidence or improperly influencing witnesses before the SEC has an opportunity to elicit testimony). Whistleblowers are also unlikely to report fraud internally at companies with weak compliance programs or with a known pattern of retaliating against whistleblowers. A recent survey by the Ethics and Compliance Initiative (ECI) suggests that retaliation against whistleblowers is likely a significant impediment to internal whistleblowing. In particular, the ECI survey found that in 2017, instances of perceived retaliation against employees doubled.

This $4.5M whistleblower award demonstrates how the SEC whistleblower program can complement, not undermine, corporate compliance programs. Here, the whistleblower’s tip enabled Biomet to promptly address an ongoing FCPA violation. By providing an early warning of the violation, the whistleblower helped Biomet stop the scheme and likely mitigated the potential penalty that would have resulted had the scheme persisted. But it is somewhat surprising that this is the first whistleblower award stemming from a company’s internal investigation of a whistleblower tip. It begs the question whether companies are taking adequate steps to investigate and remediate potential violations reported by whistleblowers.

Prior to making internal disclosures, whistleblowers should consider the rules that apply to their unique circumstances and evaluate potential remedies to combat retaliation. Due to the Supreme Court’s 2018 Digital Realty decision, internal disclosures are protected under the Dodd-Frank whistleblower protection provision only where the whistleblower also reports a potential violation to the SEC. Fortunately, the House Financial Services Committee recently approved on a bipartisan basis legislation clarifying that internal disclosures are protected under the Dodd-Frank Act (H.R. 2515). The House has not yet voted on this legislation. To learn more about remedies to combat retaliation against corporate whistleblowers, see our article Dodd-Frank Whistleblower Protection Post-Digital Realty.

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