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A law firm is running ads before movies such as "Wall Street: Money Never Sleeps" to remind potential financial services whistleblowers about the payouts possible for those expose wrongdoing.

## SEC tries to decide how to set the rewards of whistleblowing

### Banking reform law promises payouts, but who will qualify?

BY DAVID S. HILZENRATH

An unlikely ad has been getting screen time in Manhattan movie theaters that cater to a Wall Street crowd.

Referring to "the new Dodd/Frank banking reform law," it informs viewers that by exposing financial fraud they can earn substantial rewards — 10 to 30 percent of the money recovered by the Securities and Exchange Commission.

Sponsored by a New York lawyer, the ad encourages potential whistleblowers to visit his Web site, SECsnitch.com.

As the snitch pitch suggests, a new high-stakes drama is playing out at the SEC, driven by the lure of jackpot payouts and an effort to stamp out the kind of corporate cons — or alleged cons — that have propelled Enron, Bernard Madoff and Goldman Sachs to infamy.

Legislation enacted over the summer in response to the financial crisis requires the SEC to pay rewards for information that leads to enforcement sanctions of at least \$1 million.

But it falls to the SEC to translate the language of the Dodd-Frank Wall Street Reform and Consumer Protection Act into detailed regulations, and the rulemaking process is becoming a battle.

Corporations are pushing for restraints on what they fear could become an open season for bounty hunters. They have said the SEC should defer to corporations' internal programs for investigating employee tips.

"Instead of allowing companies to identify and fix problems, we are just creating a lottery," David Hirschmann, president of the U.S. Chamber of Commerce Center for Capital Markets Competitiveness, said in a recent news release.

Lawyers who specialize in representing whistleblowers say the SEC shouldn't count on companies to investigate themselves. If employees are forced to complain internally, it could be harder for them to remain anonymous, lawyers say.

"[I]t appears the companies are attempting to create so many obstacles for whistleblowers to overcome so as to render the historic statute useless for the very cases the SEC hopes to bring, involving what would be top management," Stuart D. Meissner, the lawyer and former prosecutor who is the sponsor of the movie theater ads, wrote in a letter to the SEC.

The first draft of the SEC plan, a 181-page opus, is getting two thumbs down from Stephen M. Kohn, executive director of the

National Whistleblowers Center. "My analysis is that 95 percent of all good claims will be denied under this rule," said Kohn, a Washington lawyer.

"We will not file claims under this rule," he added.

The thicket of conditions and procedural stumbling blocks would either intentionally disqualify many potentially valuable whistleblowers or cause them to inadvertently lose their chance, Kohn said.

In a letter to the SEC chairman, Kohn said the SEC proposal undercuts the Dodd-Frank law, adding: "As currently drafted, the Proposed Rules signal to Wall Street that the SEC is more sympathetic to companies that violate the law than [sic] to employees who risk their careers, reputations and jobs to report wrongdoing."

The government has long had an ambivalent relationship with whistleblowers. Some government officials want their help; others resent it. It may be human

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nature to react with anger or jealousy when whistleblowers who participated in wrongdoing profit from exposing it.

For their troubles, many whistleblowers end up being stigmatized or subjected to retaliation. But their information has stopped countless frauds — from defense contractors cheating the Pentagon to drugmakers ripping off Medicare and a major Swiss bank helping Americans hide money from the Internal Revenue Service.

Then there was Harry Markopolos, the analyst who for years tried unsuccessfully to get the SEC to see through Madoff's Ponzi scheme.

The SEC proposal says that, in some cases, after receiving a tip the agency will "describe the nature of the allegations" to the company "and give the company an opportunity to investigate the matter and report back."

In an interview, Meissner said that approach could make it easier for companies to unmask tipsters who want to remain anonymous. The SEC should conduct its own investigations, he said.

The SEC proposal also says whistleblowers could be required to sign confidentiality agree-

ments. That could leave the public in the dark and prevent whistleblowers from criticizing the agency if the SEC sits on the allegations, Kohn said.

Asked to explain the agreements, SEC spokesman John Nester said the confidentiality provision as drafted pertains only to information the SEC might share with the whistleblower.

Writing on behalf of unnamed corporate clients, the law firm Baker, Donelson, Bearman, Caldwell & Berkowitz urged the SEC to prohibit lawyers from charging contingency fees to represent whistleblowers in SEC claims.

Without such a rule, companies could be flooded with frivolous claims, the firm wrote.

Such a prohibition could preempt many tips by forcing whistleblowers to pay legal expenses out of pocket. The SEC has not proposed banning contingency fees, but it has asked for public comment on whether it should restrict fees.

Another law firm for corporations, Arent Fox, said the SEC should require employees of public companies to pursue complaints through the companies' internal channels first.

The SEC proposal does not go that far, but it asks for public comment on the idea. The draft of the regulations says the agency could consider whether employees complained internally when determining whether they qualify for more than the minimum reward.

One reason companies want whistleblowers to complain internally first is that they want a chance to turn themselves in to the government and qualify for leniency.

"The whistleblower provisions may pit the whistleblower vs. the company in a strange, yet competitive, high-stakes game of 'who has the fastest car' to Washington to disclose the conduct," wrote Mike Koehler, an assistant professor of business law at Butler University in Indianapolis.

The SEC proposal also declares that certain categories of potential tipsters are ineligible for the rewards, at least unless they give the company a reasonable chance to act on the information first.

Those include people who have a legal or contractual obligation to report wrongdoing and those in supervisory roles who are told about a potential violation in the expectation that they will do something about it.

The proposal says the agency is engaged in a balancing act.

"Although we have attempted to craft these rules to strike a balance that is consistent with the purposes of the statute," the SEC wrote, "these provisions may result in some foregone opportunities for effective enforcement action."

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