INVESTMENT COMPANY INSTITUTE

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December 17, 2010

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: Proposed Whistleblower Rules;
File No. S7-33-10

Dear Ms. Murphy:

The Investment Company Institute[1] appreciates the opportunity to comment on the rules recently proposed by the U.S. Securities and Exchange Commission to implement Section 21F of the Securities Exchange Act of 1934.[2] Pursuant to Section 21F, the Commission is charged with establishing a whistleblower reward program that will pay monetary awards to eligible whistleblowers who voluntarily provide the Commission with original information about a violation of the federal securities laws that leads to the successful enforcement of a covered judicial or administrative action or a related action.

The Institute has very serious concerns about the unintended consequences that are likely to result from the manner in which the Commission has designed its proposed whistleblower program. Our concerns are focused primarily on three aspects of the program that will have the greatest adverse impact on our members: the program's impact on internal compliance programs; the Commission's attempt to impose a new obligation on registrants to notify the Commission of *all* violations of law, irrespective of how immaterial or technical in nature; and deficiencies in the criteria for rewarding whistleblowers. In addition, we recommend that the Commission refine the definition of "original

[1] The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of $12.05 trillion and serve over 90 million shareholders.

[2] *See Proposed Rules for Implementing the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934*, SEC Release No. 34-63237 (November 3, 2010) (the "Release").

information" and clarify the limits on the prohibition against employers retaliating against whistleblowers. Our concerns are discussed in more detail below.

I. THE PROGRAM'S LIKELY ADVERSE IMPACT ON INTERNAL COMPLIANCE PROGRAMS

A. Fund Compliance Programs

Unlike other SEC registrants, federal law requires registered investment companies and investment advisers to have rigorous internal compliance programs. Following the effectiveness of Rule 38a-1 under the Investment Company Act of 1940 in February 2004, every mutual fund has been required by law to have a compliance program that meets specific conditions. As noted in the Commission's release adopting Rule 38a-1, the rule was proposed

> because it is critically important for funds and advisers to have strong systems of controls in place to prevent violations of the federal securities laws and to protect the interests of shareholders and clients. The proposed rules were designed to foster, among other things, improved compliance by clarifying the compliance obligations of fund management and to strengthen the hand of fund boards and compliance personnel when dealing with them.[3]

To ensure that funds have strong systems of control in place, the rule requires each mutual fund to designate a Chief Compliance Officer (CCO), to have the fund's CCO approved by the fund's board, and to have the fund's board adopt compliance policies and procedures that are reasonably designed to ensure the fund's compliance and that of the fund's adviser, principal underwriter, administrator, and transfer agent, with the federal securities laws. The fund's compliance policies and procedures must be reviewed annually for their adequacy and the effectiveness of their implementation. The fund's CCO must provide a written report to the board annually that, at a minimum, addresses the following: the operation of the policies and procedures of the fund and each investment adviser, principal underwriter, administrator, and transfer agent to the fund; any material changes made to those policies and procedures since the date of the last report; any material changes to the policies and procedures recommended as a result of the annual review conducted under the rule; and each material compliance matter that occurred since the date of the last report. In other words, each mutual fund is required by law to establish, maintain, and continually update a very rigorous compliance program, which is subject to regular inspections by the Commission's Office of Compliance Inspections and Examinations.

Crucial to the success of these compliance programs is the ability of the fund to discover and redress any violation of the federal securities laws. In addition to learning about and correcting any

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[3] *See Final Rule: Compliance Programs of Investment Companies and Investment Advisers,* SEC Release Nos. IA-2204, IC-26299 (Dec. 17, 2003).

such violation, a fund must document the violation in the written report submitted annually to the fund's board and that report must detail how the fund's policies and procedures have been revised to prevent a recurrence of such violations. Mutual funds and their advisers are unique in their obligations under this rule – indeed we know of no other federal registrant that is subject to similar, rigorous requirements.[4]

B. Disconnect Between the Release and the Rule Text

In light of these existing programs, we are concerned that the bounty that the Commission will offer under Section 21F will incentivize employees, particularly disgruntled employees, to report violations or suspected violations of the law to the SEC rather than to the appropriate personnel within the mutual fund's internal compliance system. This could result in whistleblowers subverting and undermining internal compliance systems in return for the SEC's bounty. To avoid this result, it is absolutely crucial that the SEC's whistleblower program be designed to respect and support existing compliance systems, and we are pleased that the Release expressly recognizes this.

