



U.S. Securities and Exchange Commission
Office of Inspector General
Office of Audits

Evaluation of the SEC's Whistleblower Program



January 18, 2013
Report No. 511




OFFICE OF
INSPECTOR GENERAL

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

MEMORANDUM

January 18, 2013

TO: Robert S. Khuzami, Director, Division of Enforcement
(Enforcement)

FROM: Jon T. Rymer, Interim Inspector General, Office of Inspector
General (OIG) 

SUBJECT: *Evaluation of the SEC's Whistleblower Program*, Report No. 511

This memorandum transmits the U.S. Securities and Exchange Commission (SEC) OIG's final report detailing the results of our audit of the SEC's whistleblower program. Our audit was conducted pursuant to Section 922 of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

The final report contains two recommendations which if fully implemented should strengthen the SEC's whistleblower program. Enforcement concurred with both recommendations. Your written response to the draft report is included in Appendix VI.

Within the next 45 days please provide OIG with a written corrective action plan (CAP) that addresses each agreed upon recommendation. The CAP should include information such as the name of the designated responsible official or point of contact for the recommendations, estimated timeframes for completing required actions, and milestones identifying how each recommendation will be addressed.

Should you have any questions regarding this report, please do not hesitate to contact me.

We appreciate the courtesy and cooperation that your staff extended to us during this audit.

Attachment

cc: Erica Y. Williams, Deputy Chief of Staff, Office of the Chairman
Luis A. Aguilar, Commissioner
Troy A. Paredes, Commissioner
Daniel M. Gallagher, Commissioner
George S. Canellos, Deputy Director, Division of Enforcement
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Background and Objectives

Background

Section 922 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) amended the Securities Exchange Act of 1934 (Exchange Act) by adding Section 21F, “Securities Whistleblower Incentives and Protection.” Section 21F directs the U.S. Securities and Exchange Commission (SEC or Commission) to make monetary awards to eligible individuals who voluntarily provide original information that leads to successful Commission enforcement actions resulting in the imposition of monetary sanctions over \$1,000,000, and certain related successful actions. The SEC can make awards ranging from 10 to 30 percent of the monetary sanctions collected, which are paid from its Investor Protection Fund (IPF). In addition, Section 924(d) of Dodd-Frank directed the SEC to establish a separate office within the Commission to administer the whistleblower program. In February 2011, the Commission established the Office of the Whistleblower (OWB) to carry out this function.

Section 922 of Dodd-Frank required the Office of Inspector General (OIG) to conduct a review of the whistleblower protections that were established under the amendments made by the section and to submit a report of findings not later than 30 months after Dodd-Frank’s enactment to the:

- Senate Committee on Banking, Housing and Urban Affairs; and
- House Committee on Financial Services.

Dodd-Frank further required that OIG make this report available to the public on our website.

Overview of the SEC’s Whistleblower Program. On May 25, 2011, the Commission adopted final Regulation 21F to implement the provisions of Section 21F of the Exchange Act. Regulation 21F became effective on August 12, 2011.¹ Among other things, Regulation 21F defines terms that are essential to the whistleblower program’s operations, establishes procedures for submitting tips and applying for awards including appeals of Commission determinations whether/or to whom to make an award, describes the criteria the SEC will consider in making award decisions, and implements Dodd-Frank’s prohibition against retaliation for whistleblowing.

OIG met with OWB’s Chief and Deputy Chief to discuss how the office handles whistleblower complaints from the initial submission to an eligible whistleblower receiving a monetary award. Our audit consisted of reviewing OWB’s

¹ Implementation of the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934, Release No. 34-64545.

procedures, decision points, whistleblower personnel practices, and its communications with whistleblowers.

The whistleblower process includes the phases shown below and are discussed in the section that follows.

- (1) Phase 1 - Intake/Triage.
- (2) Phase 2 - Tracking.
- (3) Phase 3 - Claim for an Award.

Phase 1 – Intake/Triage

During Phase 1 of intake and triage, whistleblowers submit a complaint to the SEC. Designated Division of Enforcement (Enforcement) staff review the complaint to determine whether it should be assigned for further investigation or based on their initial review no further action (NFA) is warranted. Whistleblowers can submit a complaint to the SEC through its public website, by mail, or by fax. Online submissions are automatically uploaded into the SEC's Tips, Complaints, and Referrals (TCR) system. Complaints received by mail and fax are manually entered into the TCR system by the TCR intake group.

The Office of Market Intelligence (OMI), located within Enforcement, reviews all TCRs and whistleblower complaints Enforcement receives.² OMI also triages all TCRs received by Enforcement. When OMI determines a complaint warrants further investigation, OMI assigns the complaint to one of the SEC's 11 regional offices, an Enforcement specialized unit, or an Enforcement Associate Director group located in the SEC's Headquarters. Conversely, when it is determined that a complaint does not warrant further investigation or the complaint does not fall into Enforcement's priorities, OMI will designate the complaint as NFA. NFAs get a second review before a final decision is made to close the complaint. In some cases NFAs may be referred to an external government agency or other agency for action.

On occasion the OWB Chief will determine that a whistleblower TCR is sufficiently specific, timely and credible which results in the TCR being expedited through the triage process and assigned to investigative staff by OMI.

Communication with the Whistleblower. OWB sends an acknowledgement or deficiency letter to whistleblowers for all complaints that are received by mail or fax. This letter includes a TCR submission number and if applicable, a discussion of any deficiencies the office identified such as a missing TCR form

² While OMI reviews all TCRs submitted through the public portal and most TCRs submitted internally, some internally-entered TCRs are routed, as appropriate, to the Office of Compliance Inspections and Examinations or the Office of Investor Education and Advocacy directly and not reviewed by OMI.

(which is required), missing signatures, etc.³ The letter further provides guidance to the whistleblower regarding resolving the issue.

OWB also sends whistleblowers an acknowledgement letter when they subsequently submit additional information that is used to supplement their complaint.

Whistleblowers that use the SEC's website to submit a complaint through the TCR system receive a computer generated online confirmation receipt and are provided a TCR submission number.

Additionally, phone calls to the whistleblower hotline are returned within 24 business hours.

Phase 2 – Tracking

During Phase 2, OWB personnel monitor whistleblower submissions that are assigned to investigative staff. Also, during this Phase, OWB—tracks whistleblower cases to document the whistleblower's cooperation and the content and helpfulness of whistleblower information, answers questions, and aids Enforcement staff by providing subject matter expertise regarding the whistleblower program.

Furthermore, OWB documents information needed to process whistleblower awards. The office conducts quarterly conference calls with investigative staff to reconcile items that are tracked, with work that is assigned and resourced, and to discuss the quality of each whistleblower complaint.

A whistleblower complaint results in a successful action against a defendant if the monetary sanctions:

- Exceed \$1 million. The whistleblower may then be eligible for a monetary award if all statutory criteria are met.
- Do not exceed \$1 million the whistleblower is not immediately eligible for a monetary award. However, if the case is aggregated with related SEC actions that arise out of a common body of operative facts and the total monetary sanctions in the related SEC actions collectively exceed \$1 million, then the whistleblower may be eligible for an award.

Communication with the Whistleblower. Enforcement's policy requires its staff neither confirm nor deny that an investigation has been initiated in relation to whistleblower complaints the SEC receives. However, to further OWB's outreach

³ The final rules specify that a whistleblower complaint must be either submitted online through the Commission's website, or the Form TCR must be either mailed or faxed to the SEC Office of the Whistleblower. Form TCR is located in the 17 CFR Section 249.100 final rules.

efforts to whistleblowers, the Commission gave OWB authority to communicate with whistleblowers in limited circumstances. Pursuant to this authority, OWB works closely with Enforcement and OMI staff to engage in discretionary communication with whistleblowers when appropriate, under the following circumstances:

- If NFA is determined, OWB can contact the whistleblower regarding the status of their complaint.
- If a whistleblower complaint has been assigned, OWB can inform the whistleblower their complaint has been reviewed and assigned to Enforcement staff.

Communication in these circumstances is not mandatory and is left to OWB's discretion. Per Enforcement's policy, OWB will not tell the whistleblower whether an investigation has been initiated, based on information the whistleblower has provided to the SEC.

Phase 3 – Claim for an Award

During Phase 3 a whistleblower can claim an award if information he or she provided to OWB leads to, or significantly contributes to a successful SEC action. This action could result in the whistleblower receiving a monetary award if the sanctions ordered are over \$1 million.⁴ OWB posts a Notice of Covered Action on its website for cases that result in monetary sanctions over \$1 million.⁵ Whistleblowers have 90 days to submit a claim for an award using the Form WB-APP (application). OWB's website provides a notice date and a claim due date for each covered whistleblower action.

