



Whistleblowing in the Corporate World Series: Part III

*Accountants as Whistleblowers:
Newly Empowered to Make Ethical Reporting Choices*

Presenters

www.SECwhistlebloweradvocate.com



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Presenters

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[Jordan A. Thomas](#) is a partner at Labaton Sucharow LLP and chairs its Whistleblower Representation Practice. Labaton Sucharow is one of the country's premier private securities litigation firms and the first law firm in the country to establish a practice exclusively focused on protecting and advocating for SEC whistleblowers. Prior to entering private practice, Jordan spent more than 15 years in federal law enforcement, as both a Trial Attorney at the Department of Justice and an Assistant Director in the Enforcement Division of the Securities and Exchange Commission. While at the SEC, Jordan played a leadership role in the development of its Whistleblower Program. He is also the Editor of SECwhistlebloweradvocate.com, a website dedicated to helping responsible organizations establish a culture of integrity and courageous whistleblowers to report possible securities violations—without personal or professional regrets.

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CORPORATE CHALLENGE

Recent Survey Findings I

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- KPMG, Integrity Survey, 2009
 - 74% of employees personally observed/had firsthand knowledge of wrongdoing during previous 12 months
 - 47% didn't believe they would be protected from retaliation if they reported misconduct
 - 61% didn't believe they would be satisfied with outcome if they reported misconduct
 - 60%, in the banking/finance industry, reported that the wrongdoing they observed could cause "a significant loss of public trust if discovered."
- Littler Mendelson, Whistleblower Survey, November 2011
 - 96% report concern about whistleblower claims
 - 73% reported this as an emerging risk area
 - 67% predicted that whistleblower claims increasing
 - 65% reported being "only moderately" prepared
- Ethics Resource Center, National Business Ethics Survey, January 2012
 - 45% witnessed misconduct at work
 - 42% reported that their employer had a weak ethical culture
 - 22% of employees who reported misconduct perceived retaliation

Recent Survey Findings II

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- Labaton Sucharow, US/UK Financial Industry Survey, July 2012
 - 39% believed competitors had engaged in illegal or unethical conduct
 - 26% had observed or had first-hand knowledge of misconduct in workplace
 - 94% would report wrongdoing given the protections and incentives of the SEC Whistleblower Program
 - 44% were aware of the SEC Whistleblower Program
- Labaton Sucharow, Ethics & Action Survey, September 2012
 - 54% had observed or had firsthand knowledge of misconduct in workplace
 - 84% had a positive perception of whistleblowers that report illegal or unethical conduct
 - 83% would report wrongdoing given the protections and incentives of the SEC Whistleblower Program
 - 28% were aware of the SEC Whistleblower Program

RESPONSIBILITIES

- As a learned and licensed profession, accounting primarily serves society as a whole, rather than the desires of a few.
 - AICPA Code of Professional Conduct
 - IMA (Institute of Management Accountants) Code of Conduct
 - State licensing boards echo these responsibilities.
 - Similar responsibilities for Tax Accountants and other accounting practice areas.
- Unique position to know about fraud and wrongdoing and have the technical competence to recognize, and the independent professional standing to report it.
- Especially true of CPAs, who are licensed by the state.

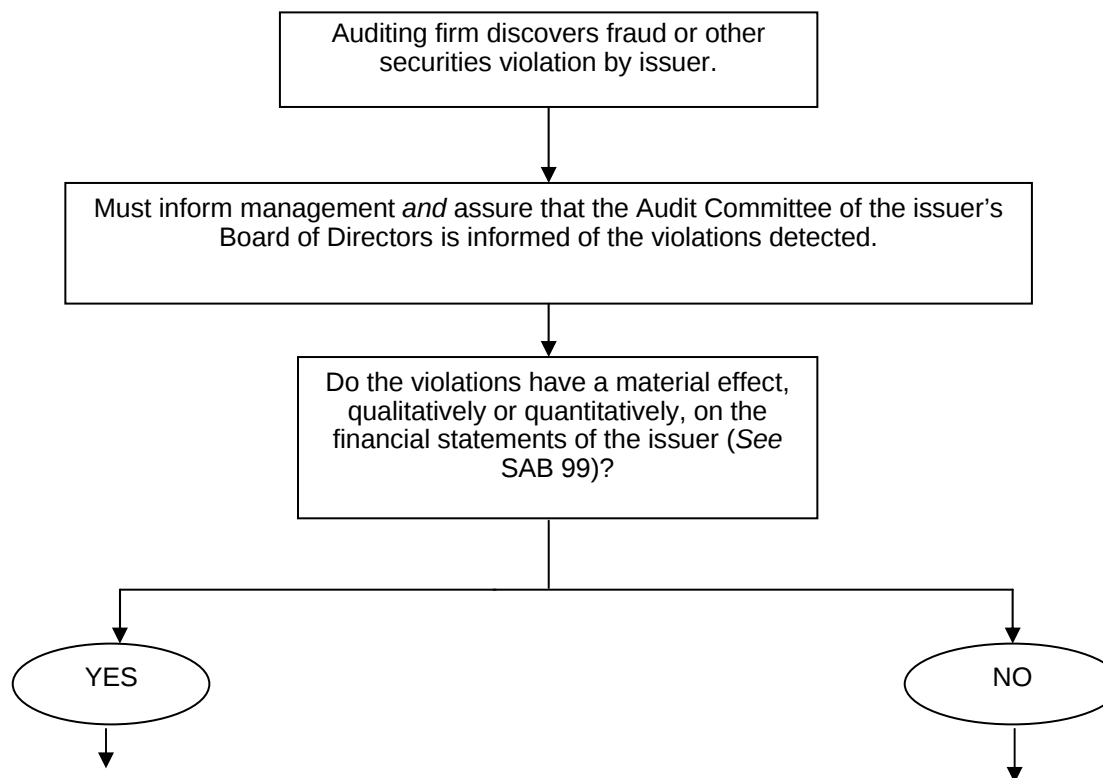
General Responsibilities

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- Auditors have always had a responsibility to report or require the client to report illegal acts that materially affect the client's financial statements.
- The PCAOB was created in response to a series of audit failures and is the de facto regulator for accounting firms' audits of public companies.
- Above all, auditors must act with integrity, "...guided by the precept that when members fulfill their responsibility to the public, clients and employers' interests are best served." (AICPA Code of Professional Conduct).
- Below are the specific guidelines for reporting when fraud is detected.