As noted in the Release, the whistleblower program proposed by the Commission "is designed to facilitate the operation of effective internal compliance programs by not creating incentives for company personnel to seek a personal financial benefit by 'front running' internal investigations and similar processes that are important components of effective company compliance programs."[5] The Release also expresses the Commission's interest in implementing "Section 21F in a way that encourages strong company compliance programs."[6] We are also pleased that, at the open meeting where the Commission's proposed rules were considered, the Chairman and each Commissioner voting on the proposal reiterated their concerns with this aspect of the proposal.[7] While being sensitive to the concern of "front running internal investigations," the Release also expresses the Commission's concern with situations in which an employer does not have a robust compliance process or lacks either assurances of confidentiality for whistleblowers or established whistleblower procedures and

[4] While FINRA Rule 3130 requires all FINRA members to designate one or more chief compliance officers and have the member's Chief Executive Officer annually certify the adequacy of the members' compliance and supervisory processes, there requirements are not as rigorous as those imposed on mutual funds and their advisers under SEC Rule 38a-1.

[5] Release at pp. 25-26.

[6] Release at p. 35.

[7] *See, e.g., Chairman Mary L. Shapiro, Opening Statement at the SEC Open Meeting: Item 3 – Whistleblower Program* (Nov. 3, 2010): " . . . the proposed rule seeks to reduce the chance that employees unnecessarily bypass internal compliance programs that their own companies have established. This is an important issue as our goal is not to, in any way, reduce the effectiveness of a company's existing compliance, legal, audit and similar internal processes for investigating and responding to potential violations of the securities laws."

protections.[8] It also expresses concern with circumstances "where the company knows about material misconduct but has not taken appropriate steps to respond."[9]

Notwithstanding these expressed concerns and repeated statements throughout the Release about the Commission's respect for internal compliance programs and its interest in encouraging "strong compliance programs,"[10] there is nothing in the text of the proposed rules that gives deference to, or even mentions, internal compliance programs. While the importance of internal compliance programs appears in the Release's discussion of "original information," "independent knowledge," "independent analysis," and the criteria for determining the amount of the whistleblower's reward, the rule text itself is completely silent on the subject of internal compliance programs. One of the more obvious examples of the disconnect between the Release's discussion of these issues and the actual rule text occurs in connection with the criteria for determining the amount of a whistleblower's reward. According to the Release,

> The Commission will consider higher percentage awards for whistleblowers who first report violations through their compliance programs. Corporate compliance programs play a role in preventing and detecting securities violations that could harm investors. If these programs are not utilized or working, our system of securities regulation will be less effective. Accordingly, the Commission believes that encouraging whistleblowers to report securities violations to their corporate compliance programs is consistent with the Commission's investor protection mission.[11]

According to proposed Rule 240.21F-6, the Commission will take into consideration the following criteria in determining the amount of a whistleblower's award:

(a) The significance of the information provided by a whistleblower to the success of the Commission action or related action;

(b) The degree of assistance provided by the whistleblower and any legal representative of the whistleblower in the Commission action or related action;

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[8] Release at p. 34.

[9] Release at p. 26. As discussed later in this letter, however, the Commission's proposal is not limited to reporting instances of "material" misconduct. Instead, it applies to persons reporting *any* violation of the federal securities laws.

[10] *See, e.g.,* Release at pp. 4, 24, 25, 26, 34, 35, and 51.

[11] Release at p. 51.

