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## REGULATORY REFORM

### CFTC's New Whistleblower Office Opens for Business



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**O**n October 24, 2011, the Commodity and Futures Trading Commission's (CFTC) whistleblower rules became effective and its Whistleblower Office opened for business. The new Whistleblower Office is charged with implementing the CFTC's recently adopted whistleblower rules mandated by Section 748 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) and Section 23 of the Commodity Exchange Act (CEA).<sup>1</sup> Under the new rules, the CFTC may pay an award to an eligible whistle-

<sup>1</sup> Section 748 of Dodd-Frank, enacted on July 21, 2010, added a new Section 23 to the CEA, entitled "Commodity Whistleblower Incentives and Protection," which requires the CFTC to pay awards to qualified whistleblowers who voluntarily provide original information about violations of the CEA. See 17 C.F.R. pt. 165 (2011).

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blower who voluntarily provides the agency with original information about a violation of the CEA that leads to a successful enforcement action.

The CFTC first published its proposed rules in December 2010 and invited public comment. During the comment period, industry groups urged the CFTC to require a whistleblower to first report the information internally to an entity to be eligible for an award in order to preserve the integrity of internal reporting systems. After the public comment period closed, the CFTC revised the proposed rules to promote harmonization with the Securities and Exchange Commission's (SEC) whistleblower rules and program, which became effective on August 12, 2011, and to respond to concerns raised during the public comment period.

The final rules, which largely mirror the SEC's whistleblower rules, were adopted by the CFTC on August 4, 2011 in a 4-1 vote. While the final rules do not require a whistleblower to first internally report the information, they do provide incentives for whistleblowers to use a firm's internal compliance system as part of the reporting process and disincentives for whistleblowers who bypass or thwart these systems.

#### Significant Elements of the Whistleblower Rules

Section 23 of the CEA requires the CFTC to pay awards to qualified whistleblowers who voluntarily provide the agency with original information regarding violations of the CEA that lead to the successful resolution of a judicial or administrative action or successful enforcement of a related action. To be eligible for an

award, the whistleblower must also (1) follow the submission process set forth in Section 165.3; (2) be the original source of the information; (3) provide the CFTC with additional information as appropriate; and (4) enter into and adhere to the terms of a confidentiality agreement if requested by the CFTC.<sup>2</sup>

### Whistleblower

Under the rules, a whistleblower is defined as any individual, or group of individuals acting jointly, who voluntarily provide the CFTC with original information about a potential violation of the CEA in the manner set forth by Section 165.3.<sup>3</sup> The whistleblower does not, however, need to be employed by the entity about which he or she is reporting.

Companies and other entities are not considered “whistleblowers” and are ineligible to receive an award.<sup>4</sup> The rules also make certain individuals ineligible for an award because of their position, status, or the manner in which they obtained the information.<sup>5</sup> In addition to persons who are ineligible because the information is not considered “independent knowledge,”<sup>6</sup> the following categories of individuals are ineligible for an award: (1) individuals employed by various government, law enforcement and regulatory agencies; (2) individuals convicted of a crime related to the underlying judicial or administrative action; and (3) individuals who submit information already submitted by another whistleblower.<sup>7</sup>

### Submission Process

Section 165.3 sets forth the process for submitting information to the CFTC. To be eligible for an award, a whistleblower must (1) submit a completed Tip, Complaint or Referral form (Form TCR) online, by mail or facsimile; and (2) declare under penalty of perjury that the information contained in the Form TCR is true and correct to the best of the whistleblower’s knowledge and belief.<sup>8</sup>

### Voluntary Submission

Both the CFTC’s and SEC’s rules require that a whistleblower voluntarily submit information to be eligible for an award. To be considered a “voluntary submission,” the information must be submitted before the whistleblower or his or her agent receives any request from the CFTC, Congress, any other federal or state authority, the Department of Justice (DOJ), a registered entity, a registered futures association, or a self-regulatory organization (SRO) about the matter.<sup>9</sup> Under both the CFTC’s and SEC’s whistleblower programs, whistleblowers who are under a pre-existing legal or contractual obligation to the CFTC or SEC, respectively, or to certain other regulatory or law en-

forcement agencies, are not eligible to receive an award.<sup>10</sup> However, unlike the SEC, the CFTC also disqualifies whistleblowers who submit information after their employer has received a related request provided that the employer’s response is timely.<sup>11</sup>