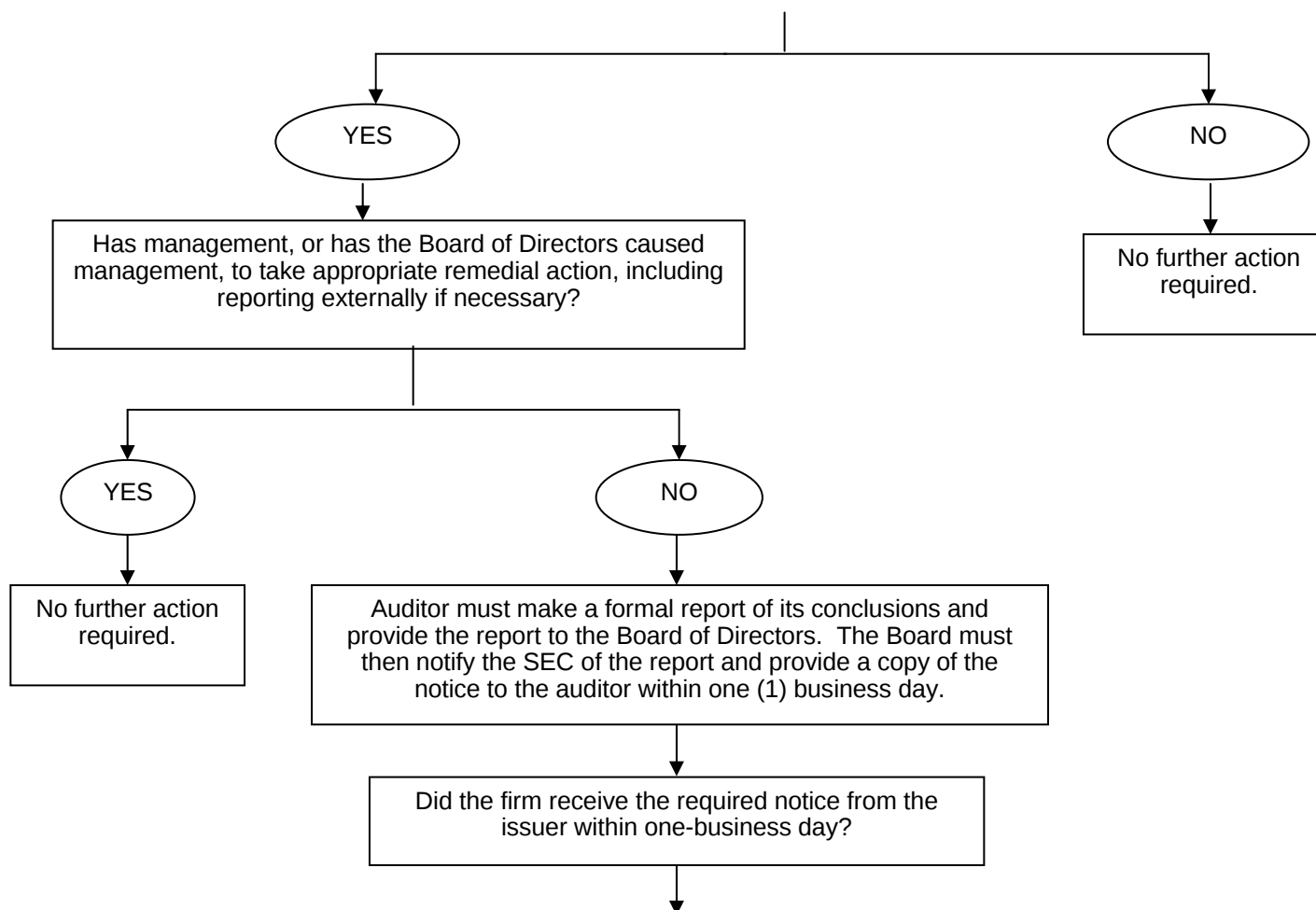
Reporting Fraud Under Section 10A of the Exchange Act