(c) The programmatic interest of the Commission in deterring violations of the securities laws by making awards to whistleblowers who provide information that leads to the successful enforcement of such laws; and

(d) Whether the award otherwise enhances the Commission's ability to enforce the federal securities laws, protect investors, and encourage the submission of high quality information from whistleblowers.

Contrary to the statements in the Release, there is absolutely nothing in these criteria – or elsewhere in the proposed rules – that codifies the Commission considering "higher percentage awards for whistleblowers who first report violations through their compliance programs." The disconnect between the Release's discussion of these issues and the rule text is troubling and raises concerns with how the Commission's whistleblower program will be run.

C. Recommended Approach

To more closely align the rule text with the Commission's repeatedly expressed interest in encouraging the use of internal compliance programs, we recommend that the rule be revised to be consistent with the Release's discussion regarding the importance of internal compliance programs and concerns with whistleblowers "front running" such programs. In particular, we recommend that the rule require, except in limited circumstances, whistleblowers to report potential violations through the employer's internal compliance program in order to become eligible for an award. To accomplish this, we recommend two revisions to proposed Rule 21F-3, relating to payment of awards to whistleblowers. First, we recommend revising condition (a)(2) to read:

> (2) With original information <u>that, if applicable, was first reported in accordance with paragraph (e) of this section</u>

Second, we recommend adding a new paragraph (e) to read:

> <u>(e)(i) To facilitate the use of internal compliance programs, in order to be eligible for an award, a whistleblower must first report the whistleblower's original information to the entity that is either committing or impacted by the violation of the federal securities laws alleged by the whistleblower.[12] If the entity has not established a compliance</u>

[12] The provision requiring the reporting of the whistleblower's information to an entity "impacted" by the alleged violation of the federal securities laws is particularly important in the mutual fund context. This is because, as recognized by the Commission's mutual fund compliance programs rule, Rule 38a-1, conduct by a mutual fund's service provider could result in the mutual fund – and unbeknownst to that fund – being in violation of the federal securities laws. Those funds that do not currently do so are likely, once the proposed rules are adopted, to require their service providers both to have a whistleblower program that is compliant with Section 301 of the Sarbanes-Oxley Act and require the service provider to report to the fund or its CCO any violations of the securities laws by the service provider that may impact the fund's compliance with such laws.

notification or whistleblower system to report potential violations of the federal securities laws that would meet the standards, including the anonymity standards, of Section 301 of the Sarbanes-Oxley Act[13] and any rules of the Commission thereunder, without regard to whether such entity is subject to the Sarbanes-Oxley Act, the whistleblower may first report its original information to the Commission.

(e)(ii) In order to pay any award to a whistleblower who relies on paragraph (e)(i) of this rule, the Commission must determine that, at the time the original information was reported to the Commission, the whistleblower's employer had no internal reporting system available to the whistleblower that met the standards of Section 301 of the Sarbanes-Oxley Act.

We additionally recommend that proposed Rule 21F-4(b)(7) be revised to clarify that a whistleblower will not be eligible for an award on the basis of providing information to the Commission within that provision's specified 90-day timeframe if the whistleblower had a Section 301-compliant means to report the information, but did not do so . Also, the threshold questions on proposed Form WB-DEC concerning a whistleblower's eligibility for an award should be revised to inquire whether the whistleblower has reported its original information to any person prior to reporting it to the Commission. If the whistleblower indicates it is first reporting the information to the Commission, the Form should also inquire, under penalty of perjury, whether the original information could have first been reported internally through other channels that were compliant with Section 301 of the Sarbanes-Oxley Act.