When OWB or Enforcement staff know that a whistleblower has provided a tip that led or significantly contributed to a successful action, they contact the whistleblower and inform him or her that a Notice of Covered Action has been posted on its website in connection with the tip or information he or she provided. OWB also advises the whistleblower on the process and timeline to apply for the award.

When a claimant submits an application, OWB reviews it to determine if it is procedurally complete and has the information needed to fully process the application. When the application does not have all the required information, OWB works with the whistleblower to ensure he or she successfully completes the application within the 90-day required timeframe by calling and/or sending a

⁴ For the whistleblower program, a Commission action is considered a "covered action" under these circumstances. See Securities and Exchange Act of 1934, Section 21F(a)(1).

⁵ A Notice of Covered Action serves as a public notification that a particular case is potentially eligible for a whistleblower award, and it begins a 90-day deadline for any interested parties to file an application for a whistleblower award.

letter to the whistleblower that identifies deficiencies and advising the whistleblower on processes and deadlines.

OWB staff analyze the claims for awards to assess whether the whistleblower satisfied the eligibility and definitional requirements for an award. When a whistleblower is determined to have satisfied these criteria, OWB then uses four positive and three negative factors to derive a recommended award range between 10 to 30 percent of the dollar amount that was collected in the action.

OWB's process for its analyses includes reviewing and comparing the facts of a claim to the whistleblower statute and regulations, reviewing relevant databases for information regarding the case and subsequent enforcement action, interviewing Enforcement staff regarding the case and the whistleblower's actions, interviewing the whistleblower and/or their counsel, and conducting due diligence and legal research to ensure proper consideration is given to each award claim.

The positive factors considered in recommending an award's percentage include the significance of the whistleblower information, assistance and cooperation from the whistleblower in the investigation and proceedings, any law enforcement interest advanced by a potentially higher award, and whether the whistleblower cooperated with the company's internal compliance system in connection with the matter. The negative factors considered include the whistleblower's culpability, an unreasonable delay in reporting wrongdoing, and the whistleblower's interference with the company's internal compliance system. Though OWB considers both these positive and negative factors, the office has discretion in making award recommendations.

When making an award recommendation OWB submits a recommendation package to Enforcement's Claims Review Staff.⁶ They then meet with the Claims Review Staff. A preliminary determination is prepared and forwarded to the whistleblower. A whistleblower has 30 days to request a copy of the record the Claims Review Staff based its decision on; and/or to request a meeting with OWB staff.

Whistleblowers can file an appeal with OWB within 60 calendar days of the later of:

- (i) The date of the preliminary determination; or
- (ii) The date when OWB made materials available for the whistleblower's review.

⁶ Pursuant to SEC Regulation 21F (the final rules for the whistleblower program) Section 240.21F-10, members of the Claims Review Staff are designated by Enforcement's Director to evaluate all timely whistleblower award claims in accordance with the criteria established in the final rules. Based on this evaluation, the Claims Review Staff will decide on a preliminary determination and consider appeals of their decision if submitted timely. The Claims Review Staff currently has five members, including Enforcement representatives from the home office, regional offices, and a representative from the Office of General Counsel.

When a whistleblower's claim is denied in the preliminary determination phase and the whistleblower fails to submit a timely response, the preliminary determination becomes the SEC's final order. If the whistleblower submits a timely response to appeal the preliminary determination decision, OWB's staff will assess the appeal and make a recommendation to the Claims Review Staff. OWB then meets again with the Claims Review Staff and the Claims Review Staff makes a proposed final determination. OWB then notifies the Commission of the proposed final determination. The Commission has 30 days to review this determination. Any Commissioner can request within 30 days of receiving the proposed final determination notification, that the proposed final determination be reviewed by the Commission. If no Commissioner objects during the 30-day window, the proposed final determination becomes the final order and OWB then provides a copy of the final order to the whistleblower.

After the final order has been issued, if a whistleblower has gotten an award that falls between 10 to 30 percent of the monetary sanctions collected in the action, the process is complete and the amount is not subject to appeal. However, if the whistleblower did not receive an award, or the award percentage is outside the statutory 10 to 30 percent that is collected from an action, the whistleblower may appeal the decision at the Federal Court of Appeals level. The Office of the General Counsel (OGC) handles these appeals for the Commission.

Whistleblower awards are paid out of the IPF that was established in the Dodd-Frank Act. Payments from the IPF are made through the SEC's Office of Financial Management (OFM) and are based on amounts that were collected from each individual case. A single payment can be made to the whistleblower if all monies are collected at the time the final order is issued, or the payment can occur on a rolling basis if the monies are collected over time, after the final order is issued.

Communication with Whistleblowers. To the extent a whistleblower is known to have participated in a covered action, OWB contacts the whistleblower to advise him or her that a Notice of Covered Action was posted on OWB's website and provide guidance on the processes and timeline to apply for an award.

An acknowledgement or deficiency letter is sent to anyone who submits a claim for an award to the SEC. The OWB may discuss with the whistleblower the evidence that was presented when assembling the claims recommendation package for the Claims Review Staff.

Whistleblowers have the right to review the record, to request a meeting with OWB, and/or to appeal a preliminary determination decision. A copy of the preliminary determination, proposed final determination, if applicable, and the final order is sent to the whistleblower.

Objectives

Objectives. Section 922 of the Dodd-Frank Act required OIG to evaluate the SEC's Whistleblower Program and answer the questions described below. OIG will examine whether the:

1. Final rules and regulation issued under the amendments of Section 922 have made the whistleblower protection program (program) clearly defined and user-friendly.
2. Program is promoted on the SEC's website and has been widely publicized.
3. Commission is prompt in:
 - a) responding to information provided by whistleblowers;
 - b) responding to applications for awards filed by whistleblowers;
 - c) updating whistleblowers about the status of their applications; and
 - d) otherwise communicating with the interested parties.
4. Minimum and maximum reward levels are adequate to entice whistleblowers to come forward with information, and whether the reward levels are so high as to encourage illegitimate whistleblower claims.
5. Appeals process has been unduly burdensome for the Commission.
6. Funding mechanism for the Investor Protection Fund established by Section 922 is adequate.
7. In the interest of protecting investors and identifying and preventing fraud, it would be useful for Congress to consider empowering whistleblowers or other individuals, who have already attempted to pursue a case through the Commission, to have a private right of action to bring suit based on the facts of the same case, on behalf of the government and themselves, against persons who have committed securities fraud.
8. The Freedom of Information Act (FOIA) exemption established in Section 21 F(h)(2)(A) of the Securities and Exchange Act of 1934, as added by the Dodd-Frank Act,
 - a) Aids whistleblowers in disclosing information to the Commission.
 - b) What impact the FOIA exemption described above has had on the ability of the public to access information about the regulation and enforcement by the Commission of securities; and
 - c) Any recommendations on whether the exemption described above should remain in effect.

The Inspector General was also given the discretion to review other matters related to the program as appropriate for this audit.

Omission of Sensitive Information. Pursuant to Section 21F(h)(2) of the Exchange Act, we have not included any information in this report that could potentially reveal the identity of a whistleblower.

OIG's Audit and Response to the Dodd-Frank Wall Street Reform and Consumer Protection Act's Questions and Our Recommendations

Question 1: Determine Whether Final Rules and Regulation Issued Under the Amendments of Section 922 Have Made the Whistleblower Protection Program Clearly Defined and User-Friendly

Pursuant to the Dodd-Frank Act, Section 922(d)(1)(A), we assessed whether the final rules and regulations issued under the amendments of Section 922 have made the whistleblower protection program clearly defined and user-friendly.⁷ OIG determined that the implementation of the final rules have made the SEC's whistleblower program clearly defined and user-friendly for users that have basic securities laws, rules, and regulations knowledge.

Final Rules Primary Audience Has Some Knowledge of Securities Laws, Rules, and Regulations

According to the OWB Chief, the final rules were primarily written for potential whistleblowers, compliance officers, corporate counsel, and law firms that are engaged in whistleblower litigation. The final rules generally exclude certain people from receiving awards under the whistleblower program such as directors, corporate officers, compliance officers, and auditors with some exceptions.⁸ The primary demographic for prospective whistleblowers include middle management personnel, controllers, finance department personnel, and other employees who are involved in international transactions.⁹ Prospective whistleblowers may submit tips or complaints related to securities law violations to the SEC. Prospective whistleblowers generally have some securities laws, rules,

⁷ 17 CFR Parts 240 and 249, *Implementation of the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934*.

⁸ 17 CFR 240 Section 21F-4(b)(4) excludes information from several sources as meeting the definition of providing "original information" required in the definition of a whistleblower. Some examples include information obtained under attorney-client privilege, if you obtain information because you were an officer, director, trustee, compliance officer, internal auditor, public accountant in an engagement required by the securities laws, etc. The rules provide for some exceptions whereby the above classes of people may submit original information as a whistleblower.