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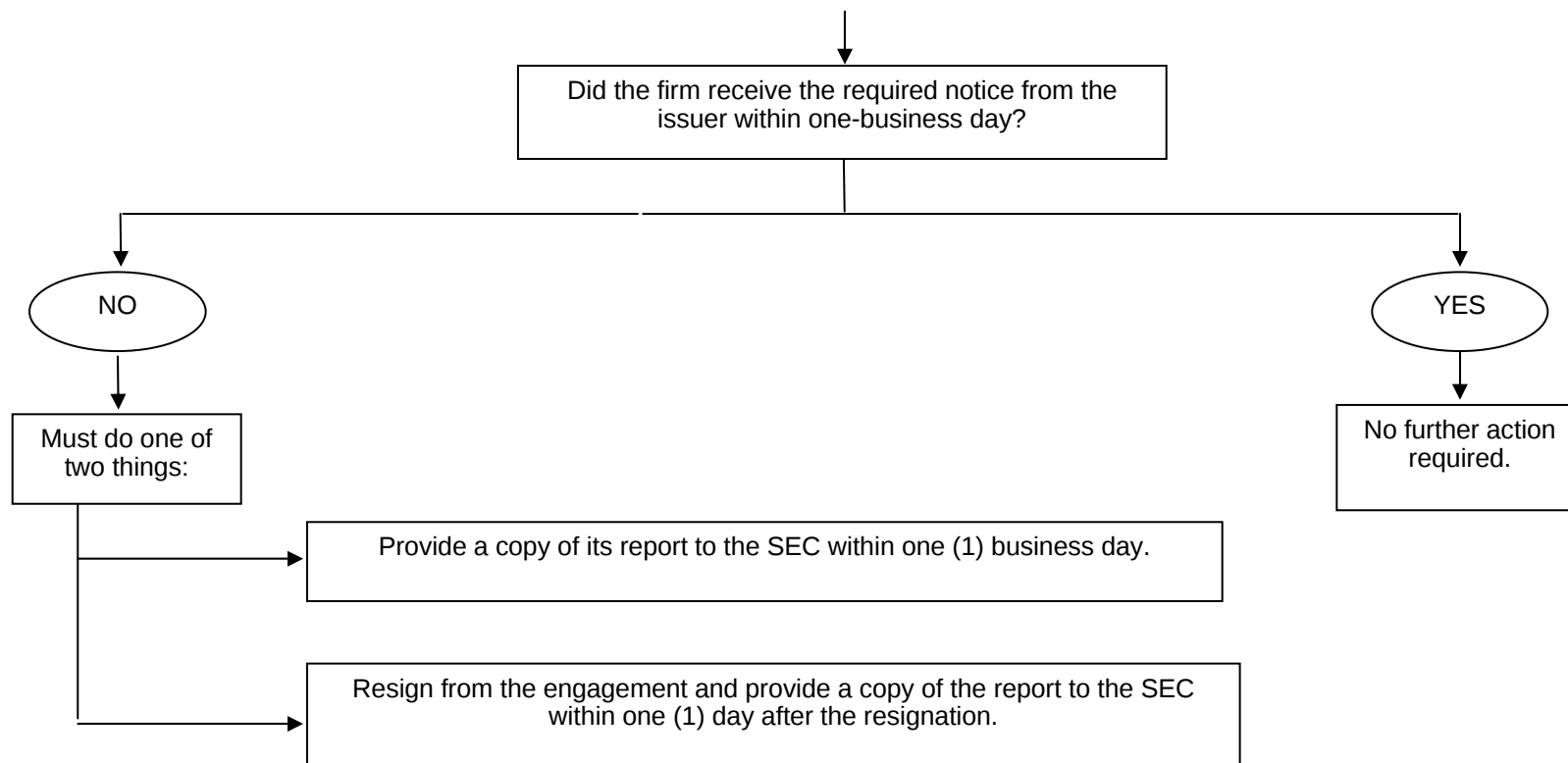
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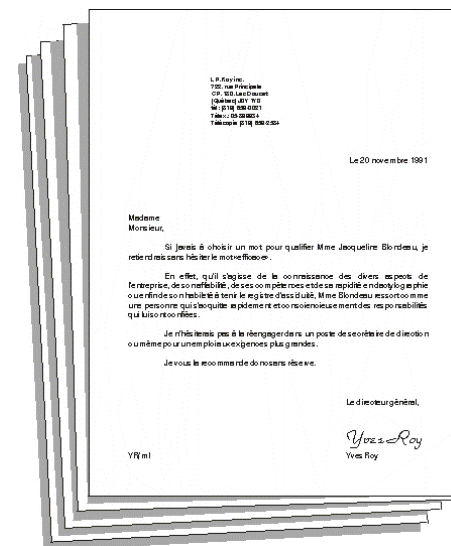


RIGHTS UNDER THE SEC WHISTLEBLOWER PROGRAM

Dodd-Frank Act

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- Dodd-Frank Wall Street Reform and Consumer Protection Act enacted July 2010
- Act required the SEC to establish a whistleblower program which offers:
 - Anonymous reporting
 - Robust employment protections
 - Significant monetary awards
- The implementing rules for the program became effective in August 2011



Anonymous Reporting— Overview

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- Confidential nature of SEC investigations
- Statutory representation requirement
- Practical reality

Employment Protections— Overview

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PROHIBITION AGAINST RETALIATION—

- (A) IN GENERAL—No employer may discharge, demote, suspend, threaten, harass, directly or indirectly, or in any other manner discriminate against, a whistleblower...because of any lawful act done by the whistleblower—
 - (i) In providing information to the Commission in accordance with this section...
 - (ii) In making disclosures that are required or protected under Sarbanes-Oxley Act of 2002..., and any other law, rule, or regulation subject to the jurisdiction of the Commission.

Employment Protections— Protected Conduct

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- Providing information about possible securities violations to the SEC
- Participating in any SEC investigation or related enforcement action
- Making disclosures to the SEC required by law

Employment Protections— Regulatory Requirements

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- Reasonable belief
- Compliance with SEC rules

Employment Protections— Avenues for Relief

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- Private right of action in federal district court
- No administrative exhaustion requirement
- Unwaivable right to a federal jury trial
- Reinstatement with equivalent seniority
- Two times back pay with interest
- Attorney's fees and related expenses

Employment Protections— Statute of Limitations

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- Six years after the date the retaliation occurred;
or
- Three years after discovering retaliation
- ...but in no event longer than 10 years after the
date of violation

Monetary Awards— Overview

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Subject to the eligibility requirements, the Commission will pay an award or awards, 10-30% of the monetary sanctions collected, to one or more whistleblowers who:

- Voluntarily provide the SEC
- With original information
- That leads to the successful enforcement by the Commission in a federal court or administrative action
- In which the SEC obtains monetary sanctions totaling more than \$1 million

The SEC will also pay an award based upon amounts collected in certain related actions.

Whistleblowers Ineligible for an Award

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- Individuals criminally convicted for related misconduct
- Members, officers and employees of the SEC and other enumerated organizations
- Family members and those that reside with an SEC member or employee
- Members, officers and employees of a foreign government
- Individuals that knowingly or willfully provide false information to the SEC

Whistleblowers with Qualified Eligibility for an Award

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- Attorneys
- Accountants
- Officers, directors, trustees, and partners
- Employees or contractors whose duties involve compliance or internal audits
- Individuals retained to conduct an internal investigation involving possible violations
- Individuals who obtain information about violations from an ineligible individual

Criteria for Determining Amount of Award

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- Factors that may increase an award include:
 - Significance of the information provided
 - Degree of assistance provided
 - Law enforcement interest in making the award
 - Participation in internal compliance systems
- Factors that may decrease an award include:
 - Culpability or involvement in the reported misconduct
 - Unreasonable reporting delay
 - Interference with internal compliance systems

COMMON QUESTIONS

What are the risks associated with reporting violations of the federal securities laws?

