

5 Tips for SEC Whistleblowers and Lessons Learned from SEC Whistleblower Awards



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Lessons Learned from SEC Whistleblower Award Determinations

The SEC Whistleblower Program has awarded more than \$150 million to 42 whistleblowers. The orders announcing the awards, while sparse, offer critical guidance on how to: (1) recover an award; and (2) maximize the award percentage. These five lessons are drawn from those orders and our experience representing SEC whistleblowers.

Tip #1: Establish a Material Violation

Many SEC whistleblower attorneys will incorrectly begin the analysis of a claim by determining a whistleblower's eligibility for an award. This puts the cart before the horse. The first step in any successful whistleblower claim is to determine whether you can establish a material violation of federal securities law. In other words, can you show the SEC that your tip concerns a violation that is serious enough to warrant the use of its limited resources?

Whistleblowers have filed more than 18,000 tips with the SEC in the past five years. In a perfect world, the SEC would be able to investigate all legitimate tips and stop even immaterial violations. However, the SEC has limited resources, so it can

pursue only the best tips. (See Tip #5 on how to get the SEC's attention with your tip.)

If you have a hunch about a violation but lack any proof, then it may be worth investigating further, rather than submitting an incomplete or speculative claim to the SEC. Tips generally fall to the wayside unless they provide "specific" and "credible" information about material violations. That said, most whistleblowers should submit their tips as soon as possible. (See Tip #3.)

Tip #2: Quickly Determine Eligibility Because It May Affect Award Percentage

The next step in any successful whistleblower claim is to determine eligibility. This step follows a finding of a material violation because, while most individuals cannot establish a material violation, almost everyone can become eligible for an award, if certain steps are taken. Lawyers, external auditors, and even individuals involved in the wrongdoing are among those who may be eligible for awards.

Analyzing an individual's eligibility is complex. The analysis differs depending on the individual's relation to the company and how the individual obtained the information. For example, auditors may report to the SEC and be eligible for an award if:

- they have a reasonable basis to believe the disclosure is necessary to prevent conduct that is likely to cause "substantial injury" to the financial interest or property of the entity or investors;
- they have a reasonable basis to believe the entity is engaging in "conduct that will impede an investigation of the misconduct"; or
- at least 120 days have passed either since they properly disclosed the information internally, or since they obtained the information under circumstances indicating that the entity's officers already knew of the information.

Auditors who obtained the information during their audit of an issuer, however, will be eligible for an award only if:

- they have a reasonable basis to believe the disclosure is necessary to prevent "a material violation of the securities laws" that is likely to cause "substantial injury" to the financial interest or property of the entity or investors;
- they have a reasonable basis to believe the entity is engaging in "conduct that will impede an investigation of the misconduct even if the submission does not contain an allegation of audit firm wrongdoing"; or
- they report the securities-law violation to a superior in their independent public-accounting firm, and the firm fails to promptly report the information to the SEC.

Eligibility depends on various factors. If whistleblowers are uncertain about their

eligibility, then they should consult with an experienced SEC whistleblower attorney. A skillful analysis may be the difference between a multimillion-dollar whistleblower award and no award at all. The analysis, moreover, may largely determine the size of an award.

Tip #3: Act Fast

It is never too early to think about maximizing your potential award. Whistleblowers may receive anywhere from 10% to 30% of the monetary sanctions collected in actions brought by the SEC and in related actions brought by other regulatory or law-enforcement authorities. And the timing of a whistleblower's tip is a significant factor that the SEC considers in determining whether, and how much, to award.

To be eligible for an award, a whistleblower must first submit "original information." Original information is any information that the SEC does not already have. Whistleblowers who wait to report information, therefore, risk that someone else will submit the same information to the SEC first. Keep in mind that even if the SEC has already opened an investigation, whistleblowers may still qualify for an award if their information "significantly contributes" to the success of an enforcement action.

Next, the whistleblower office may reduce the amount of an award if the whistleblower unreasonably delays reporting the violation to the SEC. About 20% of the awards issued through 2015 were reduced because of an unreasonable reporting delay. In making this determination, the whistleblower office considers whether:

- the whistleblower failed to take reasonable steps to report the violation or prevent it from occurring or continuing;
- the whistleblower was aware of the violation but reported to the SEC only after learning of an investigation into the misconduct; and
- there was a legitimate reason for the whistleblower to delay reporting the violation.

For example, on February 28, 2017, the SEC issued an order reducing an award to 20% of the monetary sanctions collected "because of both the Claimant's culpability in connection with the securities law violations at issue in the Covered Action and the Claimant's unreasonable delay in reporting the wrongdoing to the Commission."

Finally, to be eligible for an award, some whistleblowers must take certain actions (e.g., the 120-day exception for auditors in certain circumstances, see Tip #2) before reporting to the SEC. Whistleblowers should therefore understand and consider the specific eligibility requirements in determining when to report to the SEC.

Tip #4: Know the Rules *Before* Filing with the SEC

Besides avoiding "unreasonable delay," whistleblowers should be aware of other actions that influence the size of awards. Whistleblowers must learn the rules early on because, as mentioned, some actions must be taken prior to filing with the SEC.

For example, the whistleblower office may **reduce** the amount of an award if the whistleblower:

- participated in, or was culpable for, the reported securities-law violation; or
- interfered with the company's internal compliance and reporting systems.

On the other hand, the whistleblower office may **increase** the amount of an award based on:

- the tip's significance to the success of any proceeding brought against wrongdoers;
- the assistance that you and your legal representative provide in the SEC action or related action;
- the SEC's law-enforcement interest in deterring the specific violation; and
- whether, and the extent to which, you participated in your company's internal compliance and reporting systems.

Accordingly, whistleblowers have an incentive to report internally to their companies' compliance personnel before going to the SEC. If whistleblowers choose to report internally, then **they should also report the same information to the SEC within 120 days**. That way, in evaluating a potential award, the SEC will consider the date of the internal report, rather than the date that the whistleblower reported to the SEC. As the SEC puts it, the whistleblower office will "hold your place in line." This may determine, for example, whether a whistleblower submitted "original information."

Tip #5: Draft a Tip that Grabs the SEC's Attention

The SEC Whistleblower Office is relatively small, and thousands of tips are submitted annually. Whistleblowers and their attorneys should tailor their tips to quickly grab the SEC's attention. While we could write a book on this section alone, here are a few "rules" to keep in mind when drafting submissions:

1. Provide the SEC with a clear roadmap for a successful enforcement action. Do not submit a pile of documents and expect the whistleblower office to figure it out. Instead, walk the SEC, step by step, through specific and credible examples of the violation(s).
2. Demonstrate how the violation is "material." As mentioned, the SEC investigates only those violations that are serious enough to warrant the use of its limited resources. While demonstrating materiality, be sure to analyze the legal issues and tie them to the specific violations. This should include a discussion of potential challenges that the SEC may encounter and how the agency should address them.
3. If possible, provide the whistleblower office with documentation of the violation. The SEC is much more likely to act on a tip that is supported by

strong evidence. The SEC does not, however, want all types of evidence. For example, the SEC does not want information that may violate the company's attorney-client privilege (e.g., documents, including emails, that involve advice from inside or outside counsel).

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