⁹ Employees involved in international transactions may have knowledge about the Foreign Corrupt Practices Act violations which is a reportable violation under the SEC's whistleblower program.

regulations knowledge and an understanding of the SEC’s role in the financial markets.

The OWB has a hotline telephone number on its website that potential whistleblowers can call to inquire about the SEC’s whistleblower program. OWB’s Chief informed us that most hotline callers did not indicate they did not understand the rules, but instead, wanted reassurance from OWB’s staff regarding the filing process concerning their cases, before filing a formal complaint with the SEC.

OIG reviewed the final rules from the perspective of an individual having basic knowledge of securities laws, rules, and regulations to determine whether they were clearly defined and user-friendly. Clearly defined final rules are specific, straightforward, and unambiguous. User-friendly final rules are easy to learn, use, understand, and navigate. OIG identified attributes of the final rules that make SEC’s whistleblower program “clearly defined” and “user-friendly.” As shown below, Tables 1 and 2 illustrate our review and assessment of the final rules.

Table 1: OIG’s Review and Assessment of Final Rules – Clearly Defined

Clearly Defined Attributes	Text of Final Rules
Defines a whistleblower.	You are a whistleblower if, alone or jointly with others, you provide the Commission with information pursuant to the procedures set forth in Section 240.21F-9(a) of this chapter, and the information relates to a possible violation of the federal securities laws (including any rules or regulations thereunder) that has occurred, is ongoing, or is about to occur. A whistleblower must be an individual. A company or another entity is not eligible to be a whistleblower.
Explains the conditions required to receive an award.	The Commission will pay an award or awards to one or more whistleblowers who: (1) Voluntarily provide the Commission (2) With original information (3) That leads to the successful enforcement by the Commission of a federal court or administrative action (4) In which the Commission obtains monetary sanctions totaling more than \$1,000,000.
Clearly explains the pertinent terms related to receiving an award.	The terms <u>voluntarily</u> , <u>original information</u> , <u>leads to successful enforcement</u> , <u>action</u> , and <u>monetary sanctions</u> are defined in Section 240.21F-4 of this chapter.

Source: 17 CFR Parts 240 and 249

Table 2: OIG’s Review and Assessment of the Final Rules – User-Friendly

User-Friendly Attributes	Text of Final Rules
Outlines procedures for submitting original information.	To be considered a whistleblower . . . , you must submit your information about a possible securities law violation by either of these methods: (1) Online, through the Commission’s website located at www.sec.gov ; or (2) By mailing or faxing a Form TCR (Tip, Complaint or Referral) (referenced in Section 249.1800 of this chapter) to the SEC Office of the Whistleblower, 100 F Street NE, Washington, DC 20549-5631, Fax (703) 813-9322.
Outlines procedures for making a claim for a whistleblower award.	A claimant will have ninety (90) days from the date of the Notice of Covered Action to file a claim for an award based on that action, or the claim will be barred. To file a claim for a whistleblower award, you must file Form WB-APP, <i>Application for Award for Original Information Provided Pursuant to Section 21F of the Securities Exchange Act of 1934</i> (referenced in Section 249.1801 of this chapter). You must sign this form as the claimant and submit it to the Office of the Whistleblower by mail or fax.

Source: 17 CFR Parts 240 and 249

OIG determined that an individual with basic securities laws, rules, and regulations knowledge can easily understand the SEC’s whistleblower program requirements by reading the final rules and information the SEC provides on its website. Further, the procedures for submitting original information (i.e., a whistleblower complaint) or an application for an award are easy to understand and navigate.¹⁰ Finally, OWB’s website, which is discussed in-depth in the next section, enhances the “user-friendliness” of the program by providing a direct link to the final rules and answering commonly asked questions about the program. The OWB hotline is also available to address questions about the SEC’s whistleblower program. Therefore, OIG determined that the final rules as implemented by OWB have made the program clearly defined and user-friendly for individuals having basic securities laws, rules, and regulations knowledge.

¹⁰ The final rules state that the whistleblower must submit “original information” in order to be eligible for a whistleblower award. In order for a whistleblower submission (or complaint) to be considered original information, it must be: (i) derived from the whistleblower’s independent knowledge or analysis; (ii) not already known to the Commission from any other source, unless the whistleblower is the original source of the information; (iii) not exclusively derived from an allegation made in a judicial or administrative hearing, in a governmental report, hearing, audit, or investigation, or from the news media, unless the whistleblower is a source of the information; and (iv) provided to the Commission for the first time after July 21, 2010, *Dodd-Frank Wall Street Reform and Consumer Protection Act* enactment date.

Question 2: Determine Whether the Whistleblower Program is Promoted on the SEC’s Website and has been Widely Publicized

Pursuant to the Dodd-Frank Act, Section 922(d)(1)(B), OIG determined that the whistleblower program is promoted on the SEC’s website, that OWB’s website is readily accessible from the SEC’s website and the program has been widely publicized by a strong internet presence and OWB’s outreach efforts.

The Whistleblower Program on the SEC’s Website and Accessibility to OWB’s Website

OIG tested the ease of accessing whistleblower information on the SEC’s website to determine if this information is prominently displayed and promoted. We determined that information about the whistleblower program is prominently displayed on the SEC’s website and OWB’s website is easily accessible. SEC’s website includes images related to SEC programs that rotate on its website every few seconds. One image consists of a large whistle with the caption “Whistleblower Information” that has a hyperlink to OWB’s website. The SEC’s website also includes a “Submit a Tip or File a Complaint” hyperlink that takes users to a “Questions and Complaints” webpage. This webpage also includes hyperlinks that take the public directly to OWB’s website.

Overall, OWB’s website can be accessed from SEC’s website in several different ways. See Appendix V for detailed information on accessing OWB’s website.

OIG’s review of the SEC’s website activity determined that OWB’s website received 135,906 hits from August 2011 to September 2012. From July 2012 to September 2012, OWB’s website was ranked in the top 100 most viewed SEC uniform resource locators (URL).¹¹

The SEC’s whistleblower program has been promoted on OWB’s website since August 12, 2011, when the whistleblower final rules went into effect.¹² The website includes two videos from OWB’s Chief—a welcome video and a video explaining what happens to a whistleblower’s tip once the SEC receives it. OWB also coordinates with the Office of Investor Education and Advocacy and the Office of Public Affairs and “tweets” to approximately 200,000 followers each time a new group of Notices of Covered Actions is posted to its website. Also, OWB sends email alerts to GovDelivery¹³ when its website is updated.¹⁴

¹¹ In 2012, the website won the Chairman’s Award for Excellence in Information Technology.

¹² See www.sec.gov/whistleblower.

¹³ GovDelivery is a vendor that provides communications services for public sector clients.

¹⁴ Request to close audit recommendation one from OIG’s report “Assessment of the SEC’s Bounty Program,” Report No 474.

OWB Website Presence on Major Internet Search Engines

OIG conducted an internet search using the key word “securities whistleblower” to evaluate the SEC’s whistleblower program’s online presence and found OWB’s website on the first page of our Google, Yahoo, and Bing searches. Further, our use of the key word “whistleblower” found OWB’s website was located on the first page of Google¹⁵ and Yahoo’s¹⁶ internet search engines and on the second page for Bing.¹⁷

Outreach Efforts by the OWB

Internal Training. OWB posted training and guidance on both the Enforcement and the Commission intranet sites regarding whistleblower issues and rules. OWB provided training to various SEC divisions, offices, and internal groups who are likely to be involved in whistleblower matters.

OIG reviewed a list of 40 different presentations that OWB personnel gave to SEC staff and others from May 2011 to November 2012. Eleven of these 40 presentations were used in internal training sessions. Our review of the slides for the Miami Regional Office internal training given on April 30, 2012 included amongst other things, the OWB Chief’s background, office structure, office priorities, program creation, detailed overview of the program, and OWB staff’s contact information.

Public Speaking Appearances. OWB has a written policy regarding its staff accepting public speaking appearances to guard against the SEC appearing to favor the interests of one constituency over another. OWB’s three main constituencies are:

- (1) Whistleblowers (general public);
- (2) Corporate counsel and compliance personnel; and
- (3) Plaintiff’s counsel.

In deciding whether to make a public appearance, OWB’s policy requires a balance of factors such as, the expected size and constituency of the audience, the feasibility of participating remotely via video link or webinar, geography, and whether the group is considered an educational or lobby group.

OIG found that of the 29 external presentations OWB gave from May 2011 to November 2012, four consisted of interviews for publications and 25 were for panels, summits, conferences and other professional events.

¹⁵ See www.google.com.

¹⁶ See www.yahoo.com.

¹⁷ See www.bing.com.

Conclusion

Because of the accessibility of OWB's website from the SEC's website, the program's promotion through various social media methods, prominent presence on major internet search engines, and OWB's internal and external outreach efforts, we determined the SEC's whistleblower program is effectively promoted on its website and is widely publicized.