### Original Information

To qualify as “original information,” the submission must be made for the first time after July 21, 2010, must be derived from the whistleblower’s independent knowledge or independent analysis, and must not be already known to the CFTC from any other source, unless the whistleblower is the original source of the information.<sup>12</sup> Information will not be considered original if it is exclusively derived from an allegation made in a governmental report, judicial action, or in news media.<sup>13</sup>

### Independent Knowledge

“Independent knowledge” is defined as “factual information in the whistleblower’s possession that is not generally known or available to the public.”<sup>14</sup> While a whistleblower may obtain “independent knowledge” through business or social contacts, it cannot be obtained exclusively from news media or other public information.<sup>15</sup> Information will not be considered to derive from “independent knowledge” if it is obtained exclusively: (1) from sources generally available to the general public; (2) through a communication that was subject to the attorney-client privilege; (3) in connection with the legal representation of an entity; (4) because the whistleblower was an officer, director, trustee or partner of the entity; (5) because the whistleblower’s duties included compliance or audit; or (6) in a way that violates the law.<sup>16</sup>

“Independent analysis” may be based on information that comes from publicly available sources as long as the whistleblower provides additional evaluation, analysis or insight into the publicly available information.<sup>17</sup>

### Successful Enforcement Action and Monetary Sanctions

For a whistleblower to be eligible to receive an award, he or she must provide information that leads to a successful judicial or administrative action by the CFTC which results in total monetary sanctions in excess of \$1,000,000, or leads to the successful enforcement of a related action by certain other regulatory or law enforcement agencies.<sup>18</sup> A successful resolution to an action is one that results in either a judgment or a settlement in favor of the CFTC.<sup>19</sup> The CFTC has explained that information may be determined to have led to a successful enforcement if “because of its high quality, reliability, and specificity” it has a “meaningful nexus to the [CFTC’s] ability to successfully complete its investigation, and to either obtain a settlement or prevail in a litigated proceeding.”<sup>20</sup>

<sup>2</sup> See 17 C.F.R. § 165.5(a), (b).

<sup>3</sup> See *id.* § 165.2(p)(1).

<sup>4</sup> See *id.* (defining whistleblowers as individuals).

<sup>5</sup> See *id.* § 165.2(g)(1)-(6).

<sup>6</sup> *Id.* § 165.2(g).

<sup>7</sup> See *id.* § 165.6(a)(1)-(3).

<sup>8</sup> See *id.* § 165.3.

<sup>9</sup> See *id.* § 165.2(o)(1). A whistleblower’s submission will not be considered voluntary if the CFTC or certain other authorities makes a request, inquiry or demand to the whistleblower or his or her agent, even if the whistleblower’s response is not compelled by a subpoena or other applicable law. See *id.*

<sup>10</sup> See *id.* § 165.2(o)(2).

<sup>11</sup> See *id.* § 165.2(o)(1).

<sup>12</sup> See *id.* § 165.2(k)(1), (2), (4).

<sup>13</sup> See *id.* § 165.2(k)(3).

<sup>14</sup> See *id.* § 165.2(g).

<sup>15</sup> See *id.* § 165.2(g)(1).

<sup>16</sup> See *id.* § 165.2(g)(1)-(6).

<sup>17</sup> See *id.* § 165.2(g), (h).

<sup>18</sup> See *id.* § 165.2(a), (e), (i).

<sup>19</sup> See *id.* § 165.2(n).

<sup>20</sup> 76 Fed. Reg. 53,172, 53,177 (Aug. 25, 2011).