Being a whistleblower isn't always easy, glamorous or lucrative. Historically, reporting violations of the law has meant significant personal and professional risks for whistleblowers. Fortunately, things are changing for the better.

- Growing frustration with recent corporate scandals and bailouts
- Positive public sentiment
 - 84% of Americans have a positive perception of whistleblowers
 - More than 80% of Americans and financial service professionals would report misconduct if they had the protections and incentives offered by the SEC Whistleblower Program
- New legislative initiatives
 - Enhanced whistleblower protections and incentives
 - Channels for anonymous whistleblowing
 - Requirements for more rigorous internal reporting and compliance policies, procedures and practices

What are the most common types of securities law violations?

Common Securities Violations

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- Market Manipulation
- Offering Fraud
- Financial Fraud
- Insider Trading
- Trading and Pricing
- Foreign Corrupt Practices Act
- Municipal Securities Fraud

Market manipulation is the interference with the free and fair operation of the market by engaging in transactions and other practices that create or maintain an artificial price for a security. Examples include:

- Churning
 - Placing of both buy and sell orders for the same security at about the same price in order to create the appearance of increased trading activity, thereby increasing its price
- Pooling
 - An agreement among a group of people delegating authority to a single manager to trade in a specific stock, for a specific period of time, and then to share in the resulting profits or losses
- Pump and Dump
 - Spreading false information to increase the price of a security, then selling shares at the increased price

Offering fraud involves making material misrepresentations and/or omissions to potential investors in connection with an offering of securities. Examples include:

- **Unregistered Offering**
 - The securities being sold are not registered with the SEC as required under the Securities Act
- **Ponzi Scheme**
 - Investors are paid returns from their own money or from the money invested by subsequent investors, rather than from any actual profit earned
- **Affinity Fraud**
 - Targets members of an identifiable group, such as religious or ethnic communities, in order to induce those members to invest in a fraudulent investment opportunity

- Financial fraud occurs when a public company files materially false or misleading financial statements with the SEC. Examples include:
 - Misleading disclosures
 - Misclassifications
 - Improper recording of transactions
 - Overstatements
 - Understatements

Insider trading is the buying or selling of a corporate security while in possession of material information about that corporation that is not known to the public.

Two theories of insider trading:

- **Classical Theory**
 - Involves corporate insiders who have access to material, nonpublic information based on their positions inside a corporation
- **Misappropriation Theory**
 - Involves third parties who acquire material, nonpublic information about a corporation based on some relationship of trust with the source of the information

Trading and pricing violations involve any number of trading techniques that are illegal under the securities laws. Examples include:

- **Market Timing/Late Trading**
 - When a mutual fund permits select customers to purchase shares in the fund after trading has closed for the day
- **Wash Trades**
 - Involve the buying and selling the same security for the purpose of generating activity and increasing the price
- **Marking the Close**
 - Buying or selling a security near the close of the day's trading in order to affect the closing price
- **Front Running**
 - Buying or selling a security while knowing that another investor is about trade, or an analyst will make a recommendation, that will influence the price of the security

Foreign Corrupt Practices Act (FCPA)

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- The FCPA prohibits the offer, payment, or promise to pay money or anything of value—i.e., a bribe—to any foreign official in an effort to win or retain business from that foreign official's government.
- Affirmative Defenses:
 - The payments are legal under the written laws of the country in which the payments are made; or
 - The payment is a reasonable expenditure directly related to the conducting of business with a foreign government.

- Municipal securities fraud occurs when materially false or misleading statements are made to investors in connection with the purchase or sale of debt securities issued by state and local governments in the United States.

Who is eligible to be an SEC whistleblower?

Eligible SEC Whistleblowers

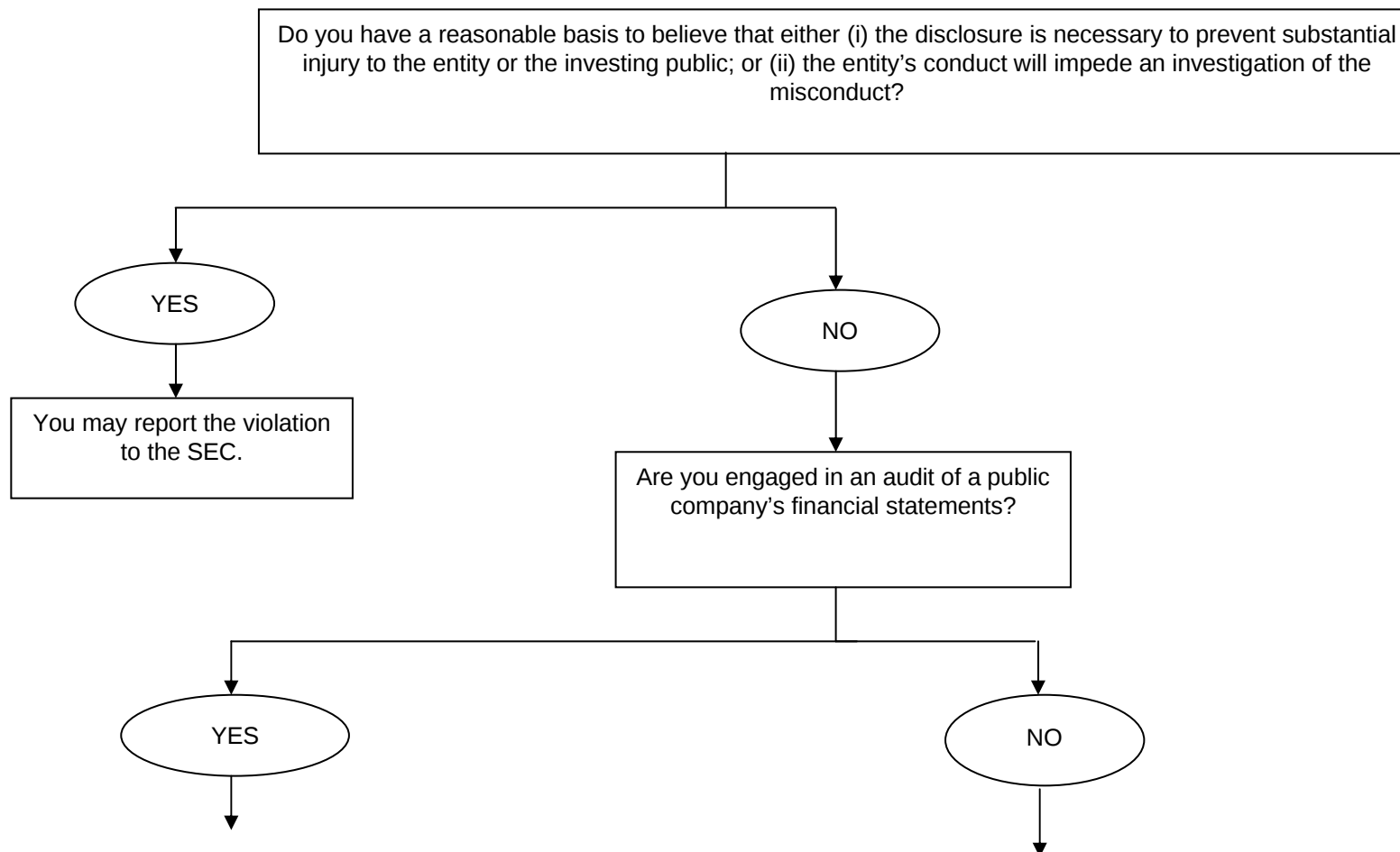
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- Any individual who, alone or jointly with others, provides information to the SEC relating to a possible violation of the securities laws that has occurred, is ongoing, or is about to occur.
- Only individuals, not companies, are eligible for the whistleblower protections and incentives in Dodd-Frank.