Question 3: Determine Whether the Commission is Prompt in Responding to Information Provided by Whistleblowers; Responding to Applications for Awards Filed by Whistleblowers; Communicating with Interested Parties

Pursuant to the Dodd-Frank Act, Section 922(d)(1)(C), OIG determined the SEC was generally prompt in responding to information provided by whistleblowers, in responding to applications for whistleblower awards, and communicating with interested parties. However, the program's internal controls need to be strengthened by adding performance metrics.

The SEC, Enforcement, OWB and OMI have written policies and manuals that cover TCR processing which includes whistleblower TCRs, manual triage, whistleblower tracking and other procedures its staff use in processing whistleblower complaints that are submitted to the SEC.¹⁸

Whistleblower TCR Testing Attributes and Results

To determine the Commission's promptness in responding to information that whistleblowers provide, OIG tested a statistical sample of 74 whistleblower TCRs that were submitted to the SEC from April 12, 2011 to September 30, 2012 using the following attributes:¹⁹

- Date TCR was submitted.
- Who submitted the TCR (General public or SEC staff).²⁰
- Date of initial review.

¹⁸ Manual triage is the process by which a TCR is evaluated to: (i) determine whether the information submitted suggests a possible violation of the federal securities laws; (ii) identify the relevant parties; and (iii) gather additional information to assess the credibility and potential risk associated with the TCR. Manual triage also includes making an initial determination as to whether and where the TCR should be assigned for resolution.

¹⁹ See Appendix II for our sampling methodology.

²⁰ SEC staff manually enters TCRs into the TCR system received from whistleblowers in hard copy or facsimile.

- Time elapsed between TCR submission and initial review.
- Date TCR was designated for No Further Action (NFA).
- Time elapsed between initial review and NFA.
- Date TCR was assigned to a point of contact (POC).
- Time elapsed between initial review and assigned to POC.
- Percentage of TCRs that were NFA and active Matters Under Inquiry (MUI)/Investigation.
- Whether active MUIs/Investigations were being tracked in OWB's Case Tracking System.

The SEC, Enforcement, OWB, and OMI further have policies that govern how TCRs will be reviewed and allocated. The SEC's promptness in responding to information whistleblowers provide is primarily determined by how quickly the TCR is processed while in Phase 1 manual triage. Although OMI generally responds promptly to whistleblower's submissions and it has detailed written procedures for manual triage, OIG determined it has not established written timeliness standards for these processes. We found the average time TCR's are in the manual triage process before it is either assigned to a POC or is designated as NFA is acceptable.²¹ Although OWB tracks the progress of whistleblower TCRs in manual triage, OMI owns the process and is responsible for its performance.

Our testing also revealed some general characteristics of the TCR whistleblower population such as:

- The percentage of whistleblower TCRs submitted online by the public;
- The percentage of whistleblower TCRs that were designated as NFA or were assigned to investigative staff; and
- Whether OWB was actively tracking whistleblower cases.

Additionally our testing found that of 74 whistleblower TCR submissions in our sample, 85 percent (63 of 74) were submitted online and 15 percent (11 of 74) were submitted to the SEC in another format such as, through the mail or by fax.²² In the later cases OMI or OWB staff manually entered the complaints into the TCR.

Average Timeline for OMI Staff's Initial Review. The average time it takes OMI staff to initially review a whistleblower TCR once OMI has received it, is less than one day. Moreover, our review of 74 complaints found that 53 percent (39 of 74) of complaints were reviewed the same day the SEC received it; 31 percent (23 of

²¹ Based on their initial review, OMI determines that some complaints require NFA. The complaint is designated NFA and is closed in TCR. Every TCR is reviewed by two OMI attorneys before it is designated NFA.

²² The public may submit tips or complaints directly into TCR through the SEC's public website. The SEC's website has a hyperlink the public can use to submit tips and complaints that leads to the TCR portal.

74) were reviewed in a day; 9 percent (7 of 74) were reviewed in 2 days; and 7 percent (5 of 74) were reviewed in 3 days of being submitted to the SEC.

Average Timeline for Initial NFA Determination. OIG's review of 51 NFA determinations found the average time from when the complaint is initially reviewed by SEC staff, to when a NFA determination was made, was 31 days. Our sample included a NFA determination being made the same day the TCR was submitted to the SEC, to one that was made 249 days after the TCR was submitted to the SEC. Overall, most NFA determinations were made in less than 30 days.

Our testing further found that 63 percent (32 of 51) of NFA determinations were made in less than 30 days. Twenty of the 32 were determined in less than 10 days, while 37 percent (19 of 51) were made in 30 days or more.

POC Assignment Timeline. Whistleblower TCRs are assigned a POC when OMI staff determines the TCR warrants further investigation. Based on OMI's allocation principles, the TCR is forwarded to a regional office, a specialized investigative unit, or a Headquarters Associate Director group in Enforcement. The average length of time from when the complaint is initially reviewed to a POC being assigned by OMI staff was 10 days.

The range of our testing consisted of a review of 38 POC assignments to include those made the same day the SEC received the complaint and assignments that were made 44 days after the SEC received the complaint. Overall, OIG found that 92 percent (35 of 38) of complaints were assigned a POC in less than 30 days after the SEC received it. Further, 25 of the 35 were assigned POCs in less than 10 days. Finally, 8 percent (3 of the 38) were assigned a POC in 30 days or more, after the SEC received the complaint.

NFA and Active MUIs/Investigations in Case Tracking System. OIG's testing of whistleblower TCRs found that 69 percent (51 of 74) of complaints were designated NFA by OMI staff and 31 percent (23 of the 74) were still being actively worked on.²³

OIG further reviewed and tested 18 TCRs that were identified as being related to active MUIs/Investigations and found 94 percent (17 of 18) were in OWB's Case Tracking System.²⁴

²³ Designating a WB-TCR NFA does not necessarily reflect a negative assessment of the quality of information provided. Some TCRs may be designated NFA, if, for example, the tip related to a matter that is currently being investigated, or is more appropriate to be investigated by another regulatory law enforcement agency.

²⁴ OWB's system is used to track the progress of whistleblower cases and it helps ensure OWB attorneys maintain communication with investigative groups working whistleblower cases. The TCR from our sample that was not in the case tracking system is located in HUB, which is Enforcement's tracking system for MUIs and investigations.

Documented Metrics. OIG requested documented metrics to support the number of days a TCR should be in manual triage before it is designated as NFA, or is assigned to a POC. The Acting Chief of OMI informed OIG that the office does not have written policy covering the number of days a TCR should remain in manual triage. She indicated the average length of time in the last year or so, was approximately 4 to 5 business days. However, some timeframes are much longer due to unusual circumstances, such as a TCR requiring independent privilege review prior to being assigned to investigative staff or additional information being needed from the complainant. OMI tracks the age of work items through weekly aging reports. Other than TCRs requiring privilege review, OMI encourages staff to act on work items within 60 days.

Although OMI is generally very responsive to TCRs in the manual triage process, there is no standard to determine whether the response time is prompt or not. Performance metrics are needed to strengthen the internal controls of the manual triage process. This is needed to ensure consistency in the SEC's processes as new personnel are assigned to the office and as turnover occurs. A lack of performance metrics may result in the degradation of performance and pertinent to this review, unnecessarily long response times to whistleblower information.

Whistleblower Application Response

The final rules specify timelines and procedures for whistleblower award applications. When a Notice of Covered Action is posted to OWB's website, whistleblowers have 90 days to submit an application for an award to the SEC using the Form WB-APP (application). When the application is received an OWB attorney logs it into a tracking sheet and then conducts a preliminary review of the application to determine its initial disposition. Each application receives either an acknowledgement or deficiency letter. If all the required information is properly addressed in the application, an acknowledgement letter is issued to the whistleblower applicant. If additional information is needed for the application, a deficiency letter is issued to the whistleblower applicant.

Our review of 10 acknowledgement and deficiency letters found on average, OWB staff sent these letters to whistleblower applicants within 27 days after the whistleblower's application was received. Table 3 shown below, illustrates the results of our review of deficiency letters. When the 122 day outlier is removed from our sample, the average number of days the acknowledgment or deficiency letter is sent to whistleblowers drops to 16.

