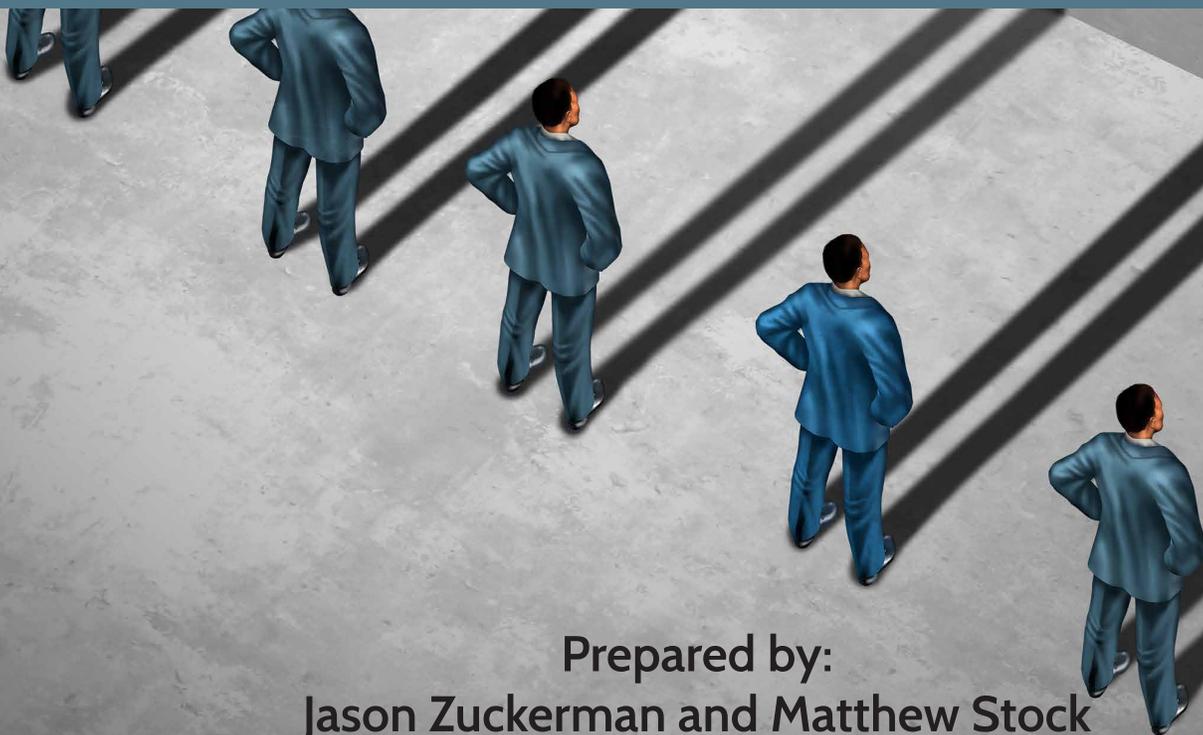




SEC Whistleblower Rewards for Reporting Inflated Key Performance Metrics



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SEC Whistleblower Rewards for Reporting Inflated Key Performance Metrics

Written by Jason Zuckerman and Matthew Stock – 7/13/18

If I report my company's inflated key performance metrics, can I qualify for an SEC whistleblower reward?

Yes, under the SEC Whistleblower Program a disclosure to the SEC about a company's falsely inflated key performance metrics can qualify for a SEC whistleblower reward in the amount of 10% to 30% of the monetary sanctions that the SEC collects in an enforcement action. For example, Exchange Act Regulation S-K Item 101 requires, where material to understanding the issuer's business, disclosure by a reporting segment of "[t]he dollar amount of backlog orders believed to be firm, as of a recent date and as of a comparable date in the preceding fiscal year, together with an indication of the portion thereof not reasonably expected to be filled within the current fiscal year, and seasonal or other material aspects of the backlog." A misleading disclosure about a reporting segment's backlog orders (i.e., future revenue) can violate Regulation S-K and also violate SEC rules that require issuers to maintain adequate internal controls over financial reporting. If the SEC collects more than \$1 million as a result of a whistleblower's tip about such violations, the whistleblower is eligible to receive between 10% to 30% percent of the monetary sanctions collected as a whistleblower reward.

Enforcement Action for Inflated Key Performance Metrics

In 2018, the SEC took an enforcement action against KBR for inflating backlog orders in its public filings, which misled investors about the company's anticipated revenue under the contracts. In particular, the SEC found that KBR included "\$459 million in its publicly disclosed backlog for one of seven contracts it entered into to complete pipe fabrication and modular assembly contracts in Canada, even though KBR had not received — and the counterparty was not obligated to provide — any orders under the contract." KBR's annual report (Form 10-K) defined "backlog" as "the dollar amount of revenue we expect to receive in the future as a result of performing work on contracts awarded. . . All backlog is attributable to firm orders. . . Certain contracts provide maximum dollar limits, with actual authorization to perform work under the contract agreed upon on a periodic basis with the customer. In these arrangements, only the amounts authorized are included in backlog." Including more the amount of actual work authorizations as backlog was misleading to shareholders because it improperly inflated projected revenue.

In addition, the SEC found that KBR made inaccurate estimates of the costs to complete the contracts and that its internal accounting controls were not properly designed to prevent or detect these errors. As noted in the SEC's order, KBR ultimately issued a restatement that disclosed the additional projected costs to complete the projects resulting in charges of \$156 million, consisting of the reversal of \$24 million in previously recognized pre-tax profits, the recognition of approximately \$97 million in pre-tax losses at completion, and a \$35 million reduction in previously recognized revenue. The \$156 million charge represented 91% of KBR's 2013 net

income (as restated). KBR agreed to pay a \$2.5 million penalty to settle the SEC's charges.

SEC Whistleblower Program

Under the SEC Whistleblower Program, the SEC will issue awards to whistleblowers who provide original information about violations of the U.S. federal securities laws that leads to enforcement actions with total monetary sanctions (penalties, disgorgement, and interest) in excess of \$1 million. A whistleblower may receive between 10% to 30% percent of the monetary sanctions collected as a whistleblower reward. The largest SEC whistleblower awards to date are \$50 million and \$33 million.

Since the inception of the SEC Whistleblower Program, it has proved to be an unmitigated success in enabling the SEC to discover fraud and protect investors. The SEC Whistleblower Program has received more than 22,000 tips since 2011, some of which led to enforcement actions resulting in more than \$1.4 billion in financial remedies from wrongdoers. As of March 2018, the SEC Whistleblower Office has paid more than \$266 million in awards to whistleblowers. Over the next few years, we expect the SEC to issue millions of dollars in awards to individuals exposing companies' deceptive financial metrics.

To learn more about the SEC Whistleblower Program, download the eBook *SEC Whistleblower Program: Tips from SEC Whistleblower Attorneys to Maximize an SEC Whistleblower Award*.

SEC Whistleblower Lawyers:

<https://www.youtube.com/watch?v=2PDqnkJJ7N8>

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