When is an accountant eligible for a monetary award under the SEC Whistleblower Program?

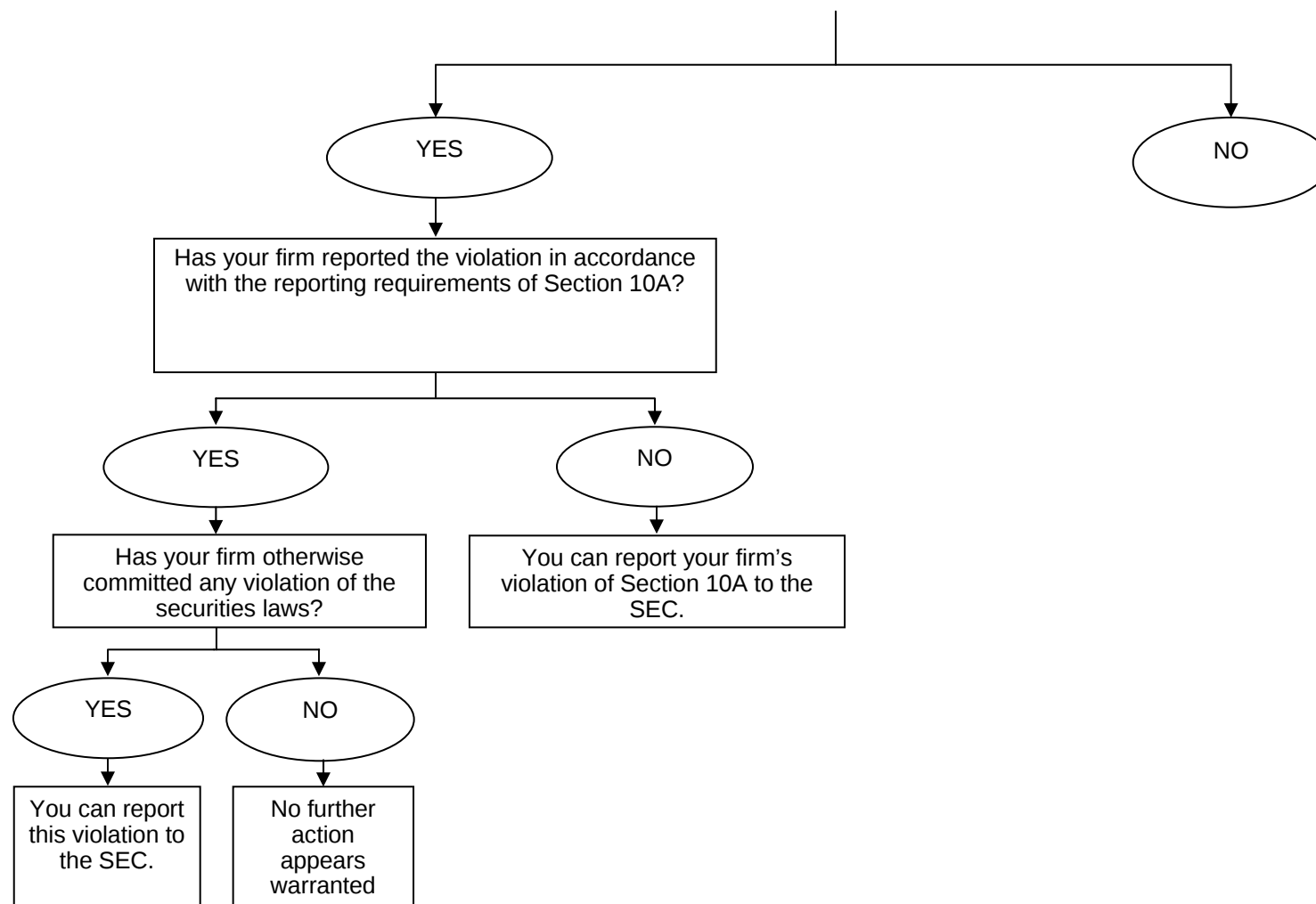
Accountants' Eligibility For Monetary Awards