In making these recommendations, we are mindful of situations in which internal compliance and whistleblower reporting systems are either ineffective or deficient or would fail to protect a whistleblower's anonymity. Our proposed solution would address these concerns by enabling the Commission to determine whether an entity's whistleblower program meets certain minimum criteria standards, consistent with Section 301 of the Sarbanes-Oxley Act. So, for example, if the whistleblower's employer either did not have a whistleblower system for reporting complaints or had a system that was not compliant with the requirements of Section 301 of the Sarbanes-Oxley Act, the whistleblower could bypass such internal compliance system and report directly to the Commission. The Commission, as part of its review of the whistleblower's allegations, could determine the sufficiency of the employer's internal compliance/whistleblower program to determine whether there was merit in the whistleblower bypassing it and first reporting its original information to the Commission. Where there was merit in the whistleblower bypassing the internal program, this

[13] Section 301 of the Sarbanes-Oxley Act requires the audit committee of a publicly listed company to establish a complaint notification (whistleblower) system to facilitate the receipt, retention, and treatment of complaints. Such system must be designed to maintain the anonymity of complaints made by company employees. In connection with its use under our recommended revisions to the SEC's whistleblower rules, the internal whistleblower system would need to accommodate all reports of violations of the Federal securities laws and not just those issues covered under Section 301 of Sarbanes-Oxley.

approach may render useful information to the Commission staff regarding deficiencies in the internal program, which may have implications beyond the violation alleged by the whistleblower.

This approach will also facilitate the pragmatic "filter" function of internal compliance programs. The very purpose of the Commission's whistleblower program is to provide "high quality information" regarding potential violations of law and valuable information with a "high likelihood of a substantial securities violation."[14] The Release acknowledges that whistleblowers "could be mistaken," that there "could be an overflow of noisy signals," and that "erroneous cases" should be "eliminated before reaching the Commission."[15] This filter function is dependent upon internal reporting because company personnel would likely be better informed about whether certain conduct constitutes a violation of the securities laws. Requiring a whistleblower to first report within an employer's Sarbanes-Oxley reporting program will assist the Commission in separating "the wheat from the chaff" and thereby enabling it to concentrate its time and resources on more material or substantive violations.

To further demonstrate its commitment to the rigorous internal compliance programs of registrants, we recommend that the Commission adopt, as an operating policy and procedure, that, except in extraordinary or exigent circumstances,[16] when the Commission receives a whistleblower's allegation of a violation of the securities laws, it will notify the registrant of the allegation (while preserving the whistleblower's anonymity) and provide it an opportunity to investigate the allegation and report back to the Commission on its findings. Such a policy would avoid the Commission having to utilize its resources to investigate each and every allegation of a potential violation of law and provide the registrant, which may be better suited to quickly investigating and analyzing its internal information, the opportunity to address any violation it finds and report back to the Commission regarding its findings and any corrective action taken.

II. THE PROGRAM'S ATTEMPT TO IMPOSE NEW REPORTING OBLIGATIONS ON REGISTRANTS

The Institute also has very serious concerns about another disconnect between the language of the Release and the wording of the proposed rule. Our concerns relate to the rule's presumption that entities subject to the rule have a duty to report to the Commission each and every violation of the federal securities laws, regardless of how minor or immaterial.[17] In particular, to determine whether a whistleblower has provided the Commission original information that is derived from the

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[14] Release at pp. 35, 109-110.

[15] Release at pp. 112-113.

[16] Examples of extraordinary or exigent circumstances might include when the fraudulent activity is systemic in the firm from management on down (such as with a ponzi scheme) or where delay may exacerbate any harm to investors.

[17] For example, the Commission has referred to the late filing of transaction reports under a registrant's code of ethics as an "immaterial violation." *See Personal Investment Activities of Investment Company Personnel,* SEC Release IC-23958, at n. 25 (Aug. 20, 1999). The Commission's current proposal does not distinguish material violations from immaterial ones.

whistleblower's independent knowledge or analysis, "the proposed rule [*i.e.,* Rule 21F-4(b)(4)] focuses on whether the entity [that is the subject of the information] proceeded in bad faith *or did not disclose the information to the Commission within a reasonable time.*"[18] [Emphasis added.]