Although an “action” generally refers to a single captioned judicial or administrative proceeding, for the purposes of making awards available in more cases, the CFTC will determine whether the \$1 million threshold is met by aggregating amounts ordered to be paid in separate actions that “arise out of the same nucleus of operative facts.”<sup>21</sup> However, any sanctions assessed against the whistleblower or any entity based on actions undertaken or directed by the whistleblower will not be counted in determining the total award amount.<sup>22</sup>

### *Amount of the Award*

Whistleblower awards are paid from the CFTC Customer Protection Fund established by Dodd-Frank.<sup>23</sup> As with the SEC’s whistleblower rules, the CFTC’s rules provide that the amount awarded to a whistleblower is in the discretion of the CFTC, which may exercise its discretion directly or through delegated authority.<sup>24</sup>

The CFTC has delegated the determination of most award amounts to the Whistleblower Award Determination Panel, a panel composed of staff from three of the CFTC’s offices or divisions, excluding the Division of Enforcement and the Office of General Counsel.<sup>25</sup> However, the heads of the offices or divisions of the staff members comprising the Panel must make award determinations in matters involving monetary sanctions exceeding \$15 million.<sup>26</sup> In addition, whether an award is made to one individual or to multiple whistleblowers in connection with the same action, the aggregate award amount must be at least 10 percent and no more than 30 percent of the monetary sanctions collected by the CFTC, the SEC and other authorities.<sup>27</sup>

In determining the award amount, the CFTC must consider various factors, including the following:

- **Significance of the Information Submitted to the Success of an Action** – e.g., whether the reliability and completeness of the information resulted in the conservation of resources; the degree to which the information supported successful claims;
- **Degree of Assistance Provided by the Whistleblower and His or Her Legal Representatives** – e.g., whether the whistleblower provided ongoing, extensive and timely cooperation and assistance; the timeliness of the whistleblower’s initial submission; whether the whistleblower encouraged the cooperation of others; remediation efforts undertaken by the whistleblower; and any unique hardships experienced by the whistleblower as a result of his or her whistleblowing activity;
- **Law Enforcement Interests and Enhancement of Enforcement Objectives** – e.g., the extent to which the

information furthers the CFTC’s programmatic interest in deterring violations; the degree to which an award enhances the CFTC’s ability to enforce the CEA; the degree to which an award encourages the submission of high quality information from whistleblowers; whether the subject of the submission is an enforcement priority; the danger posed to market participants by the underlying activity; the effectiveness of the whistleblower’s cooperation; and

- **Participation in Internal Compliance Systems** – e.g., whether the whistleblower made an internal report of the violation(s) before or at the same time as his or her report to the CFTC, and whether the whistleblower provided assistance during any internal investigation.<sup>28</sup>

Further, the following factors may decrease the size of an award: (1) the whistleblower’s culpability or involvement in the underlying violation; (2) any unreasonable delay in the whistleblower’s reporting of the violations; and (3) the whistleblower’s interference with internal compliance and reporting systems.<sup>29</sup> In addition, the CFTC must consider any potential adverse incentives from oversized awards.<sup>30</sup>

### *Related Actions*

Like the SEC, the CFTC will pay an award based on amounts collected in related actions, which are defined as judicial or administrative actions brought by certain entities, and are based on the same original information that the whistleblower voluntarily provided to the CFTC that led it to obtain sanctions of more than \$1,000,000.<sup>31</sup> However, the CFTC’s rules are broader than the SEC’s in that they permit actions brought by a greater number of entities to be deemed related and they permit awards even if the SEC has already paid an award for the same information.<sup>32</sup>

Under the CFTC’s rules, actions brought by the DOJ, an appropriate department or agency of the federal government, a registered entity, a registered futures association, an SRO, a state criminal or appropriate civil agency, or a foreign futures authority may qualify as “related actions.”<sup>33</sup> In contrast, the SEC’s rules provide that only actions brought by the Attorney General of the United States, an appropriate regulatory authority, an SRO, or a state attorney general in a criminal case may qualify as “related actions.”<sup>34</sup> In addition, the CFTC permits awards for related actions even if the SEC has already awarded the whistleblower for the same infor-

<sup>21</sup> See *id.* at 53,173; 17 C.F.R. § 165.2(a).