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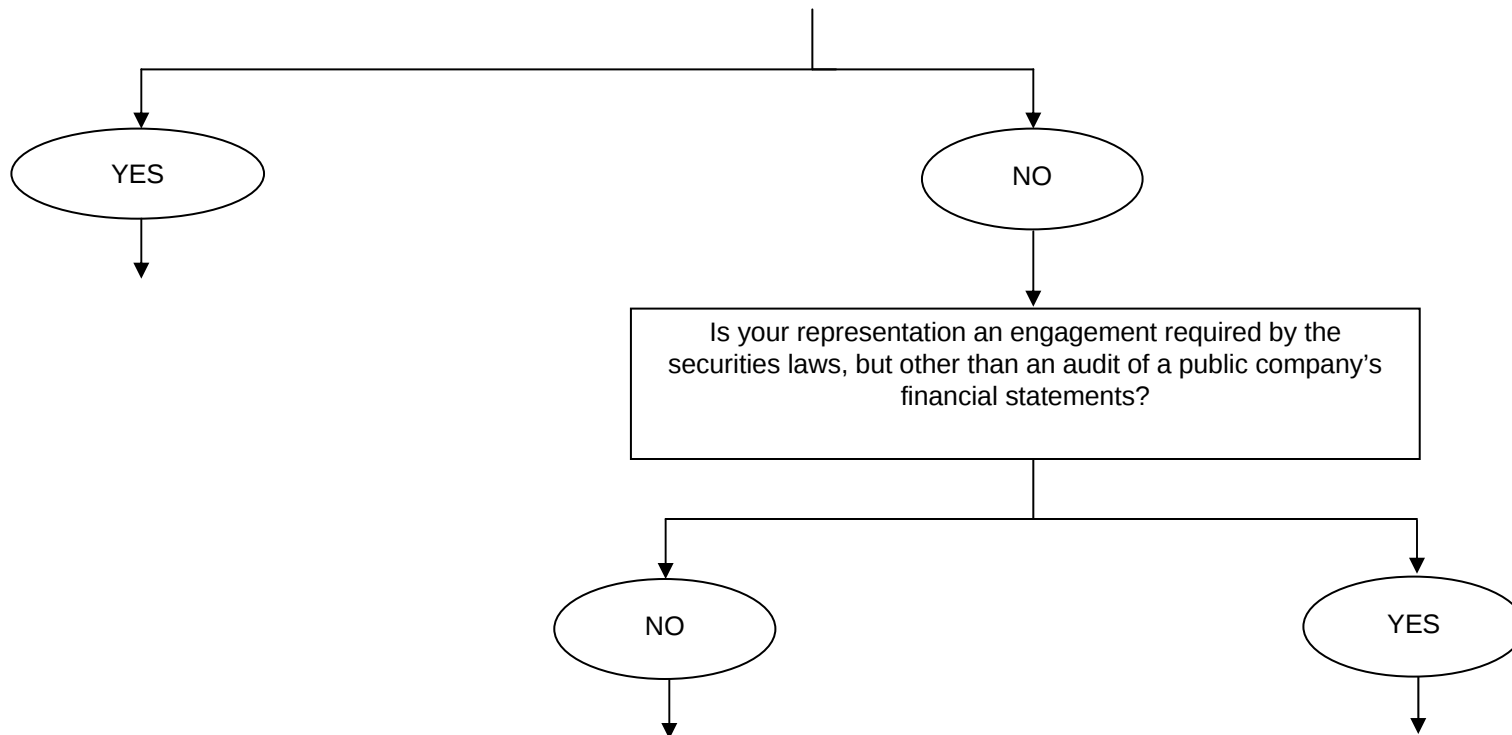
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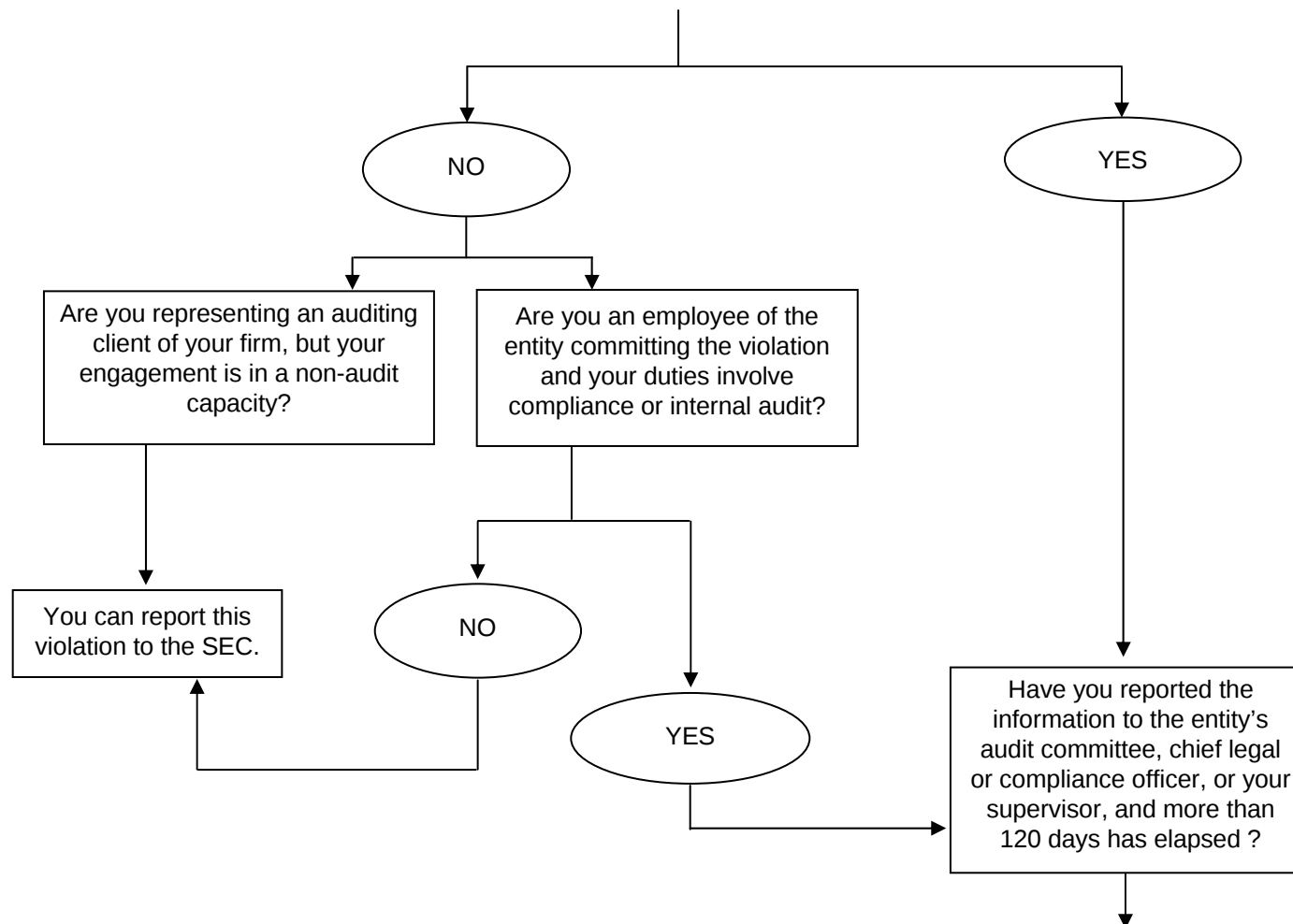
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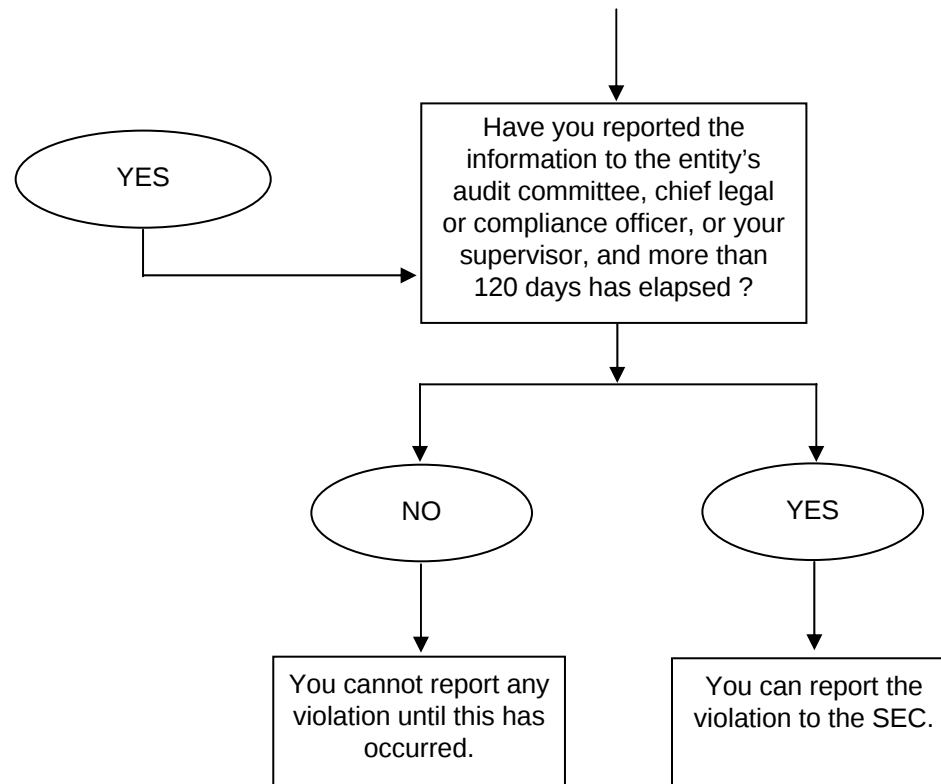