A. The Rules' New Reporting Requirements

According to the Release, "this provision does not impose new reporting requirements in addition to those existing under the federal securities laws."[19] But it certainly implies that non-disclosure of the violation may make a whistleblower eligible for an award. This is inappropriate given the fact that the federal securities laws do not impose *any* duty on registrants to report to the Commission all violations of the federal securities laws.[20]

Under the Commission's proposed whistleblower program, unless a registrant voluntarily reports *all* such violations of law,[21] it runs the risk of enabling those employees who have "legal, compliance, audit, supervisory, or governance responsibilities" to be granted whistleblower status based on the employer's failure to voluntarily report to the SEC. It may be difficult for the employer that is the subject of the whistleblower's allegation to know, at the time it discovers a violation – regardless of how minor the violation – whether it might result in the Commission assessing a fine in excess of $1 million. Indeed, unlike FINRA, which publishes its Sanctions Guidelines and provides its members a list of minor violations,[22] the Commission provides no guidance that might alert registrants to the Commission's views regarding the severity of various violations or the fines and penalties that may be assessed. The only way for a registrant to avoid unintentionally – and to its own detriment – enabling a person to acquire whistleblower status would be for registrants to report *all* violations of the federal

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[18] Release at p. 26.

[19] Release at fn. 36.

[20] In light of the absence of a legal obligation to self-report violations of law, over the years the Commission has sought ways to incentivize self-reporting. *See, e.g., Speech by SEC Staff: 24th Annual Ray Garret Jr. Corporate and Securities Law Institute,* Stephen M. Cutler, Director, SEC Division of Enforcement (April 29, 2004), "As you would expect, the provision of extraordinary cooperation . . . including self-reporting a violation . . . can contribute significantly to a conclusion by the staff that a penalty recommendation should be more moderate in size or reduced to zero." *See, also,* Chapter 6, "Fostering Cooperation," *SEC Enforcement Manual,* SEC Division of Enforcement (Jan. 13, 2010.) Clearly, the Commission does not have the authority to impose self-reporting on all registrants.

[21] Pursuant to proposed Rule 21F-1, a whistleblower is a person who provides the Commission with "original information about violations of the federal securities laws." Presumably this includes all such violations. Though not included in the rules' text, according to the Release, the term "whistleblower" includes individuals who also report "a *potential* violation of the federal securities laws." [Emphasis added.] Release at p. 6.

[22] *See* FINRA Sanctions Guidelines and Schedule A thereto.

securities laws to the Commission, notwithstanding the Release's statements that the proposed rules "do not impose new reporting requirements" on registrants.

B. Unintended Consequences

Contrary to the Release's assertion that, in proposing the rules, the Commission has "attempted to maximize the submission of high-quality tips and to enhance the utility of the information reported to the Commission,"[23] the provisions of Rule 21F-4(b)(4) may have the exact opposite effect. By implicitly requiring all registrants to report all violations to the SEC to avoid conferring whistleblower status on employees, the Commission can expect to be overwhelmed with information regarding minor violations of law that in no way advance the Commission's interest in protecting the investing public from serious fraud or abuse.[24] Indeed, the more time the Commission staff must spend receiving, processing, and investigating information regarding such minor violations, the less time and resources it has available to discern, investigate, and redress serious misconduct. As a result, the investing public may be *worse* off as a result of the Commission's proposal.

C. Recommended Approach

We recommend that the Commission avoid this result and ensure that the proposed rules do not implicitly or explicitly impose any new reporting requirements by revising the language in Rule 21F-4(b)(4)(iv) and (v) to read in relevant part:

> . . . , unless the entity did not take corrective action ~~disclose the information to the Commission~~ within a reasonable time or proceeded in bad faith;

This revision would both avoid incenting registrants to report immaterial violations to the Commission and ensure that such non-disclosure would not confer whistleblower status on employees unless the registrant failed to take corrective action within a reasonable period or proceeded in bad faith.