Table 3: Length of Time OWB Takes to Issue Acknowledgement and Deficiency Letters to Whistleblower Applications

Sample Number	Application Received	Letter Sent	Days Elapsed
1	10/19/11	11/18/11	30
2	2/7/12	6/8/12	122
3	2/24/12	3/6/12	11
4	8/6/12	8/28/12	22
5	2/8/12	2/15/12	7
6	10/28/11	11/18/11	21
7	11/9/11	11/18/11	9
8	2/22/12	2/27/12	5
9	2/2/12	2/27/12	25
10	4/24/12	5/8/12	14
Average Days			27

Source: OWB Whistleblower Application Log and Acknowledgement/Deficiency Letters

In general, OWB is prompt in responding to applications for awards that are filed by whistleblowers. However, this is another area in the whistleblower program that OIG determined had no performance metrics. Although there were no adverse consequences for delayed response time shown in Table 3, sample number 2, there could have been adverse consequences. For example, if the whistleblower’s application was deficient, the deficiency letter would have arrived after the deadline for an award application (e.g., 90 days after the Notice of Covered Action was posted). This would have resulted in the whistleblower being ineligible for an award, unless special consideration was given by SEC.

Updating Whistleblowers About the Status of Their Applications

Below are the ways OWB communicates with whistleblowers after they submit an award application to the SEC:

- An acknowledgement or deficiency letter is sent to all applicants indicating whether the whistleblower’s application is procedurally correct.
- An OWB attorney who conducts a full review of a covered action generally communicates with whistleblowers who have submitted award applications under a covered action.
- A written notification of the Claims Review Staff’s preliminary determination and whistleblower rights in the awards claims process are sent to the applicant.
- There’s an opportunity for the whistleblower to request the record that was used by the Claims Review Staff in making the preliminary determination.
- There’s an opportunity for the whistleblower to request a meeting with OWB to discuss the preliminary determination.

- If a claim is appealed to the Claims Review Staff, (1) a written acknowledgment of receipt of appeal and (2) the results of the appeal (i.e., proposed final determination), will be sent to the whistleblower.
- If the preliminary determination is not appealed to the Claims Review Staff and no award is made, OWB sends a letter enclosing the final order of the Commission to the whistleblower.
- Written notification of a proposed final determination being issued (whether pursuant to an appeal to the Claims Review Staff or by virtue of the preliminary determination becoming a proposed final determination under the statute in the case of an award being recommended).
- Notification of the Commission's final order.

OWB uses different methods to update whistleblowers on the status of their applications. In most cases this communication is event-driven, (e.g., after a preliminary determination has been issued by the Claims Review Staff), rather than timeline driven. Our review determined that OWB's communication with whistleblowers who submit award applications is effective and appropriate.

Communications with the Interested Parties

OWB's communication with interested parties (the whistleblower and/or counsel for the whistleblower) is detailed in earlier sections of this report and was shown to be generally prompt. However, the whistleblower hotline voicemail offers another means whereby interested parties can communicate with OWB. OWB's written policies specify that all voicemails received on its public telephone line are to be returned within 24 business hours and at least two OWB staff should be on the call.

We selected a sample of all calls that were received from various dates and tested them against OWB's phone policy. Our testing included whether: (1) calls were returned within 24 business hours, and (2) calls were made with less than two OWB staff on the call. OWB's callback hotline performance is shown in Table 4.

Table 4: OWB's Telephone Callback Hotline Performance

Date	Number of Calls	Less than 2 Staff on Call	Calls Not Returned within 24 hours
9/19/11	14	0	0
10/19/11	15	0	1
11/8/11	13	0	0
12/12/11	13	0	1
2/16/12	11	0	0
4/11/12	7	0	0
6/5/12	15	0	3
8/29/12	16	0	0
9/11/12	22	0	0
Total	126	0	5

Source: OWB Phone Call Log

As illustrated in Table 4, OWB complied with its policy to have two staff on hotline call backs 100 percent of the time. Four percent (5 of 126) of OWB hotline calls were not returned with 24 business hours. Therefore, 96 percent of the time OWB complied with its call-back policy. For the 5 exceptions found in our sample, call backs were made within 48 hours after the calls were received. It should be noted that for some calls in OWB's log such as hang ups, unintelligible messages, no call back number, and frequent/abusive callers—OWB did not return the call.

Based on our review of OWB's response to information provided by whistleblowers, their communication with whistleblowers and their prompt response to calls made on OWB's hotline, we determined OWB promptly communicated whistleblower information to interested parties in whistleblower cases.

Internal Controls for the Whistleblower Program

The Office of Management and Budget (OMB) Circular A-123, *Management's Responsibility for Internal Control*, requires management to establish and maintain internal control to achieve the objectives of effective and efficient operations, reliable financial reporting, and compliance with applicable laws and regulations. Monitoring the effectiveness of internal control should occur in the normal course of business. In addition, periodic reviews, reconciliations or comparisons of data should be included as part of the duties of regular assigned personnel. We determined that adding metrics for certain key performance areas of the whistleblower program will assist OWB in monitoring program performance and making corrections as necessary.

In two particular areas OIG found that OWB and OMI have not established any performance metrics. First, with respect to OMI, there is no standard on how long a TCR should remain in manual triage. Our sample testing indicated the

average time a TCR is designated as NFA in the manual triage process is 31 days. This included a TCR designated as NFA on the same day it was received, as well as a TCR that was designated as NFA 249 days after it was submitted to the SEC. On average TCRs assigned to a POC were in manual triage for 10 days. These timelines may be appropriate; however there is no standard by which performance can be measured. Thoughtfully chosen performance metrics will strengthen the whistleblower program's internal controls and ensure consistency in its processes and procedures as new personnel are assigned to OMI and turnover occurs. A lack of performance metrics may result in the degradation in performance and unnecessary long response times to whistleblower information.

OWB did not have a performance metric for the maximum length of time staff should respond to applications for awards filed by whistleblowers. Our audit found OWB sent an acknowledgement letter to a whistleblower applicant 122 days after the application was submitted. Though there were no adverse consequences for this delayed response, there could have been consequences. For example, if the whistleblower application was deficient, the deficiency letter would have arrived after the award application deadline, which is 90 days after a Notice of Covered Action is posted. This would have resulted in the whistleblower being ineligible for an award, unless special consideration was given by the SEC.

Conclusion

OWB has developed an internal control plan that identifies several quantitative and qualitative key performance measures. An example of the quantitative performance measure is "average length of time to respond to applications of awards filed by whistleblowers." OWB and OMI should take this measure one step further and use the data collected on key performance measures to establish meaningful performance metrics that will enable the office to objectively measure the whistleblower program's performance. For example, OWB could establish a policy that the office will send either an acknowledgement or deficiency letter to a whistleblower within 30 days after receiving the whistleblower's award application. OMI could also establish a policy that TCRs should remain in manual triage no longer than 30 days unless a justification is provided to the OMI Chief. These examples are not intended to be prescriptive; however, they are the types of metrics OWB and OMI should establish.

Recommendation 1:

The Division of Enforcement should ensure that the Office of Market Intelligence (OMI) assesses the manual triage process and establishes key performance metrics that can be used to measure process performance. These performance metrics should be documented in OMI's written policies and procedures.

Management Comments. Enforcement concurred with this recommendation. See Appendix VI for management's full comments.

OIG Analysis. We are pleased Enforcement concurred with this recommendation.

Recommendation 2:

The Division of Enforcement should ensure that the Office of the Whistleblower (OWB) assesses the key performance measures that are contained in their internal control plan and develop performance metrics where appropriate. These performance metrics should be added to OWB's internal control plan.

Management Comments. Enforcement concurred with this recommendation. See Appendix VI for management's full comments.

OIG Analysis. We are pleased Enforcement concurred with this recommendation.

Question 4: Determine Whether Minimum and Maximum Award Levels are Adequate

Pursuant to the Dodd-Frank Act, Section 922(d)(1)(D), our assessment of whether the minimum and maximum reward levels are adequate to entice whistleblowers to come forward with information and the reward levels are high enough to encourage illegitimate whistleblower claims found the SEC's whistleblower award levels are comparable to other federal government agencies with the maximum award level being 30 percent in all the programs we reviewed. Based on the past experience of other whistleblower programs and practical concerns in the administration of the SEC's program, we determined the SEC's whistleblower minimum and maximum award levels are reasonable.

Review of Academic Literature on Minimum and Maximum Award Levels for Whistleblower Programs

Dodd-Frank Act allows qualifying whistleblowers to receive 10 to 30 percent of collected sanctions from successful lawsuits that are brought by the Commission, based on original information the whistleblower provided to the SEC. Since whistleblower award amounts were not a debated part of the Dodd-Frank Act, it appears the award levels may be based on the percentages used by other federal government agencies with whistleblower programs. Additionally, few empirical studies have been done on how monetary award levels influence whistleblowing behavior. The two most detailed studies we reviewed concluded

high rewards can motivate potential whistleblowers to come forward because the monetary amount may mitigate the cost of professional and social sanctions that can result.

