Faith Anderson
Chair, Whistleblower Protections/Awards Working Group
North American Securities Administrators Association
750 First Street NE, Suite 1140
Washington, DC 20002
faith.anderson@dfi.wa.gov

Re: Model Whistleblower Award and Protection Act

Dear Chairs Egan and Anderson:

We welcome the opportunity to submit our comments regarding the Model Whistleblower Award and Protection Act (the "Model Act"). We are attorneys at Constantine Cannon LLP and Katz Marshall & Banks LLP who represent whistleblowers in retaliation cases and whistleblower reward matters. Collectively, our firms' attorneys have represented hundreds of whistleblowers, including under the reward and anti-retaliation provisions of the Dodd- Frank Act. Our understanding of what motivates whistleblowers and the significant risks and burdens they undertake when reporting wrongdoing informs our comments.

We commend your efforts to standardize and expand the protections available to whistleblowers who expose securities laws violations. As the SEC's whistleblower program demonstrates, when properly incentivized whistleblowers can play an indispensable role in exposing fraud, abuse, and misconduct in the securities industry. The Model Act has adopted many of the best practices of the SEC program, including an anti-retaliation cause of action, a prohibition on impeding communications with regulators, and a sensible award process.

However, the Model Act diverges from the SEC program in several ways that will undermine its

ineffective" until Congress mandated minimum rewards.[7] And at the state level, the Indiana and Utah discretionary award programs upon which the Model Act is partially based have seen little success, collectively producing only "a small number" of tips and just two awards over the past decade.[8]

Congress correctly diagnosed why these programs have failed: many individuals are unwilling to risk "career suicide" without assurance that they will receive some reward for doing so.[9] No question, laws protecting whistleblowers from retaliation, like the provisions included in the Model Act, help deter and punish retaliation against whistleblowers. But retaliation—whether through termination, marginalization, harassment, or blacklisting—remains very real.[10] We know this firsthand from our clients, and studies continually underscore the point. This retaliation has a substantial chilling effect on those who are inclined to "do the right thing" but justifiably fear losing their livelihood if they do so. While robust protections are critical, Congress also recognized that only the guarantee of a reward is sufficient to persuade these potential whistleblowers to come forward.

In addition, financial incentives allow whistleblowers to more easily partner with qualified counsel to represent them through the legal process. In the vast majority of cases, blowing the whistle means more than just submitting a tip. The whistleblower may also attend interviews with government agents, respond to requests for documents, provide ongoing consultation as the government investigates, and even testify in depositions or trials. Most whistleblowers cannot afford hourly legal representation for this process and instead rely on counsel being willing to represent them on a contingency basis. Without a mandatory reward, qualified counsel are very unlikely to offer such contingency arrangements. In addition, from the government's perspective, the involvement of counsel helps conserve scarce resources by weeding out frivolous complaints and by packaging those that are worthy with legal arguments and evidence that streamline the government's evaluation of the potential claim.

For these reasons, we strongly urge you to make clear that rewards under the Model Act are mandatory for all whistleblowers who meet the eligibility criteria set out in Section 3.

---

[7] Id.

[8] Request for Public Comments at 2.

[9] S. Rep. No. 111-176, at 111.

[10] For example, a survey published by the nonprofit Ethics Resource Center in 2014 reports that "[m]ore than one in five workers (21 percent) who reported misconduct said they suffered from retribution as a result." Press Release, Ethics Resource Center, Survey: Workplace Misconduct at Historic Low (Feb. 4, 2014) https://www.businesswire.com/news/home/20140204006180/en/Survey-Workplace-Misconduct-Historic.

B. Whistleblowers Should Be Rewarded, Not Penalized, When Their Information Leads to Restitution for Victims

The Model Act also diverges from Dodd-Frank in excluding "restitution" from the calculation of a whistleblower award. That divergence could lead to lack of clarity, excessive litigation, and an undermining of the incentives for whistleblowers to come forward.

Section 2(2) of the Model Act defines "Monetary Sanction" to include "disgorgement" but exclude "restitution." As an initial matter, that formulation is confusing. Disgorgement is often considered one type of restitution. For example, in a recent case involving the SEC's disgorgement authority, the Supreme Court noted "that disgorgement is a form of [r]estitution measured by the defendant's wrongful gain."[11]

Aside from unclear drafting, there are other problems. Assuming that the Model Act intends to preclude awards based on restitution (i.e., amounts ordered returned to investors), such a divergence from Dodd-Frank is unwise.