III. DEFICIENCIES IN THE PROGRAM'S CRITERIA FOR REWARDING WHISTLEBLOWERS

Consistent with the concerns discussed above, we are concerned with the proposed criteria for determining the amount of award to be paid to a whistleblower. Noticeably lacking from Rule 21F-6 are any criteria relating to the whistleblower's duty to act reasonably and in good faith, the materiality of the information provided, the whistleblower's interest in profiting from selling information relating

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[23] Release at p. 5.

[24] The frivolity of information the Commission can expect to receive should not be underestimated. Our members have reported their whistleblower hotlines being used to complain about co-workers' grooming habits.

to the complaint, or the Commission's determination to provide no reward to the whistleblower. Each of these issues is briefly discussed below.

A. The Whistleblower's Duty to Act Reasonably and in Good Faith

It is not difficult to imagine situations in which disgruntled employees inappropriately utilize the Commission's whistleblower program. Accordingly, it seems appropriate for the Commission to be able to expressly consider, in determining the amount of an award, the *bona fides* of the whistleblower and whether the whistleblower, in reporting the information, acted reasonably and in good faith. To accomplish this, we recommend that proposed Rule 21F-6 be revised to add as an additional criteria for determining the amount of the award, the whistleblower's duty to act reasonably and in good faith in providing the information to the Commission. This would both provide the Commission greater flexibility to take into account the whistleblower's *bona fides* when determining the amount of an award and enable it to reduce the award of any whistleblower who was more interested in harming his or her employer than uncovering wrongdoing. This new criteria would enable the Commission to consider: the whistleblower's motives in providing the information; the level of cooperation provided by the whistleblower to its employer to correct the problem once the violation is discovered; whether the whistleblower was involved with or contributed to the alleged violations; and whether the whistleblower brought the alleged violation or misconduct to the attention of either the employer or the SEC, as applicable, within a reasonable amount of time after discovering it, among other factors. The adopting release should expound on these and other factors the Commission might consider in assessing whether a whistleblower acted reasonably and in good faith.

B. The Materiality of the Information Provided

As discussed above, the scope of the whistleblower program extends to *all* violations of the federal securities laws. This breadth may likely result in the Commission being inundated with "jaywalking" complaints – those that involve neither fraud nor abusive conduct nor perceptible harm to investors. Various subdivisions of 21F-6 seem to imply that the materiality of the information will be considered,[25] but there is no express affirmation of this as a standard.

To better enable the Commission both to discourage the filing of non-consequential information and expressly consider the relevance of the information provided by a whistleblower in determining the amount of an award, we recommend that the criteria in proposed Rule 21F-6(a) for determining the amount of an award be revised to add an express standard that goes to the materiality of the whistleblower's original information.

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[25] For example, the criteria in subdivisions (c) and (d) regarding furthering "the programmatic interest of the Commission in deterring violations of the securities laws" and "enhancing the Commission's ability to enforce the federal securities laws, protect investors, and encourage the submission of high quality information from whistleblowers."

C. Profiteering

There is a significant danger that the Commission's whistleblower program will be seen as a "get rich quick scheme" by disgruntled employees. Lawyers reportedly have launched web sites, begun aggressive advertising campaigns, and are cold calling financial services employees to attract whistleblowers on the promises of riches to come.[26] We do not believe the intent behind Congress enacting Section 21F or the Commission's rules implementing this provision was to create profiteers or the illusion of riches for reporting violations of the securities laws to the Commission. Instead, the law was designed to provide an incentive the Commission could use to obtain access to useful information concerning serious wrongdoing.

