

An hourglass with blue sand is centered in the frame against a solid blue background. The sand is flowing from the top bulb to the bottom bulb. The hourglass is made of clear glass, and the sand is a vibrant blue color. The background is a uniform, bright blue.

This webinar will begin shortly.

**FIA**



# Self-Reporting in the Age of Whistleblowers



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An L&C Division Webinar  
December 5, 2024



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# Presenters

## Host:

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# Why should you care?

- Most investigations start with whistleblowers.
- How you handle and react to whistleblowers can materially affect the outcome of an investigation.
- Clock starts ticking with whistleblower complaint
  - Decide if, when, and how to self-report.
  - Consequences can be significant either way.
- You can learn how to avoid the avoidable and take advantage of opportunities.
  - Enforcement actions stemming from missteps with whistleblowers are avoidable.



# SEC and CFTC Whistleblower Programs

- **Hefty awards = increased incentives.**
  - SEC: ~\$1.9B since 2011
  - CFTC: ~\$365M since 2014
- **The whistleblower will not receive civil or criminal amnesty.**
  - Whistleblower can be culpable, although the size of the award may be adjusted based on whistleblower's conduct.
- **Internal reporting or consultation with corporate counsel is not required.**
- **Whistleblowers can submit information anonymously.**
- **Increased diversity of whistleblowers.**
  - Company insiders and outsiders.



# The DOJ's Whistleblower Program

- Basic elements:
  - Patterned after successful SEC/CFTC programs
    - Designed to fill in gaps
    - Awards information in one of four areas – financial fraud, foreign corruption, domestic corruption and healthcare fraud
  - **Voluntary reports of original, truthful information that is materially helpful to prosecution**
    - Original: “independent knowledge or independent analysis.”
    - Non-public and previously unknown to the DOJ





# The DOJ's Whistleblower Program

- Basic elements, continued:
  - No DOJ award if eligible for other whistleblower awards
  - The whistleblower report must result in a civil or criminal forfeiture recovery of more than \$1 million
  - Awards are discretionary
- Program encourages whistleblowers to first report issues internally





# Overview of the Program

The Pilot Program encourages companies to make voluntary self-disclosures:

- A corporation can still qualify for the benefits of making a self-disclosure if it makes a disclosure within 120 days of receiving an internal whistleblower report or before the DOJ reaches out to the company, whichever is sooner.
- Thus, in practice, a company may have less than 120 days to make a voluntary self-disclosure.
- Self-report within 120 days: company eligible “presumption of a declination,” regardless of who first reported to DOJ
- DOJ intent is to create “a race to the front steps” of the Department
  - Force companies to re-assess the calculus of making a self-report





# Protecting Whistleblowers

- **Anti-retaliation and “pre-taliation” measures.**
  - Aggressive pursuit of those who inhibit or interfere with whistleblowers.
  - Regulators interpret overbroad contract terms as attempts to chill reporting.
- **CFTC**
  - Settled charges for impeding voluntary communications with the CFTC about possible violations. Employment and separation agreements included broad non-disclosure provisions governing confidential information.
- **SEC**
  - Settled with seven companies for using employment, separation, and settlement agreements that included provisions impeding reporting, including “disclaim[ing] and waiv[ing] any right to share or participate in any monetary award resulting from the prosecution of such charge or investigation or proceeding.”
- No actual acts impeding or interfering with reporting or that company took action to enforce agreements



# Basic Fact Pattern

- **Lonestar Legends is an energy company with operations around the world and a trading desk in Houston used primarily to hedge its assets.**
- **Bayou City Brokers is a registered introducing broker based in Houston, Texas.**
- **Lonestar Legends is a customer of Bayou City Brokers.**
- **H-Town Trading is a proprietary trading firm affiliated with Bayou City Brokers.**
- **Bayou City Brokers and H-Town Trading are also based in Houston.**



# Scenario 1:

- An employee (Wendy Whistle) of Bayou City Brokers has evidence of another Bayou employee obtaining non-public information of Lonestar's orders and trading ahead of those orders for the benefit of H-Town Trading (in which he has a financial interest).
- Wendy Whistle tried to submit a complaint to Bayou City Brokers' hotline, but it was not functioning at the time. Wendy then sends an email to her supervisor, David Hardlycares.
- Hardlycares tells Wendy Whistle to submit the complaint to Bayou City Brokers' hotline. She tries again, but the hotline is still not functioning.
- Hardlycares briefly discusses the complaint with his manager, but they find the complaint to be frivolous and do not enter it into the company's internal reporting system.
- A month later, Bayou City Brokers' compliance manager mentions Wendy Whistle's complaint to you, the GC of Bayou City Brokers, in passing.



