

The Dodd-Frank Act together with factors unique to China combine to create the perfect storm

Aug 25 2010 [Rebekah Poston](#)

The Dodd-Frank Wall Street Reform and Consumer Protection Act, signed by President Obama on July 21, 2010, has been predicted by many to increase commodities, securities and [Foreign Corrupt Practices Act](#) enforcement actions by paying bounties to persons who blow the whistle on these types of violations. According to the chairperson of the Securities and Exchange Commission, Mary Schapiro, the SEC intends to add 800 new permanent staff members to accommodate the SEC's expanded role in dealing with this new law.

The Association of Certified Fraud Examiners found in its 2008 report that over 54 per cent of all securities fraud cases that the SEC prosecuted were derived from tips. Considering that the US False Claims Act's whistle-blower provisions have resulted in more than \$24bn in recoveries from settlements and judgments since 1986, the success of the Dodd-Frank Act's whistle-blower incentives will no doubt prove equally formidable.



Whistle-blowers can be awarded a bounty of between 10 to 30 per cent of any monetary sanction more than \$1m in a judicial or administrative action brought by the SEC. The SEC will determine the award based on the significance of the "original" information, the level of cooperation provided and the ultimate success of the enforcement action brought by the SEC. Information is not considered "original" if it came from "an allegation made in a judicial or administrative hearing, out of a governmental report, hearing, audit, investigation, or from the news media". Original information must be derived from the whistle-blower's independent knowledge or analysis.

Section 922 of the Dodd-Frank Act authorises the SEC to share the information provided by a whistle-blower with certain federal, state and foreign enforcement authorities. Under certain circumstances, if these authorities' actions are based on the same information that the whistle-blower provided to the SEC, the whistle-blower may be entitled to a portion of any monetary sanctions that result from the actions brought by these other enforcement agencies. Whistle-blowers will be unable to collect a bounty if they were convicted of a criminal violation in relation to the investigation. Persons cannot qualify as whistle-blowers if the information they discover was uncovered through the performance of an audit of the target company. Employees of regulatory or governmental agencies are excluded from qualifying as whistle-blowers.

Whistle-blower protection includes not only whistle-blowers who are employees of publicly traded companies but also employees of subsidiaries and affiliates whose financial information is included in the consolidated statements of a publicly traded company. If an employer is also covered under the [Sarbanes Oxley Act of 2002](#), it may not discharge or in any manner retaliate against an employee who provided information, caused information to be provided, or assisted in an investigation by a federal regulatory or law enforcement agency. Whistle-blowers under SOX are also protected if they assisted in an investigation by a member or committee of Congress, or an internal investigation by the company relating to an alleged violation of mail, wire, bank or securities fraud, or violating SEC rules or regulations or federal laws relating to fraud against shareholders.

A person wrongfully discharged is entitled to reinstatement, twice the amount of back pay, litigation costs and reasonable attorneys' fees. The identity of a whistle-blower, including any information that if revealed could identify the whistle-blower, is prohibited. So ask yourself this: will whistle-blowers forego talking to their company's internal auditors or compliance personnel and instead let the violation grow larger so they can tell the SEC, to qualify for a large bounty? Will a company feel pressure to self-report even more quickly than it would otherwise do, to prevent a whistle-blower from getting to the SEC before it can? Does the statute protect employees located outside the US? Does the statute apply to companies outside the US? What defenses are available to the employer if a whistle-blower alleges retaliation?

Some lawyers expect the regulators to define who is a covered employee under the whistle-blower provisions of the Dodd-Frank Act. It is also believed that employees working outside the US will be protected, along with US citizens working for companies located outside the US, as well as US citizens working for foreign entities controlled by a US company.

The SEC and US Department of Justice focus their FCPA investigations on industries and companies, as well as individuals who work closely with foreign governments. The more involved a foreign government is in a US business venture, the more likely the US authorities are to find an FCPA violation. The greater chance there is for an FCPA violation, the more likely it is to find a whistle-blower

in the mix.

Conducting investigations in China

One of the challenges that often appears when conducting FCPA investigations in the People's Republic of China is the concern that the investigation may arouse anger in the PRC employees being interviewed. This anger may then drive the employee to act as a whistle-blower to the relevant PRC authorities, inciting an investigation from within the PRC. At this point, the Dodd-Frank Act may be the least of the company's troubles.

Just as there are strict provisions regarding retaliation against whistle-blowers in the Dodd-Frank Act, China has its own strict standards for disciplining employees who may be involved in the very acts about which they may wish to blow the whistle. Unless one's company manual and employment agreements are carefully drafted to state specific behavioural standards, it may be impossible for the company to sever an employee against whom there is a strong suspicion of wrongdoing, but no "smoking gun".

Too often a company's employment agreements permit termination for violations of laws, or serious company policy, but the investigation will not uncover sufficient evidence to show a violation of law has occurred involving that employee. The company manual may not specify the conduct involved is prohibited. Companies are then left taking less severe disciplinary measures and being forced to keep wrongdoers on the company's payroll. It is, therefore, very important to review one's manual and employment contracts to see if they are strong enough to protect the company if an FCPA investigation and discipline are required in the future.

This becomes a very treacherous sea to navigate when a whistle-blower becomes involved. Having a whistle-blower on the payroll, one against whom retaliation is prohibited or one who may be complicit in the alleged conduct but not yet convicted, presents the perfect storm. Companies will need to keep an eye on the horizon for the SEC regulations coming out which hopefully will further explain the whistle-blower provisions of the Dodd-Frank Act and its application to employees and US companies doing business abroad.

In the meantime, having an experienced captain and crew manning the corporate ship is a must. Companies need to have a plan of action in place to respond to whistle-blower allegations. Prompt investigations into their allegations must occur and be effectively managed. Interaction between the company's compliance, legal and human resources divisions will be imperative, particularly where multiple jurisdictions may be involved.

Companies must incorporate into their training policies and procedures instruction on how not to retaliate against company whistle-blowers. At the same time, companies must provide the safe, secure and confidential avenues to accommodate whistle-blower complaints and encourage such reporting. Companies need to have their employees feel the company's compliance and internal reporting controls are strong and effective, especially when one considers the significant financial incentives for reporting to the SEC or the Commodity Futures Trading Commission.



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