The proposed rules should be revised to make clear that their provisions are not a "get rich quick scheme" by prohibiting "double dipping" (permitting whistleblowers to be rewarded in a variety of forums based on the same violation the whistleblower reported to the Commission). To accomplish this, we recommend that the rules expressly prohibit any whistleblower who provides original information to the Commission and cooperates with the Commission in its investigation of the information from being paid by a third party to provide the information or similar information relating to a violation of the securities laws.[27] Second, the rules should prohibit any person from collecting an award as a whistleblower if the person is or becomes a plaintiff in any civil litigation that is based on any original information that had been provided to the Commission by the whistleblower. Together, these revisions should avoid whistleblowers attempting to get rich off of their original information, make them elect whether they plan to cooperate with the SEC or the private bar, and avoid any sort of double dipping in reaping rewards based on their original information.[28]

D. The Granting of No Award

Rule 21F-6 should expressly preserve to the Commission the authority to determine, based on an assessment of the listed criteria, that no award should be granted to the whistleblower. It is possible, based on a consideration of the totality of criteria listed in Rule 21F-6, the Commission determines that

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[26] *See, e.g., "Get Snitch Quick: 'Wall Street' stirs whistleblower outreach idea,"* NY Post Business Section (Nov. 20, 2010). *See also "First Comes the Whistleblower, Then Comes the Securities Class Action?,"* The Wall Street Journal (Nov. 18, 2010); *"The Wall Street snitch pitch,"* The Washington Post (Nov. 22, 2010). For an example of a web site, *see* www.SECsnitch.com (noting that "the new [whistleblower] statute will no doubt make many people rich").

[27] The one exception to this should be those whistleblowers who, consistent with the rules' provisions for anonymity, retain an attorney to provide the information to the Commission. Our recommendation above regarding adding the whistleblower's *bona fides* as a condition for determining the amount of an award would also enable the Commission, in making an award, to consider the whistleblower's motives.

[28] Similarly, the Commission should ensure that the rules' provisions addressing related actions do not enable a whistleblower to collect a bounty under multiple agencies' whistleblower programs based on the same original information.

no award should be granted, notwithstanding a whistleblower's objective eligibility.[29] To accommodate these situations, we recommend the Commission revise Rule 21F-6 to provide itself this flexibility.

IV. Additional Considerations

A. Original Information

We recommend that the definition of "original information" be revised to narrow its overly broad scope in two areas. The first area relates to information concerning a violation of law that has been corrected by the registrant. In instances where a violation, or potential violation, of law was corrected by the registrant, the rules should make clear that a whistleblower who informs the Commission of the violations should not be rewarded. We recommend that the definition of original information in Rule 21F-4(b) be revised to add a new subdivision expressly providing that, to be considered original information, the information must be "information relating to a violation that has not been addressed by the entity that is alleged to have violated the securities laws."

Our second concern with the definition of "original information" relates to its open-ended nature. In particular, the proposed rules do not specifically address "original information" involving either violations that occurred beyond the applicable statute of limitation or situations in which there is uncertainty regarding the applicable statute of limitations. To clarify this issue, we recommend revising the definition of "original information" in Rule 21F-4(b)(iv) as follows:

> (iv) Provided to the Commission for the first time <u>between</u> ~~after~~ July 21, 2010 (the date of enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act) <u>and the date on which the statute of limitations applicable to the potential violation would have expired. When the potential violation is not be subject to a particular statute of limitations, the statute of limitations in Section 21F(h)(B)(iii) of the Securities Exchange Act of 1934 shall be used as the applicable statute of limitations.</u>[30]

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[29] For example, if the whistleblower could have taken action to report, prevent, or mitigate the violation and failed to do so; if the whistleblower failed to cooperate with his or her employer's attempts to discover or redress the violation; and if the whistleblower put his or her own self-interest ahead of the interest of the employer or investors, the Commission may not want, from a programmatic perspective, to be seen as rewarding this type of behavior.

[30] In the event there is no specific statute of limitations relevant to the particular violation, there should still be a period beyond which the whistleblower's information should not be considered "original information." We recommend that this period be the period set forth in Section 21F(h)(B)(iii) of the Securities Exchange Act of 1934 – *i.e.,* not more than six years after the date of the violation or more than three years after the violation is discovered or should have been discovered.