The Model Act does not pay whistleblower awards out of the money that would otherwise go to victims, but instead directs that awards "shall be paid from a fund established elsewhere under state law."[12] This structure is modeled after Dodd-Frank's creation of the Investor Protection Fund used to pay awards under federal law.[13] The decision to set up a separate fund is prudent. Awards paid to whistleblowers from the proceeds of a successful securities action would create competition between whistleblowers and victims, whi-2 (e)9 (o)6 (m)4-1

the recovery of $500,000 in disgorgement and a $500,000 fine. The whistleblower would be entitled to a reward of $100,000–$300,000. But if the securities regulator returned the $500,000 in disgorged funds to victims, arguably a better outcome, then the whistleblower would only receive $50,000–$150,000 for the same tip. That disparity is unjustified.

Indeed, it would appear not only arbitrary but unjust that a whistleblower whose information allows victims to be made whole should receive less than an identical whistleblower whose case does not.

For all these reasons Dodd-Frank does not create such distinctions, but awards whistleblowers 10–30% of monetary sanctions imposed in any "related action," whether criminal or civil.[15] The same is true of the similar whistleblower award regime applied to IRS whistleblowers.[16] Victims are fully compensated, and whistleblowers are fairly rewarded.

Whistleblower rewards are most effective when they are predictable and perceived to be fair. Eliminating the distinction betwsatistin t(cts)1 (wj 0.245 0 Ts (v)J 0.002 Tc 6lr0.245 0 T)Tj EM6(e)

WistleLBodylWs f -1 g the4. dste/TT2 (s f c 45 a)-12 (7)1 (l)-1 (o)/TT1 (s f 1 (w)3 (er)-1 (s ar0.533 (e)

WistleblWs f 1 (w)3 (er)-1 (s ar3 (i)-4(e)4 (Ad3 (1 (Tw 12.745 rt)5 (le)1y)h)C.a)1 (ct)-1[(f)5 (a)1Tc -0c

concealed. While the government is typically very protective of whistleblower identities, certain circumstances require their disclosure.[17] And of course, mistakes happen.

Typically, a whistleblower's hesitation to risk disclosure is grounded in a real fear of retaliation, often because they are in a uniquely vulnerable position professionally or personally. In some cases, they are reluctant to come forward because the nature of the wrongdoers they seek to expose causes them to legitimately fear for their own safety. Some, over time, will reveal their identity, particularly if the government has demonstrated an interest in pursuing their information. But having the ability to proceed anonymously at the outset has convinced many key whistleblowers to bring their information to light.

The Model Act can permit anonymous reporting without sacrificing any of its goals. Indeed, the SEC program's provisions on anonymous reporting strike the right balance, and we encourage NASAA to incorporate them.[18] SEC whistleblowers have the right to proceed anonymously if they comply with certain requirements.[19] Primarily, they must be represented by an attorney. That attorney takes on some of the verification function typically conducted by the regulator: they must certify to the Commission that they have reviewed the information in the tip and that it is true and correct. Additionally, the whistleblower must sign the tip under penalty of perjury; that copy is preserved by the attorney and must be provided to the Commission if it has concerns that the submission contains false information. Finally, should the whistleblower ultimately be eligible for an award, they must disclose their identity to the Commission and have it verified before they can receive any payment.

This structure encourages additional whistleblowers to come forward without sacrificing the integrity of the program. By requiring an attorney, the Dodd-Frank program sensibly preserves the gatekeeping function that might otherwise be lost with anonymous reporting. The attorney for an anonymous whistleblower puts their own reputation on the line, so they have a strong incentive to assure the tip is credible. Moreover, most attorneys who represent whistleblowers do so on a contingency basis, so their economic incentive to avoid squandering time on low-quality information promotes further vetting.

Most importantly, the regulator can still interact directly with the whistleblower. Under Dodd-Frank, with the attorney as a go-between, the SEC regularly interviews anonymous whistleblowers, testing their credibility and developing their information just as they would with an identified source. Although the logistics are minorly more complex, the results are just as

---

[17] See, e.g., 17 C.F.R. § 240.21F-7(a).