OWB Staff's Views

The OWB Chief informed OIG that it is important to have an award floor to incentivize whistleblowers to come forward. A guaranteed award amount mitigates the risk to whistleblowers' employment prospects or reputation. Although he believes there's no theoretical need for a ceiling on awards, OWB's Chief feels it is useful for the office, for practical purposes to limit awards to 30 percent. Since OWB recommends the amount of each award based on merits without relation to other awards that are granted, this process is made simpler when limited to a clearly stated award range. The Chief further told OIG that the SEC's current 10 to 30 percent range appears to be appropriate.

Views of Other Federal Government Agencies' Whistleblower Programs

We solicited views from other federal government agencies with whistleblower programs on the minimum and maximum award levels that are established in their programs. Respondents typically indicated they did not have an opinion on award levels since the award levels were statutorily mandated. Further, respondents were not particularly concerned that award levels could induce illegitimate claims since they were confident their review process would weed out illegitimate claims through independent corroboration of asserted facts. One respondent suggested that a hard cap on whistleblower awards may be appropriate in cases where the recovery is substantial. However, the respondent also believed that whistleblower attorneys and advocacy groups would strongly oppose such caps.

Comparison of Whistleblower Award Levels

As shown below, Table 5 compares the SEC's whistleblower award levels to the award levels that are established at the U.S. Commodity Futures Trading Commission (CFTC), U.S. Internal Revenue Service (IRS), and Department of Justice (DOJ).

Table 5: Comparison of Award Levels for Federal Whistleblower Programs

Government Agency	Minimum Award Collected	Maximum Award Collected
SEC	10%	30%
CFTC	10%	30%
IRS	15%	30%
DOJ (Government)*	15%	30%
DOJ (Non-government)*	25%	30%

Source: OIG Questionnaire

* DOJ's False Claim Act has two scenarios under which an individual may collect an award when the government: (1) intervenes; and (2) does not intervene.

Whistleblower award levels are comparable across federal government whistleblower programs. As shown in Table 5, the maximum whistleblower award level is 30 percent for each agency we identified. Based on the past experience of other whistleblower programs and practical concerns in administering the SEC's program, we concluded the SEC's minimum and maximum award levels are consistent with other federal agencies and appear to be reasonable.

Conclusion

We determined the SEC's minimum and maximum award levels are reasonable. Since there are few empirical studies on whistleblower award levels, to obtain cross-cutting results it may be beneficial if the Government Accountability Office would conduct a long-term, government-wide study on how whistleblower motivations are affected by award levels.

Question 5: Determine Whether Appeals Process has been Unduly Burdensome for the Commission

Pursuant to the Dodd-Frank Act, Section 922(d)(1)(E), OIG's assessment of whether the appeals process has been unduly burdensome on the Commission found that, currently no whistleblower appeals have been filed with the Federal Court of Appeals. However, one whistleblower has appealed a preliminary determination that the Claims Review Staff made.²⁵ Based on our analysis of the appeals process we do not believe it has been unduly burdensome on the Commission.

²⁵ The date of the whistleblower appeal was November 6, 2012.

Rights of Appeal in SEC's Whistleblower Program

Section 21F of the Exchange Act provides the whistleblower with the opportunity to appeal SEC whistleblower final orders within 30 days after the order is issued to the Federal Court of Appeals under the following conditions:

- If the whistleblower has received an award that falls between 10 to 30 percent of the monetary sanctions collected in the action, the process is complete and the amount is not subject to appeal.
- If the whistleblower was found to be ineligible for an award, or the award amount is outside of the statutory 10 to 30 percentage that is established for monetary sanctions, the whistleblower may appeal the decision at the Federal Court Of Appeals level.²⁶

The final rules also give the whistleblower a right to appeal a preliminary determination made by the Claims Review Staff.

- Once the Claims Review Staff has issued a preliminary determination, the whistleblower has 30 days to request a copy of the record the Claims Review Staff used to make their decision and/or request a meeting with OWB staff to discuss their case.
- The claimant may file an appeal within 60 calendar days of the later of (i) the date of the preliminary determination, or (ii) the date when OWB made materials available for review.

Status of Appeals

To date no actual appeals of the Commission's final order in a whistleblower case have been filed with the Federal Court of Appeals. Four whistleblowers (includes two that submitted multiple applications for awards) have requested a copy of the record that the Claims Review Staff used in making preliminary determinations in their particular cases. One whistleblower sent an email to the OWB staff declaring their intention to appeal the preliminary determination. The OWB staff anticipates that the four whistleblowers who requested copies of the records will also appeal their preliminary determinations. To date, one appeal to the Claims Review Staff has been submitted to OWB.

Appeals Process

When a whistleblower requests a copy of the record that the Claims Review Staff made a preliminary determination on, the OWB staff must review the record to

²⁶ OGC handles the appeal for the Commission.

ensure sensitive information is not released and OWB redacts the record as appropriate. OWB staff coordinates with the whistleblower and has them sign a non-disclosure agreement before the record is released to them. In the event that an appeal of the SEC's final order is filed in the Federal Court of Appeals, OWB would need to collect pertinent records to assist OGC with the litigation. These efforts by the Commission are reasonable and are generally expected in a regulatory agency.

Conclusion

OIG determined that potential whistleblower appeals have not been unduly burdensome on the Commission.

Question 6: Determine Whether the Funding Mechanism for the Investor Protection Fund is Adequate

Pursuant to the Dodd-Frank Act, Section 922(d)(1)(F), OIG determined that the funding mechanism for the IPF, which was established by Section 922, is adequate. The IPF was established at a funding level that has not required replenishment in over two years. If the IPF balance drops below \$300 million, Enforcement and OFM will replenish it by identifying qualifying receipts for deposit. Currently, the fund is earning interest through short-term investments with the Bureau of Public Debt.

Establishment of the Fund

The IPF was established in the fourth quarter of fiscal year 2010 to be available to the Commission, without further appropriation or fiscal year limitation for paying awards to whistleblowers and funding the work activities of OIG's employee suggestion program. The SEC is required to annually request and obtain apportionments from OMB to use these funds. OFM has developed policies and procedures for IPF that include a description of the whistleblower awards process, financial reporting requirements, budget request procedures, and procedures for replenishing the IPF.

The IPF was first established in August 2010 with approximately \$452 million of non-exchange revenue that was transferred to the fund from the SEC's disgorgement and penalties deposit fund. In the SEC's fiscal year 2013 apportionment, nearly \$452 million was still available in IPF. Since its establishment the IPF's balance has not fallen below \$300 million and no additional qualifying collections have been deposited into it.

Ongoing Funding Mechanism

The IPF can be replenished in the following ways:

- If the balance falls below \$300 million, qualified collections identified by Enforcement and OFM's Treasury Operations Branch can be used to replenish the fund.²⁷
- The SEC has authority to invest amounts in the IPF in overnight and short-term market-based Treasury bills through the Bureau of the Public Debt. The interest earned on the investments is a component of the balance of the IPF and is available to be used for the fund's expenses.

Use of the Investor Protection Fund

In 2012, the IPF was used to pay one whistleblower award which amounted to approximately \$46,000. As previously mentioned, the fund is also used to pay for OIG's employee suggestion program activities which amounted to \$112,000 in fiscal year 2011 and \$70,000 in fiscal year 2012.²⁸ Even though some expenditures were paid from the fund, its balance has not substantially changed since the fund was established.

Conclusion

OIG determined that the funding mechanism for the IPF established by Section 922 of the Dodd-Frank Act is adequate for three reasons. First, the IPF was initially established at a funding level that has not required replenishment since its inception. Secondly, if the IPF balance ever drops below \$300 million Enforcement and OFM can replenish the fund by identifying qualifying receipts for deposit. Finally, interest earned on the IPF through short-term investments with the Bureau of Public Debt amounted to an additional contribution of \$990,000 into the fund in fiscal year 2011, and \$757,000 in fiscal year 2012. These contributions exceeded the total expenditures for both years.

²⁷ Exchange Act Section 21F(g)(3).

²⁸ Exchange Act Section 21F(g)(2)(B).

Question 7: Determine Whether a Private Right of Action Should be Added to SEC’s Whistleblower Program

Pursuant to the Dodd-Frank Act, Section 922(d)(1)(G), OIG’s assessment of whether, in the interest of protecting investors and identifying and preventing fraud it would be useful for Congress to consider empowering whistleblowers or other individuals, who have already attempted to pursue a case through the Commission, to have a private right of action to bring suit based on the facts of the same case on behalf of the government and themselves, against persons who have committed securities fraud—found that it is premature to introduce a private right of action into the SEC’s whistleblower program at this time, since the program is still relatively new and has only been in place since August 2011.²⁹ Any fundamental changes in approach would disrupt the system that is currently in place. Upon collecting additional data and assessing the effectiveness of the program after a reasonable amount of time, the OIG will be in a better position to opine on the usefulness of adding a private right of action to the SEC’s whistleblower program.