# Questions

- What do you do once you receive the complaint?
- If subject to scrutiny by government regulators or other third parties, does Lonestar Legends' internal reporting framework pass muster?
- You understand that time is of the essence and need to decide how to respond to the complaint.
  - How should you decide the appropriate steps to take?
  - What weight should you give to the new DOJ policy, which gives whistleblowers a 120-day window to report misconduct following an internal report?



# Answers/Next Steps

- When you receive the complaint:
  1. Ensure preservation of documents and relevant information. Publish a litigation hold.
  2. Ensure the hotline protocol and other relevant reporting protocol is followed. This typically includes logging the complaint and notifying the appropriate personnel.
    - Lonestar's protocol would not pass muster.
  3. Conduct the appropriate internal investigation.
    - a. Investigate early and thoroughly. You won't know until you investigate if you will want to take advantage of the 120-day window.



# Scenario 2

- **New Facts:**
  - After looking at Wendy Whistle's personnel files, you learn that she has a recent history of poor performance reviews, and was warned that she would be terminated if her performance did not improve.
- **Questions:**
  - What steps, if any, should Bayou City Brokers take in response to Wendy Whistle's personnel issues?
  - None. Her personnel issues should not change your response to the complaint. You still have to investigate it thoroughly and objectively, no matter what. This is a good reminder, however, of the fundamental questions to ask yourself when conducting an internal investigation: (1) what is the scope of your investigation, and (2) who is going to conduct it?





# Scenario 2, Cont'd

What if Wendy Whistle's complaint was submitted anonymously? You would like to get more information from the anonymous reporter on the allegations; what, if anything, should you do to identify and approach her?

- Your initial steps should focus on an objective, thorough investigation of the allegations. It can create unnecessary risk to hunt for the identity of the whistleblower. You want to create an environment in which people feel free to raise concerns and are confident that the concerns will be investigated and responded to in an objective, fair manner, and that they will not be subjected to ridicule or discipline for raising concerns.
- If the identity of the whistleblower is uncovered during the investigation, that is okay, but you should not actively try to figure it out. Generally, the person who reports an issue does not change the assessment of the allegations, which should always be fair and objective.



# Scenario 3

- You, as the GC, initiate an investigation of the complaint. The assigned investigator collects and reviews the emails of the employee who allegedly misused confidential information but does not find any evidence of misconduct and closes the investigation. The investigator does not conduct any interviews or look at other sources of evidence. The investigator does not contact Wendy Whistle.
- Questions:
  - What additional steps should Bayou City Brokers have taken to ensure an appropriately-resourced investigation?

# Scenario 3 Answers/Next Steps

- Generally, it is best practice to interview the whistleblower, so long as they are willing to engage. There are situations where that might not be appropriate, but usually you interview the whistleblower and hear what they have to say.
- You have to handle the interview carefully, allow them to tell their story and are not be made to feel like they are being “grilled.” You want them to know you are investigating their concerns and following up on what they uncover.
- Once again, it is always good to consider who should conduct your investigation. Factors such as involvement of senior management, headline-grabbing conduct, or significant misconduct should be handled by outside counsel.



# Additional Facts

- As part of the investigation, the investigator meets with Wendy Whistle to discuss her complaint. During the meeting, she informs the investigator that she was unhappy with the way her supervisor handled her complaint, and that she has already reported the misconduct to the CFTC through its whistleblower program.
- Question:
- How should the Bayou City Brokers respond?
  - **Answer:** It should not change the investigation, but now you're on the 120 day clock. Even though the report is made to the CFTC, you need to investigate and determine if you should self report to the CFTC and/or DOJ.

# To Self-Report or Not to Self-Report: That Is the Question

## Point:

- **Ian McGinley, CFTC Director of Enforcement:**
  - “Ample” reasons to self-report; can “really make a difference” and can lead to “an opportunity for significant self-reporting credit.”

## Counterpoint:

- **Caroline Pham, CFTC Commissioner:**
  - “By creating an impossible-to-meet standard for receiving cooperation credit, or by being arbitrary in the application of any standard, the CFTC’s policy on self-reporting looks a lot like bait-and-switch.”



# Issues to Evaluate/Consider

- **When?**
  - “Reasonably prompt”
  - Is there time to investigate first? Typically, yes
  - Identify key “relevant” facts
  - With reasonable certainty
- **Is it necessary?** Factors to consider:
  - Front page news or material to f/s
  - Involves senior management
  - Fraud or deceit involved
  - Issue ongoing or resolved and remediated





# CFTC Whistleblower

- **Reminder:** During your meeting with Wendy Whistle, she told you that she had reported the misconduct to the CFTC.
- **Should you self-report to the CFTC?**
  - When? Investigate, or report right away?
  - What if the employee identified by Wendy Whistle resigns?
  - What if a second employee has filed a whistleblower report?
  - What should you consider doing to protect Wendy?
- **Change the Facts:** If Wendy went straight to the Department of Justice, does that change the way you should act?