[18] The Dodd-Frank Act's only reference to anonymous reporting is to require representation by an attorney. See 15 U.S.C. † × X–6(d)(2)(A). The provision is given specific life in the implementing regulations at 17 C.F.R. §§ 240.21F-7(b), F-9(c).

[19] See 17 C.F.R. §§ 240.21F-7(b), F-9(c).

strong as without anonymity. Those small hurdles are a small price to pay for encouraging the most vulnerable whistleblowers still to come forward.

II. SUGGESTED IMPROVEMENTS TO THE RETALIATION PROVISIONS

While allowing anonymity provides some measure of protection for employee whistleblowers, that step alone is insufficient to protect employees fully and incentivize them to come forward. To further shift the cost-benefit calculus in favor of whistleblowing, strong anti-retaliation measures must also be provided. The two seminal laws enacted in the 21st Century to reform corporate responsibility – the Sarbanes-Oxley Act and the Dodd-Frank Act – work together to do just that. While neither law is perfect, working in tandem, they have provided an umbrella of protection for corporate whistleblowers.

The Model Act wisely mirrors the anti-retaliation protections in Dodd-Frank Act, but because it does not incorporate critical components of the Sarbanes-Oxley Act, it does not adequately protect corporate whistleblowers from retaliation. Three suggested improvements will make for a significantly stronger Act.

A. Internal Whistleblowing Should Be Protected

Most employees who encounter potential securities violations at work first report the misconduct internally. They do so for a variety of reasons, but most often because they hope the company will take immediate corrective action or because they have no choice unless they allow themselves to be implicated in the unlawful conduct otherwise. The Model Act should encourage such internal whistleblowing because it can be one of the most effective ways to quickly stop ongoing misconduct and in doing so protect investors from further harm. Internal reporting also frequently leads companies to self-report to regulators, which has the dual benefit of quickly stopping the misconduct that harms investors and alerting the regulators to the misconduct.

As the Model Act is currently drafted, there is no protection from retaliation for whistleblowers who report internally if the retaliation happens before they report to the state securities regulator. Like the Dodd-Frank Act, it only protects employees who externally report. On the federal level, however, the Dodd-Frank Act's limited retaliation protection is complemented by the Sarbanes-Oxley Act's protections for internal reporting.

The Model Act should mirror not just the Dodd-Frank Act, but the fuller body of federal corporate whistleblowing law, by protecting both internal and external whistleblowing. To do so, it needs to replace the term "whistleblower" in Section 9 with the term "individual," the

least "employee." It also needs to add language similar to the Sarbanes-Oxley Act that protects individuals who report potential securities violations internally.[20]

B. Broader Rights and Remedies Should Be Provided

In addition to this expanded coverage, to be in full alignment with federal corporate whistleblowing law, the Model Act should expand its protection of the rights and remedies of whistleblowers.

First, the available relief should be expanded to include emotional distress and reputational harm damages, which are remedies typically available in whistleblower statutes.[21] Providing these non-economic damages is critical in retaliation cases because some frequent, actionable forms of retaliation have no economic damages, such as industry blackballing, "outing" a whistleblower, and workplace harassment. Additionally, facing unlawful retaliation causes substantial emotional distress and reputational harm, which should be compensable. The Model Act should provi

It is also critical that the Model Act incorporate similar language to the Dodd-Frank Act that protects the other rights and causes of action available to whistleblowers. The Dodd-Frank Act states: "Nothing in this section shall be deemed to diminish the rights, privileges, or remedies of any whistleblower under any federal or state law, or under any collective bargaining

for state legislatures who wish to enact a compelling whistleblower program to bolster their securities enforcement. When the SEC and IRS enacted whistleblower regimes incorporating these provisions, they received an enormous boost to enforcement efforts. States that adopt similar measures should achieve similar results. We thank you for your time and consideration.

Sincerely,

Eric Havian
ehavian@constantinecannon.com

Michael Ronickher
mronickher@constantinecannon.com

Christopher McLamb
cmclamb@constantinecannon.com

CONSTANTINE CANNON LLP
150 California Street, Suite 1600
San Francisco, CA 94111
Tel: (415) 639-4001
Fax: (415) 639-4002

Alexis Ronickher
ronickher@kmblegal.com

KATZ, MARSHALL & BANKS, LLP