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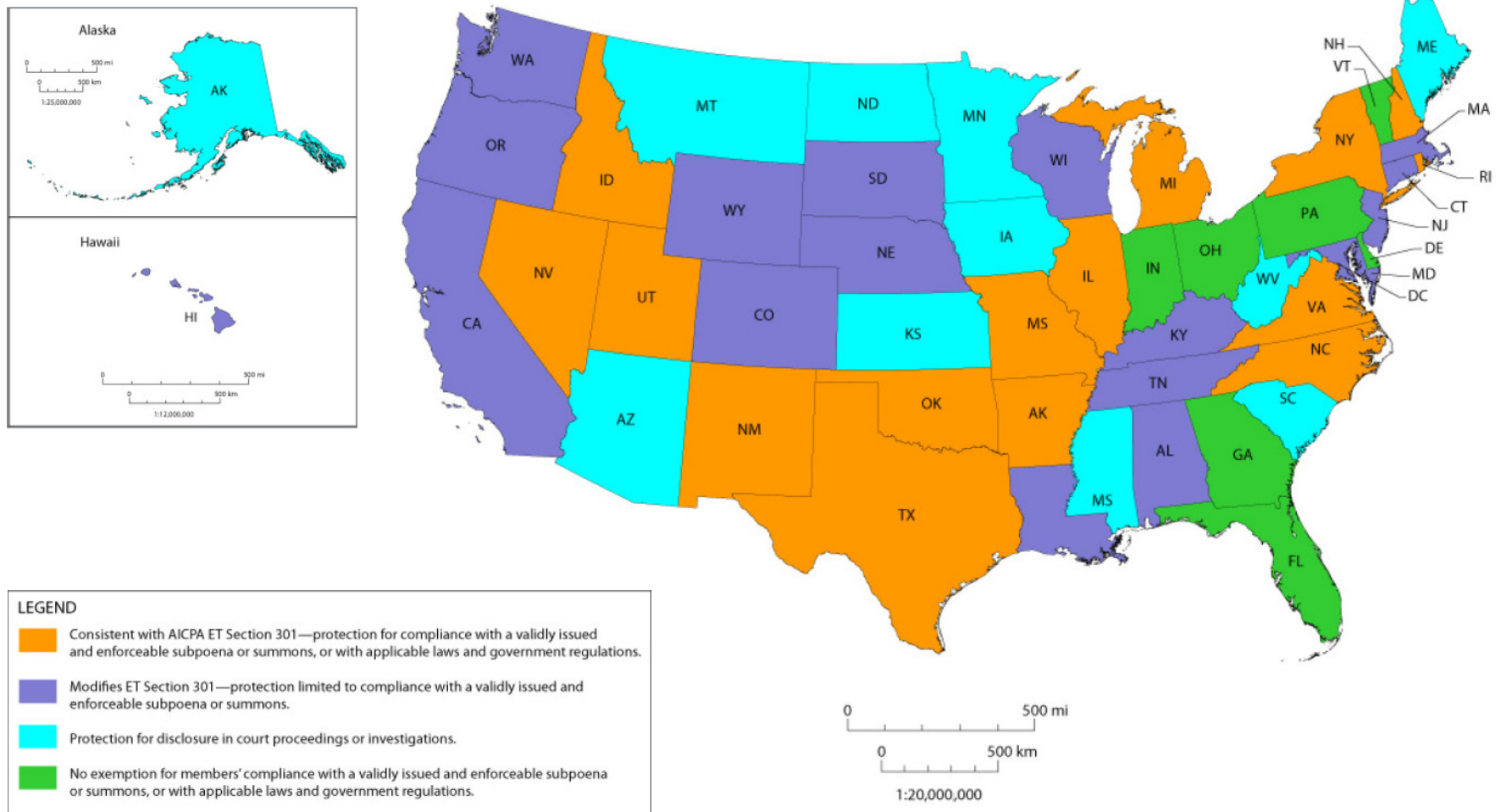
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Will I lose my license if I report a possible securities violation to the SEC?