# CFTC Whistleblower – Answers/Next Steps

## Considerations for self-reporting to the CFTC:

- You will almost always investigate first, unless you have a very serious violation that you need to report immediately.
- The potential wrongdoer's resignation does not change anything, since the conduct occurred on your watch. Your oversight and supervision are implicated.
- A second whistleblower report signals that you may have a pattern of misconduct. You would likely want to expend more resources; if you have not already done so, you should hire outside counsel.
- Protecting Wendy: you should instruct her supervisors to avoid taking any negative action towards her.



# If Wendy went straight to the DOJ...

This really does not change the scope of your investigation, but it does affect timing -- you are now “on the clock” because the 120-day window is open.

The objective remains – conduct a fair and objective investigation, consider all the factors and decide whether to self-report.

**There are incentives and risk with self-reporting.**



# Self-Reporting: The Incentives

- Opportunity to frame the issue.
  - You create the narrative before they do.





# Self-Reporting: The Incentives

- **Self-Reporting Credit**

- **What *should* it look like?**

- Strong compliance program → uncover and report compliance failures  
→ receive credit

- **What *does* it look like?**

- Earning it is “not easy” – Ian McGinley
  - Requires not only self-reporting, but full cooperation and remediation.
  - No set formula for giving credit so outcome is often unpredictable



# Cooperation: The Incentives

- Cooperation Credit

- *What should it look like?*

- Timely, meaningful, and full cooperation → meaningfully assists the Commission's investigation/enforcement action → credit

- *What does it look like?*

- Several factors: material assistance, **timeliness**, nature, quality, but no formula.
- "...one significant factor ... is whether the company's cooperation resulted in material assistance...and the success thereof. If the whistleblower has already provided us with some, most, or all of the relevant information...the opportunity for the company to be a real value add may be limited." – Ian McGinley



# Remediation: The Incentives

- Remediation Credit

- **What *should* it look like?**

- Take action in response to misconduct → add internal measures to prevent same or similar misconduct → address employment of persons responsible for misconduct → receive credit

- **What *does* it look like?**

- Mostly as it should, with exceptions (Raizen case)
- But no formula and therefore unpredictable



# Scenario 4

- **New Facts:**
  - The internal investigations team collects and reviews the communications and trade data of the alleged wrongdoer. The team also interviews Wendy Whistle and several others.
  - Through the course of the investigation, the team learns that there were at least five other employees who had been taking the opposite side of Lonestar Legends' customer orders on behalf of accounts at Bayou City Brokers and H-Town Trading, with profits ranging from \$1-1.5M.
  - The team also learns that one of the employees was disciplined for misusing confidential information previously.

## What do you do?





# Scenario 4 Answers/Next Steps

- **You have a serious problem and need to proceed accordingly.**
  - You need to conduct a swift and thorough investigation, pull all of your facts together, and bring this to the regulators. A thorough, forthcoming self-report is likely in your best interests.
  - The 120-day clock is ticking. Consider whether to report to CFTC, and/or DOJ.

# Self-Reporting: The Risks

- Enhanced Penalties for Recidivism

- But what really *is* recidivism?

- Reflection of a bigger issue, or ticky-tack problems to clean up

- “The Division intends to prioritize recidivism as a **significant aggravating factor** under our existing penalty guidance. This means that recidivists can expect the Division to recommend increased penalties...and will be a significant factor that will influence whether the Division will recommend a corporate compliance Monitor or Consultant.” – Ian McGinley





# Self-Reporting: The Risks

- **Opening the Door to Parallel Investigations**
  - Self-report to the CFTC, and then DOJ or the SEC come knocking.
- **Opening the Door to a Failure to Supervise Charge**
  - What constitutes failure to supervise? (166.3)
    - Has significantly expanded to include not just customer account handling
  - Evaluating Compliance Programs
    - Impacts how you design your program
    - Whether to consider recidivism in your compliance



# Failure to Supervise?

- Recall that upon receipt of Wendy Whistle's complaint, David Hardlycares shared the information with the compliance managers. The managers briefly discussed it, but they concluded it was frivolous and did not enter it into either company's internal reporting system or follow-up.
- Assume now that the CFTC has issued a subpoena asking for information about matters that were the subject of the Wendy's complaint?
  - What should you do?
  - Failure to supervise?