B. Prohibition Against Retaliation

We recommend that the Commission's rules or adopting release clarify or discuss the limits on the prohibition in Section 21F(h)(1) of the Securities Exchange Act against employers retaliating against a whistleblower. The Commission's Release and proposed rules currently are largely silent on this subject.[31] Our members are concerned that some employees may be lulled into thinking that, so long as they obtain whistleblower status under the Commission's rules, they are immune from any adverse action on their employment (*e.g.,* demotion or firing) even when the conduct in question is unrelated to the reporting of information to the Commission. Under 21F(h)(1), this is clearly not the case. Instead, its protections are limited to instances in which an employer discharges, demotes, suspends, threatens, harasses, or otherwise discriminates directly or indirectly on a person's employment because of any lawful act done by the whistleblower in providing information to the Commission or cooperating with the Commission under its whistleblower rules.

To avoid employees being misled, we recommend that the Commission expressly affirm in its rules or adopting release that adverse action taken by an employer against an employee is not actionable under Section 21F(h)(1) if such adverse action is based on information or facts unrelated to the employee's cooperation with the Commission. Of concern to our members is that some employees will misread Section 21F(h)(1) and the Commission's rules thereunder and believe that, so long as they provide any original information under the Commission's whistleblower rules, the employee will thereupon have guaranteed employment. Employees should understand that the rules are not intended to protect them from firing, demotion, or other adverse action if the employer can demonstrate that such action is unrelated to the employee's status as a whistleblower. Also, if the whistleblower provided false information to the Commission as a whistleblower or committed perjury under the Commission's whistleblower program forms, an employer should not be prohibited from taking adverse action against the employee. Accordingly, the Commission should confirm in such instances that nothing in Section 21F(h)(1): (1) precludes an employer from firing, demoting, or taking other adverse action against a whistleblower so long as such action is not based on the employee's status as a whistleblower; or (2) requires the employer to retain a whistleblower as an employee if the person has poor performance or attitude or violates company policy, the law, or SEC rules, including its whistleblower rules.

C. Foreign Entities

The Commission's proposed rules are silent as to their impact on or accommodation of violations involving foreign affiliates of SEC registrants. We recommend that the Commission

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[31] It appears that the rules' only mention of Section 21F(h)(1) is in proposed Rule 21F-2, which provides that "for purposes of the anti-retaliation provision of [Section 21F(h)] the requirement that a whistleblower provide 'information to the Commission in accordance' with Section 21F is satisfied if an individual provides information to the Commission that relates to a potential violation of the securities laws." The Release merely repeats this provision without expounding on it. Release at p. 7.

expressly clarify that the information reported to the Commission under the rules only extends to matters within the SEC's jurisdiction. In addition, the Release should clarify that, to the extent the laws of the European Union or other foreign jurisdiction either prohibit providing information to regulators anonymously or require that it be provided anonymously, the Commission will respect and give deference to the laws of the jurisdiction to which the whistleblower is subject.

D. Non-Federal Government Employees as Whistleblowers

As discussed in the Release, Section 21F(c)(2) of the Securities Exchange Act prohibits certain persons from being eligible for a whistleblower award. These persons are members, officers, or employees of "an appropriate regulatory agency," the Department of Justice, a self-regulatory organization, the PCAOB, or a law enforcement agency. The Commission should expand and clarify this exclusion to cover other government employees. In particular, any information that a whistleblower obtains as a result of being an employee of a Federal, state, or foreign government entity that is charged by law with overseeing compliance with securities laws should not be considered "original information" for purposes of the SEC's whistleblower rules. So, for example, if a state or foreign securities regulator discovers a violation of the securities laws of the United States, such person cannot obtain whistleblower status by providing the information to the SEC.

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The Institute appreciates having the opportunity to provide these comments to the Commission on its proposed rules for implementing the whistleblower provisions of Section 21F of the Securities Exchange Act. If you have any questions concerning these comments, please contact the undersigned at (202) 326-5815 or Tamara Salmon at (202) 326-5825.

Sincerely,

/s/
Karrie McMillan
General Counsel