News & Publications

The Whistleblower Debates

1/17/2011 – by Joshua Horn

One of the most important aspects of Dodd-Frank is the addition of a whistleblower section to the Securities Exchange Act. The SEC rulemaking process for the proposed whistleblower rule has fomented significant comment. The proposed rule provides, among other things, for the SEC Whistleblower Office to administer the program, that no party engaged in wrongdoing shall be eligible to receive an award, and includes anti-retaliatory provisions.

The debate over the adoption of this rule has focused on a few areas. One set of commentators have advocated that employees of publicly traded companies be required to first report the purported wrongdoing to an internal committee before becoming eligible for an award. Others contend that this requirement would have a chilling effect on whistleblowers. In other words, an employee would be less inclined to report wrongdoing if he or she had to first report it to their employer. This debate has focused primarily on the use of internal corporate compliance programs where one side of the debate wants employees to report to the internal compliance group before becoming eligible for

an award and the other side of aisle believes that such a requirement would fundamentally undermine existing compliance programs that are focused on preventing wrongdoing altogether.

The other central debate over the whistleblower rule focuses on whether whistleblowers should be barred from hiring lawyers on a contingency fee basis where the attorney would receive a percentage of the award the whistleblower obtains. The supporters of such a restriction contend that the availability of contingency fee litigation would only result in a flood of frivolous lawsuits. Importantly, the SEC's proposed rule did not directly address this concern even though there is a belief that 90% of all whistleblower cases would be handled on a contingency fee basis. It should not be a surprise that many lawyers take issue with any such restriction, arguing that there is no authority to impose such a restriction on a lawyer's ability to contract with his/her client for the provision of legal services.

A similar debate rages over the SEC's report due on January 21 regarding the regulation of financial advisors and the imposition of the uniform fiduciary duty. Although most commentators are convinced that the SEC will recommend a uniform fiduciary duty standard for investment advisors and broker dealers, the concern that has percolated revolves around disclosure requirements for conflicts of interest. One set of debaters contend that disclosure/consent regimes effectively do away with the fiduciary duty standard altogether. Yet other commentators posit that this type of disclosure and consent is what the fiduciary duty standard contemplates.

In the end, these debates will not stop rules from being adopted. Instead, this debate will inevitably lead to more litigation with legal challenges to the scope and meaning of any rules and regulations.