State Confidentiality Rules Relevant to Whistleblowing

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- General Rule: Under the law of federal preemption, a law or regulation enacted by the federal government preempts conflicting state law.
- Application: Any state disciplinary rule that subject an otherwise qualifying accountant whistleblower to potential disciplinary action would be preempted by the whistleblower provisions in Dodd-Frank and invalid.

What constitutes a security?

- **Section 2(a)(1) of the Securities Act of 1933:**
“any note, stock, treasury stock, security future, security-based swap, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, pre-organization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a ‘security’”
- Similar definitions can be found in other federal securities statutes, including Section 3(a)(10) of the Securities and Exchange Act of 1934

- *SEC v. W. J. Howey Co.* test:
 - An investment contract is a “security” if “the person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party.” *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946)
- Elements of the test:
 - An investment in money
 - A common enterprise
 - Expectation of a profit
 - Solely from the effort of others

What is the international reach of the U.S. securities laws?

Reach of the SEC Whistleblower Program

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- With few exclusions or qualifications, a whistleblower can be any individual or group of individuals – regardless of citizenship.
- Eligible securities violations may occur anywhere in the world
- Potential international violators can be individuals or organizations (public or private)
- Jurisdictional Nexus: investors, investments, operations, employees or clients in the United States
- International Information Sharing

What is the statute of limitations for bringing an SEC enforcement action?

- 28 U.S.C. § 2462:
 - A “catch all” statute of limitations for actions brought by federal agencies in federal court
 - SEC has five years to bring an enforcement action seeking civil penalties from the date that the claim first accrued

- **Discovery Rule**
 - Common law rule that applies only to fraud claims
 - Holds that the statute of limitations for a fraud claim does not accrue until the fraud is discovered, or could have been discovered with reasonable diligence
- **Fraudulent Concealment/Equitable Tolling**
 - Temporarily suspends the statute of limitations clock, even though a claim has already accrued, if the defendant took affirmative steps to conceal the wrongful conduct
 - Applies to non-fraud claims also
 - SEC or private plaintiff must plead facts establishing that the defendant took affirmative steps to conceal the wrongful conduct

What steps can my organization take
to deter and detect securities violations?

5 Tips For Every Responsible Organization

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1. Invest in compliance
2. Have a game plan
3. Self-report
4. Communicate more
5. Establish a culture of integrity

What should every potential accountant whistleblower know?

5 SEC Insider Tips...

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1. Address the problem internally first.
2. Know the odds.
3. Attempt to identify violations.
4. Legally collect evidence.
5. Report anonymously.

Where can potential whistleblowers and other interested parties learn more about the securities laws and the SEC enforcement process?

Additional Resources

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SECWhistleblowerAdvocate

WHISTLEBLOWER PROGRAM

CORPORATE ETHICS

RESOURCES

ABOUT US



REQUEST CASE EVALUATION

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In this era of corporate scandal, the world needs more truth tellers. History has consistently shown that law enforcement authorities cannot effectively and efficiently police the marketplace without the assistance of private individuals and entities. Labaton Sucharow is dedicated to helping responsible organizations establish a culture of integrity and courageous whistleblowers to report possible securities violations—without regrets.

SEC Insider's
Guide

SEC Whistleblower
Program Handbook

Securities
Law Primer

SEC Whistleblower
Eligibility Calculator

SEC Whistleblower
Sanctions Database

Recent Op-Ed in USA Today Examines Ethical Breakdown in Financial Services Industry

Jordan Thomas - Monday, September 10, 2012

On September 5th, nestled between columns dissecting the presidential political drama as it unfolds, *USA Today* made space for another critical topic: *How Wall Street Creates Criminals*. In this [column](#), Cornell Law professor Lynn Stout and I address how and why the financial services industry has lost its moral compass, and the necessary first step for recovery: accountability. Building on data gathered in Labaton Sucharow's recent survey of the US & UK Financial Services Industry, *Wall Street, Fleet Street, Main Street: Corporate Integrity at a Crossroads*, we argue that Wall Street has to admit that it has a corporate ethics problem and then take bold measures to change it.

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A Powerful Partnership in Full Swing: SEC Issues First Award to Whistleblower

Jordan Thomas - Thursday, August 23, 2012

In the News

 Bloomberg Law—The SEC Whistleblower Program's Annual Report

 Fox Business—Will Whistleblower Rules Help SEC Investigations?

 Labaton Roundtable—Global Impact of U.S. Financial Reforms

[VIEW ALL NEWS](#)

**For the People.
By the People:**
The SEC Whistleblower
Program & Establishing
a Culture of Integrity

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