# Answers/Next Steps

- If the CFTC has issued a subpoena, it is unlikely you can get credit for self-reporting. *But* you are still eligible for remediation and cooperation credit, so you need to follow the process and procedures to put yourself in a position to receive it.
- Whether or not you are tagged with a failure to supervise charge depends on the circumstances and whether the compliance managers can demonstrate that they had a reasonable basis for not entering it into the system.
  - Remember that a compliance failure  $\neq$  supervision failure.



# Scenario 5

- **New Facts:**
  - Now assume that there was no whistleblower, but through the companies' extensive trade surveillance programs and internal review system, Bayou City Brokers discovered the misconduct after one month and reported it to the CFTC.
    - Failure to supervise?
      - What if it took six months to report it?



# Scenario 5 Answers/Next Steps

- This should not lead to a failure to supervise charge. Bayou City Brokers uncovered the misconduct, took the necessary action to remediate it, and reported it. That is not a failure to supervise, that is how the system is supposed to work.
- If they delayed in reporting the issue, they will need to explain why. If it was to fully investigate and remediate, that might be okay, but the longer the delay, the more likely the CFTC is to ask questions.



# Self-Reporting: The Risks

- **Opening the Door to a Fraud Charge?**
  - “The CFTC has sought to bring fraud charges against market participants for allegedly making false statements to the CFTC when a market participant later discovers that the information provided in a self-report was not entirely accurate—even when it thought the information was accurate at the time of the disclosure to the CFTC.” – Caroline Pham
- **If this happens, should you revise a self-report?**
  - Consider:
    - If you self-reported and you find there was something wrong, correct it promptly as your duty.





# Key Takeaways

- 1. Design and implement a strong compliance program to proactively detect and remediate misconduct. Test the program regularly to assess effectiveness.**
  - A robust compliance program and related internal controls with a strong compliance culture is the best defense against employee misconduct.
  - Periodic efforts to assess and enhance the compliance program and culture serve companies well in the event that misconduct occurs at some future time.
- 2. Have multiple internal reporting channels to allow employees to report misconduct easily and anonymously to the company instead of the CFTC, DOJ, or other regulators.**
  - Companies should also conduct training, so employees are not only aware of these channels, but also understand how to make timely reports.
  - To encourage reporting, companies must provide assurance to employees that their allegations will be taken seriously and addressed.
  - Sharing information with employees, including about culture survey results and, as possible, internal investigations, can foster employee confidence.



# Key Takeaways

3. Investigate all reports swiftly, so whistleblowers know that their concerns are being acted upon and possibly dissuade whistleblowers from escalation outside of the company.
4. Have clear policies on anti-retaliation, making clear that employees are always free to go to the government.
5. Given the increased risk of detection, when allegations of misconduct arise, companies should work promptly with counsel to consider whether a voluntary self-disclosure is appropriate, preempting government notification by a whistleblower and maintaining eligibility for the benefits offered for such disclosures.

The slide features a white background with decorative geometric shapes. In the top-left corner, there is a small, overlapping shape composed of a light green triangle and a light blue triangle. On the right side, there is a large, overlapping shape composed of a light blue triangle and a light green triangle. The word "Questions?" is centered on the slide in a large, dark blue, sans-serif font.

# Questions?

# REFERENCES

1. SEC Whistleblower Program, <https://www.sec.gov/enforcement-litigation/whistleblower-program>
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6. Principal Deputy Assistant Attorney General Nicole M. Argentieri, Remarks on DOJ Whistleblower Program September 17, 2024, <https://www.justice.gov/opa/speech/principal-deputy-assistant-attorney-general-nicole-m-argentieri-delivers-remarks-newly>
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9. Keynote Address of Ian McGinley Before NYC Bar Association Futures and Derivatives Committee Conference, April 11, 2024 <https://www.cftc.gov/PressRoom/SpeechesTestimony/opamcginley3>
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12. Remarks of Enforcement Director Ian McGinley at the New York University School of Law Program on Corporate Compliance and Enforcement: “The Right Touch: Updated Guidance on Penalties, Monitors, and Admissions,” October 17, 2023, <https://www.cftc.gov/PressRoom/SpeechesTestimony/opamcginley2>
13. 17 C.F.R. §166.3 Supervision, <https://www.law.cornell.edu/cfr/text/17/166.3>



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The logo consists of the letters 'FIA' in a bold, sans-serif font. The 'F' is dark grey. The 'I' is dark grey with a green triangle overlapping its right side. The 'A' is formed by a green triangle on the left and a blue triangle on the right, with a smaller blue triangle overlapping the bottom right of the green one. The background features large, overlapping geometric shapes in light green, light blue, and white.