

New York Attorney General's Proposal Furthers a Trend Toward Greater Incentives for Whistleblowing and Greater Risks for Corporations

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Last week, New York Attorney General Eric Schneiderman announced his proposed "Financial Frauds Whistleblower Act," which would provide compensation to whistleblowers who report fraud in the banking, securities, insurance, and financial services industries. Modeled after the federal Dodd-Frank whistleblower provisions, Attorney General Schneiderman's proposal would give whistleblowers 10 to 30 percent of certain state fines that exceed \$1 million. Because New York regulatory and enforcement agencies have brought enormous and far-reaching enforcement actions in recent years, Attorney General Schneiderman's proposal could create significant incentives for employees to provide information to the government rather than (or in addition to) reporting the information internally. With employees facing such powerful incentives, it is more important than ever for companies to have sophisticated compliance programs and to act quickly to investigate allegations or evidence of misconduct.

The New York Proposal

Although Attorney General Schneiderman has not yet released the proposed text of the Financial Frauds Whistleblower Act, he has presented the general terms of his proposal. If passed by the New York State legislature, the proposal would provide monetary rewards to individuals who voluntarily provide original information, not previously known to the Attorney General, on illegal activity in the banking, securities, insurance, or financial services industries. Under the proposed legislation, whistleblowers would receive 10 to 30 percent of the money obtained in certain financial fraud cases if their information leads to a state enforcement action with sanctions of more than \$1 million. The proposal also would protect employees against retaliation by strengthening existing labor protections to make it explicitly unlawful for employers to discharge, demote, suspend, or otherwise harass employees who report suspicious or fraudulent activity to supervisory or internal compliance staff. Attorney General Schneiderman thus promised his proposed law would be "the strongest, most comprehensive in the nation."

Whistleblower Incentives are Greater than Ever

This most recent announcement reflects a widespread trend toward strengthening the incentives for whistleblowers to come forward with information regarding possible fraud or misconduct. The potentially lucrative -- and in some cases life-changing -- rewards that are available under the federal Dodd-Frank Act have garnered much attention. But the less-noticed New York proposal could likewise have a significant impact, because New York regulators and enforcement agencies have been very active in bringing some of the largest investigations and enforcement actions in the financial sector. For example, in the three years since it was created, the New York State Department of Financial Services (DFS) has obtained more than \$3 billion in fines from banks around the world, including \$2.2 billion from BNP Paribas, \$340 million from Standard Charter, and \$250 million from the Bank of Tokyo Mitsubishi. DFS has also imposed independent compliance monitors in many settlements.

On the federal level, the SEC has already pushed to bring more whistleblower cases since the 2010 passage of the Dodd-Frank financial reform bill, which created the Agency's whistleblower program. The addition of §21F to the Securities Exchange Act of 1934, codified at 15 U.S.C. §78u, mandates a reward of 10 to 30 percent of any money the government collects from an enforcement action based on "original" information received from the whistleblower resulting in sanctions (including fines,

disgorgement, and interest) against the company in excess of \$1,000,000. It appears that whistleblowers have been encouraged by the program, with the SEC fielding 3,620 tips on potential violations in 2014. This represents a 21 percent increase from two years before.

Importantly, government officials are aggressively looking for any signs of retaliation against whistleblowers or other efforts to silence whistleblowers. According to The Wall Street Journal, the SEC recently launched a probe into an undisclosed number of companies, asking them to turn over every nondisclosure, confidentiality, severance, and settlement agreement they entered into with employees since Dodd-Frank went into effect.

Implications for Your Company

If the New York Attorney General is correct and the proposed law amounts to the "gold standard" in whistleblower regulation, the legal and compliance landscape for companies will be more treacherous than ever. This makes it all the more important that companies have sophisticated compliance programs that are appropriately tailored to the companies' risk profiles, and that companies move quickly to investigate allegations and evidence of misconduct. While even the most effective compliance program cannot prevent all potential wrongdoing, history has shown that enforcement agencies are particularly focused on the extent to which companies that are under investigation took steps to prevent misconduct and how those companies responded when evidence of misconduct came to light. Failure to act quickly and appropriately can cost your company greatly -- and it can provide an enormous windfall to opportunistic employees who stumble upon evidence of wrongdoing.

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