<sup>22</sup> See 17 C.F.R. § 165.17.

<sup>23</sup> See *id.* § 165.2(f). The CFTC deposits into the Fund any monetary sanctions it collects in any covered judicial or administrative action that are not otherwise distributed to victims, unless the Fund exceeds \$100 million. See *id.* § 165.12(b)(1). A “covered judicial or administrative action” is any action brought by the CFTC under the CEA that results in sanctions exceeding \$1 million. See *id.* § 165.2(e). However, the CFTC may not consider the size of the Fund in determining an award. See *id.* § 165.9(d).

<sup>24</sup> See *id.* § 165.9.

<sup>25</sup> See *id.* § 165.15(b).

<sup>26</sup> See *id.*

<sup>27</sup> See *id.* § 165.8(a)(1)-(2).

<sup>28</sup> See *id.* § 165.9(a), (b). Like the SEC, the CFTC refused to require whistleblowers to first report potential violations through internal compliance systems. However, both agencies provide incentives for whistleblowers who use internal compliance systems and punish whistleblowers who undermine an entity’s internal compliance system. Specifically, the CFTC’s rules provide (1) larger awards to whistleblowers who use internal compliance systems; and (2) credit for information reported by the entity as a result of investigations or audits resulting from the whistleblowing activity. See *id.* §§ 165.2(e)(3), 165.9(b)(4).

<sup>29</sup> See *id.* § 165.9(c)(1)-(3).

<sup>30</sup> See *id.* § 165.9(a)(5).

<sup>31</sup> See *id.* § 165.2(m).

<sup>32</sup> See *id.* §§ 165.2(p), 165.11(a).

<sup>33</sup> See *id.* § 165.11(a)(1)-(5).

<sup>34</sup> *Id.* § 240.21F-3(b)(1).

mation – the SEC, however, would bar an award if the situation were reversed.

### Appeals

A whistleblower may appeal eligibility and award determinations to an appropriate federal appellate court.<sup>35</sup> However, any such challenge must be filed within 30 days of the issuance of the CFTC's final order.<sup>36</sup>

### Anti-Retaliation Measures

Like the SEC, the CFTC provides statutory protections for whistleblowers who suffer retaliation as a result of their whistleblowing activity. Section 23(h) of the CEA establishes broad anti-retaliation protections for whistleblowers even if they are not ultimately eligible for an award.<sup>37</sup> To qualify for such protection, a whistleblower must (1) have a reasonable belief that the information submitted relates to a possible violation of the CEA, or the rules or regulations thereunder, that has already occurred, is ongoing, or is about to occur; and (2) submit the information to the CFTC in the manner set forth in Section 165.3.<sup>38</sup>

The primary protection provided to whistleblowers is an assurance of confidentiality. Under its rules, the CFTC must maintain in confidence information that could reasonably be expected to reveal the identity of a whistleblower except when disclosure is required to a defendant or respondent in connection with a government proceeding.<sup>39</sup> However, if the CFTC determines that disclosure is necessary to accomplish the purpose of the CEA and to protect customers, it may disclose the information to the DOJ, certain state and federal government departments and agencies, registered entities, registered futures associations, SROs, and foreign futures authorities.<sup>40</sup> In addition, the rules permit whistleblowers to submit information anonymously to the CFTC, in accordance with the procedures set forth in Sections 165.3 and 165.7(c).<sup>41</sup>

Further, Dodd-Frank provides whistleblowers who submit information to the CFTC a federal private right of action against employers who retaliate against them for making a submission to the CFTC.<sup>42</sup> This private right of action is available even if the whistleblower is not eligible to receive an award.<sup>43</sup> Under this anti-retaliation provision, retaliation is broadly defined to encompass any form of discrimination against a whistleblower, including termination, demotion, suspension, threats and harassment.<sup>44</sup> Further, the provision provides that a prevailing whistleblower may be entitled to reinstatement, back pay and other compensation, including reasonable attorneys' fees.<sup>45</sup>

<sup>35</sup> See *id.* § 165.13(a).