Review of Academic Literature on Private Rights of Action for Whistleblower Programs

Since this provision of Dodd-Frank contemplates the possibility of a qui tam-type action for securities violations, our review of academic literature focused on the private rights of action under Rule 10b-5 of the securities regulation and the False Claims Act (FCA) qui tam provision.³⁰

An overview of Rule 10b-5 offers insight into the issues that arise in the context of private enforcement of securities laws and the qui tam provision of FCA, which provides a procedural standard comparison to the right of action contemplated in Dodd-Frank. Critics of private rights of action argue the private enforcement of broad regulations is likely to result in wasteful deterrence. Public entities may adjust enforcement levels, as well as the types of sanctions that are imposed on corporations in response to market realities, but private actors bring suit for the sole purpose of seeking monetary damages. Since qui tam actions could attract unscrupulous bounty hunters, a regulatory regime that relies on private enforcement may result in undesirable outcomes such as frivolous litigation,

²⁹ In the context of SEC’s whistleblower program a private right of action would allow an individual to sue a company or individual that violated the federal securities laws on behalf of themselves and the SEC.

³⁰ The text of Dodd-Frank asks OIG to study whether it would be useful “for Congress to consider empowering whistleblowers or other individuals, who have already attempted to pursue the case through the Commission, to have a private right of action to bring suit based on the facts of the same case, on behalf of the government and themselves,” which suggests a qui tam right of action. Dodd-Frank Wall Street Reform and Consumer Protection Act Section 922(d)(1)(G), 124 Stat. 1376, 1849 (2010). For comparison to the language of the qui tam provision of the False Claims Act, see 31 U.S.C. Section 3730(b)-(c) (2010).

collusion between plaintiffs and defendants, and delays in bringing a suit for the purpose of increasing the bounty award amount.

Some studies we reviewed concluded the best way to ensure that private enforcers' interests are aligned with taxpayers' is to permit a public regulator to oversee the proposed lawsuits. A public enforcer can allow legitimate claims to go through, but deny harmful, profit-seeking ones from reaching the judicial system. This gatekeeping mechanism would reduce the risk of the system being abused. Therefore, if Congress grants a private right of action to individuals who want to sue for securities fraud on behalf of the government and themselves, the studies suggest it is important to include the condition that a public enforcer has the authority to oversee such litigation and to exercise veto power over opportunistic lawsuits.

Views of the OWB Chief

OWB's Chief informed OIG it is premature to consider the benefits of significantly restructuring the SEC's approach to a whistleblower award program and sufficient time has not passed to assess the effectiveness of the current program which has only been in-place since August 12, 2011. The OWB Chief is particularly concerned that the system currently in place would be disrupted if a private right of action were added to the enforcement mechanisms. Additionally, he anticipated adjustments to the OWB program that may address some of the same issues a private right of action could remedy. He suggested data should be gathered on the program's effectiveness before considering a dramatic enforcement measure such as adding a private right of action to the existing laws.

Views of Other Whistleblower Programs

OIG solicited the views of other federal government agencies with whistleblower programs on the use of a private right of action in their programs. In general the respondents' views were against a private right of action. Two respondents suggested private rights of action tend to weaken the government's ability to shape and develop the law and may lead to wasteful, detrimental developments, such as pursuing a position that is inconsistent with executive and judicial interpretations. Another respondent suggested a private right of action for whistleblowers in the securities industry could lead to moral hazard. For example, an uninjured plaintiff, who would not have a standing without the whistleblower statute, could short a company's stock and then sue the company for an alleged violation of the securities laws in the hopes the suit would harm the stock price. On the positive side, one respondent said that a private right of action may be helpful when a government agency's resources are constrained. However, this may mean that private individuals pursue a case that the government does not think should be pursued and would not have spent resources on anyway.

Conclusion

Our research determined that a private right of action to bring a suit based on the facts of a whistleblower complaint that previously was considered by the SEC, may be useful in furthering the interest of protecting investors and preventing fraud in some cases. However, the unintended consequences of such a legislative move is generally undesirable. It is premature to consider the benefits of significantly restructuring the SEC's approach to the whistleblower award program. Sufficient time has is needed to assess the effectiveness of the current program. Fundamental changes in the current approach would disrupt the system that is currently in place. Upon collecting additional data and assessing the effectiveness of the program in another two or three years, OIG will be in a better position to opine on the usefulness of adding a private right of action to the SEC's whistleblower program.

Question 8: Determine Whether the FOIA Exemption Added by Dodd-Frank Aids Whistleblowers in Disclosing Information to SEC; What Impact it has had on the Ability of the Public to Access Commission Information; Should be Retained

Pursuant to the Dodd-Frank Act, Section 922(d)(1)(H), OIG further assessed:

- (a) Whether the Freedom of Information Act (FOIA) exemption established in Section 21 F(h)(2)(A) of the Securities and Exchange Act of 1934, as added by the Dodd-Frank Act, aids whistleblowers in disclosing information to the Commission;
- (b) What impact the FOIA exemption described above has had on the ability of the public to access information about the regulation and enforcement by the Commission of securities; and
- (c) Any recommendations on whether the exemption described above should remain in effect.

OIG determined that the FOIA exemption added by Dodd-Frank aids whistleblowers in disclosing information to the Commission by serving as an additional safeguard for whistleblower confidentiality. Further, this exemption essentially had no impact on the public's ability to access information about the Commission's regulation and enforcement of securities. Therefore, we determined the exemption should be retained.

FOIA Exemption (b)(3) Added Into the Dodd-Frank Act

There are nine FOIA exemptions the Commission and other federal agencies can use to deny the release of certain information the public may request. Exemption 3, 5 U.S.C. Section 552(b)(3)(B) or (b)(3) pertains to information that is prohibited from disclosure by another federal law.

The Dodd-Frank Act which became effective in July 2010, included FOIA exemption (b)(3), which provides an additional safeguard to whistleblower's confidentiality and aids whistleblowers in disclosing information to the Commission. FOIA exemption (b)(3) states the following:

Except as provided in subparagraphs (B) and (C), the Commission and any officer or employee of the Commission shall not disclose any information, including information provided by a whistleblower to the Commission, which could reasonably be expected to reveal the identity of a whistleblower, except in accordance with the provisions of section 552a of title 5, unless and until required to be disclosed to a defendant or respondent in connection with a public proceeding instituted by the Commission or any entity described in subparagraph (C). For purposes of section 552 of title 5, this paragraph shall be considered a statute described in subsection (b)(3)(B) of such section.

Information that is withheld on the basis of the new FOIA exemption has always been withheld by the SEC's FOIA office, based on other similar exemptions, in addition to exemption (b)(3), which indicates that whistleblower confidentiality was addressed under FOIA's pre-existing exemptions.³¹ We discussed the use of FOIA exemption (b)(3) with the SEC's FOIA Officer and determined the following:

- Whistleblower records are housed in the TCR system, and whistleblower records can be identified in TCR. The FOIA office will determine whether a FOIA request is related to a whistleblower based on whether or not the records requested are flagged as such.
- Under this exemption the FOIA office has no discretion regarding the release of "information provided by a whistleblower to the Commission, which could reasonably be expected to reveal the identity of a whistleblower." Under other exemptions the FOIA office has discretion in weighing the privacy interest of the individual against the public's right to know the information. Therefore, the new exemption allows the FOIA office to withhold

³¹ Examples of the other FOIA exemptions that have caused SEC to withhold a whistleblower's identity include: (i) Exemption 6 – information involving matters of personal privacy; and (ii) Exemption 7 – records or information compiled for law enforcement purposes . . . among others.

more information than would be withheld based on other similar exemptions. However, in practice this has never been the case.

The SEC's FOIA Officer informed us the FOIA office has always withheld information based on FOIA exemption (b)(3), as well as other similar exemptions.

Frequency that FOIA Exemption (b)(3) is Used at SEC

OIG reviewed the FOIA office's statistics for fiscal years 2010 to 2012, regarding the frequency and use of FOIA exemption (b)(3). Our review found the exemption was not the sole reason for denying information request. Further, we determined the Dodd-Frank exemption has not impacted the public's ability to access information about the SEC's regulation and enforcement of securities, since information requested would have been withheld anyway under another FOIA exemption. We determined the exemption provides additional assurance to the whistleblower that their identity will be protected. The OWB Deputy Chief told OIG the exemption was a vital feature of the whistleblower program because it gives whistleblowers an additional level of comfort. OIG's overall results of our review of the SEC's FOIA exemption (b)(3) denials for fiscal years 2010 to 2012 are found below in Table 6.