<sup>36</sup> See *id.*

<sup>37</sup> 7 U.S.C. § 26(h).

<sup>38</sup> 17 C.F.R. § 165.2(p)(2).

<sup>39</sup> 7 U.S.C. § 26(h)(2); 17 C.F.R. § 165.4(a).

<sup>40</sup> See 7 U.S.C. § 26(h)(2)(C)(i); 17 C.F.R. § 165.4(a). The CFTC may also make disclosures in accordance with the Privacy Act of 1974, 5 U.S.C. § 552a. See 7 U.S.C. § 26(h)(2)(A).

<sup>41</sup> 17 C.F.R. § 165.4(b).

<sup>42</sup> See 7 U.S.C. § 26(h)(1)(B); 17 C.F.R. pt. 165, App. A.

<sup>43</sup> See 7 U.S.C. § 26(h)(1)(B); 17 C.F.R. pt. 165, App. A.

<sup>44</sup> See 7 U.S.C. § 26(h)(1)(B); 17 C.F.R. pt. 165, App. A.

<sup>45</sup> See 7 U.S.C. § 26(h)(1)(B); 17 C.F.R. pt. 165, App. A. Under the CFTC's whistleblower rules, the statute of limitations for a private right of action for retaliation is two years from the

## Other Elements of the Whistleblower Program

### No Immunity from Prosecution

The rules do not provide whistleblowers who violate the law with immunity from prosecution.<sup>46</sup> Thus, the CFTC may bring an action against a whistleblower even if the whistleblower has provided information to the agency.<sup>47</sup> However, the CFTC's Division of Enforcement will consider the whistleblower's cooperation in determining any sanctions recommendations it makes to the CFTC.<sup>48</sup>

### Communications with Whistleblowers from Represented Entities

The CFTC staff is authorized to communicate directly with a whistleblower, even if the whistleblower is a director, officer, member, agent or employee of an entity that has counsel.<sup>49</sup> Further the staff is not required to seek the consent of the entity's counsel.<sup>50</sup>

### Nonenforceability of Rights and Remedies

The rights and remedies provided for in the rules cannot be waived by any agreement, policy or condition of employment, including an arbitration of disputes agreement.<sup>51</sup> Such agreements are considered unenforceable.<sup>52</sup>

## Conclusion

The strong financial incentives and whistleblower protections provided by the CFTC whistleblower rules almost certainly will accomplish the goals of Dodd-Frank – to promote the reporting of credible whistleblower tips to the CFTC and other government agencies. In turn, this influx will lead to a significant increase in enforcement activity. Thus, firms are now facing heightened risk from enforcement actions and related private civil litigation. These risks underscore the need for firms to evaluate and strengthen compliance programs to ensure there are open channels of communication with employees, strong policies and procedures and training programs, strict anti-retaliation policies, and well-trained compliance and legal personnel who can quickly conduct investigations.

Many industry observers fear that the new CFTC and SEC whistleblower programs will undermine or hamper private internal compliance programs by allowing whistleblowers to bypass internal reporting systems in favor of direct reporting to the federal government. Although the CFTC and SEC attempt to address and mitigate these concerns in their rules, neither agency requires a whistleblower to actually use existing internal compliance systems. This will mean that an entity may first learn about a whistleblower's complaint when it receives a call from the government. Nonetheless, even in

date of the violation. See 7 U.S.C. § 26(h)(1)(B)(iii). In contrast, the SEC's rules allow six years from the date of the violation or three years from when the material facts supporting the claim were known or should have been known. See 15 U.S.C. § 78u-6(h)(1)(B)(iii).

<sup>46</sup> See 17 C.F.R. § 165.16.

<sup>47</sup> See *id.*

<sup>48</sup> See *id.*

<sup>49</sup> See *id.* § 165.18.

<sup>50</sup> See *id.*

<sup>51</sup> See *id.* § 165.19.

<sup>52</sup> See *id.*

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those circumstances, the entity should still conduct a thorough internal investigation, consider reporting the

results of the investigation to the government, and institute appropriate remediation.