Table 6: SEC's FOIA Exemption (b)(3) Denials During Fiscal Years 2010 to 2012

Fiscal Years 2010 to 2012 Denials	Number
Number of FOIA requests processed	33,315
Number of times exemption (b)(3) used	26
Number of times exemption (b)(3) added by Dodd-Frank used	7
Number of times request denied on the basis of exemption (b)(3) added by Dodd-Frank in conjunction with other exemptions	7
Number of times request denied solely on the basis of exemption (b)(3) added by the Dodd-Frank Act	0

Source: SEC's FY 2010 – 2012 Annual FOIA Report

Conclusion

Although FOIA Exemption (b)(3) established in Dodd-Frank allows the FOIA office to withhold more information than would have been withheld under other exemptions, in practice this has not been the case. Therefore, the public's ability to access information about the SEC's regulation and enforcement of securities remains essentially unchanged by this new exemption. OIG determined that whistleblowers gained additional confidentiality safeguards and the Dodd-Frank FOIA exemption should remain in effect.

Abbreviations

CFTC	U.S. Commodity Futures Trading Commission
COSO	Committee of Sponsoring Organizations of the Treadway Commission
DOJ	Department of Justice
Enforcement	Division of Enforcement
Exchange Act	Securities Exchange Act of 1934
Dodd-Frank	Dodd-Frank Wall Street Reform and Consumer Protection Act
FCA	False Claims Act
FOIA	Freedom of Information Act
IPF	Investor Protection Fund
IRS	U.S. Internal Revenue Service
MUI	Matters under inquiry
NFA	No Further Action
OFM	Office of Financial Management
OGC	Office of General Counsel
OMB	Office of Management and Budget
OIG	Office of Inspector General
OMI	Office of Market Intelligence
OWB	Office of the Whistleblower
POC	Point of Contact
TCR	Tips, Complaints, and Referrals
SEC or Commission	U.S. Securities and Exchange Commission

Scope and Methodology

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Scope. Our audit focused on the SEC's policy and procedures for processing whistleblower complaints. As required by Dodd-Frank Section 922, we also reviewed the operations of OFM and the FOIA office related to the whistleblower program. Additionally, we tested whistleblower TCRs submitted to the SEC from August 12, 2011 to September 30, 2012.

Methodology. To meet the objective of determining whether the whistleblower final rules made the whistleblower program clearly defined and user-friendly, we defined and examined "clearly defined" and "user-friendly" attributes and reviewed the final rules to determine how these attributes were presented in the text of the final rules. Further, we reviewed and tested the SEC's website pertaining to the whistleblowers program to determine if it was user-friendly.

To meet the objective of determining whether the whistleblower program is promoted on the SEC's website and has been widely publicized, we tested the accessibility of OWB's website from the SEC's public homepage, reviewed webpage statistics, and assessed the public's accessibility on major internet search engines to the SEC's whistleblower program and whistleblower information. Finally, we reviewed OWB's use of social media sources and its internal and external outreach efforts to promote the whistleblower program.

To meet the objective of determining the SEC's promptness in responding to whistleblower information, award applications, and general requests for information, we walked through the whistleblower process with OWB and reviewed Enforcement, OWB, and OMI policies and procedures on the whistleblower program and TCR. We also tested a statistical sample of whistleblower TCRs using different attributes related to processing timeliness. Finally, we tested OWB's promptness in responding to award applications and OWB's hotline telephone calls.

To meet the objectives of determining whether the whistleblower minimum and maximum award levels were adequate and whether the SEC's whistleblower program should include a private right of action, we reviewed academic literature on both topics and solicited opinions from OWB and other federal government

agencies with whistleblower programs. We also compared key features of SEC's whistleblower program with these agency's whistleblower programs.

To determine whether the appeals process was unduly burdensome for the Commission we reviewed potential appeals submitted to the SEC and reviewed the appeal processes and procedures.

To determine whether the funding mechanism for the IPF is adequate, we reviewed OFM's IPF policies and procedures, the IPF financial statements, and budget documents. Additionally, we reviewed the history of the IPF to include its establishment, expenditures, and investing activities. Finally, we reviewed the procedures established for replenishing the fund.

Finally, to determine whether the FOIA exemption added by Dodd-Frank aids whistleblowers in disclosing information to the Commission, its impact on the ability of the public to access SEC information, and whether the exemption should be retained, we reviewed the SEC's annual FOIA report for fiscal years 2010 to 2012, interviewed SEC's FOIA Officer, and reviewed the history of SEC's use of the new exemption.

Internal Controls. The Internal Control—Integrated Framework, published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) provides a framework for organizations to design, implement, and evaluate controls that facilitate compliance with federal laws, regulations, and program compliance requirements.³² For our audit, we based our assessment of OWB's internal controls significant to our objectives on the COSO framework as follows: control environment, risk assessment, control activities, information and communication, and monitoring. Among the internal controls we assessed were the Commission and Enforcement's controls related to processing TCRs, the annual risk assessment for the Federal Manager's Financial Integrity Act assurance statement, OWB's policies, procedures, OWB's internal controls plan, and OWB's controls over external communications of the whistleblower program.³³

Use of Computer-Processed Data. We used the SEC's TCR system to generate the universe of whistleblower TCRs that were submitted to the SEC from August 12, 2011 to September 30, 2012. We also used the TCR system to retrieve key documents for our whistleblower TCR testing.

Statistical Sampling. To review the SEC's promptness in responding to whistleblower information OWB used the TCR system to generate whistleblower TCR's that were submitted to the SEC from August 12, 2011 through September 30, 2012. Our audit universe consisted of 3,335 whistleblower TCRs.

³² Committee of the Sponsoring Organizations of the Treadway Commission, *Internal Control – Integrated Framework* (1992).

³³ Federal Manager's Financial Integrity Act of 1982.

We used the EZ Quant Statistical Analysis Audit Software to generate a statistical sample of 74 whistleblower TCRs.³⁴ Our sample was designed to project rates of occurrence (e.g., percentage of whistleblower TCRs that were submitted by the public) with 90% confidence and the point estimation was within $\pm 5\%$ of the universe of TCRs under consideration.

Prior Coverage. The OIG conducted an audit of SEC's now defunct bounty program and issued *Assessment of the SEC's Bounty Program*, Report No. 474 on March 29, 2010. The objectives of this audit were to:

- (1) Assess whether necessary management controls have been established and operate effectively to ensure bounty applications are routed to appropriate personnel and are properly processed and tracked; and
- (2) Determine whether other government agencies with similar programs have best practices that could be incorporated into the SEC bounty program.

The report found that although the SEC had a bounty program in-place for more than 20 years that rewarded whistleblowers for insider trading tips and complaints, there were very few payments made under the program. The report further found the Commission received few applications from individuals seeking bounties over this 20-year period and the program was not widely recognized inside or outside the Commission. Finally, the report determined the bounty program was not fundamentally designed to be successful.

³⁴ EZ Quant is statistical analysis software provided by the Defense Contract Audit Agency at their public website. It is freeware and its use and copying is unrestricted. EZ Quant has the capability to perform both attribute and variable sample selection and evaluation.

Criteria

Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Section 922. Section 922 outlines the statutory requirements for SEC's whistleblower program and required OIG to conduct an evaluation of the SEC's whistleblower program.

Securities and Exchange Act of 1934, Section 21F. This is an amendment in Dodd-Frank that covers the SEC's whistleblower program.

17 CFR Parts 240 and 249, Implementation of the Whistleblower Provisions of Section 21F of the Securities and Exchange Act of 1934. The final rules provide key definitions, determine who is eligible for a whistleblower award, and outline the procedures for submitting whistleblower complaints and applications for awards.

Enforcement Manual. This is Enforcement's internal manual and it serves as a reference guide its staff uses to aid with investigating potential violations of federal securities laws. The manual also includes general guidance on the SEC's whistleblower program.

SEC, Enforcement and OWB Policy on Handling TCRs. Internal SEC policy and procedures on handling tips, complaints, and referrals.

OWB Policies and Procedures. This includes OWB's policy and procedures on the SEC whistleblower program's operations, guidance on tracking and documenting whistleblower claims, procedures for notifying whistleblowers on the status on their complaints, OWB's hotline telephone call protocol, etc.

OMI Triage Manual and Allocation Principles. OMI's internal policy and procedures covering the review, disposition and allocation of TCRs the SEC receives.

OFM Policies and Procedures on the Investor Protection Fund. OFM's internal policy and procedures covering IPF, to include financial reporting requirements, budget submissions, and replenishing the IPF.

5 USC Section 552, Freedom of Information Act. FOIA requires federal agencies to make certain agency materials available for public inspection and copying. FOIA also provides for exemptions to this requirement.

OMB Circular A-123, Management's Responsibility for Internal Control. Establishes that management has a fundamental responsibility to develop and maintain effective internal controls.

List of Recommendations

Recommendation 1:

The Division of Enforcement should ensure that the Office of Market Intelligence (OMI) assesses the manual triage process and establishes key performance metrics that can be used to measure process performance. These performance metrics should be documented in OMI's written policies and procedures.

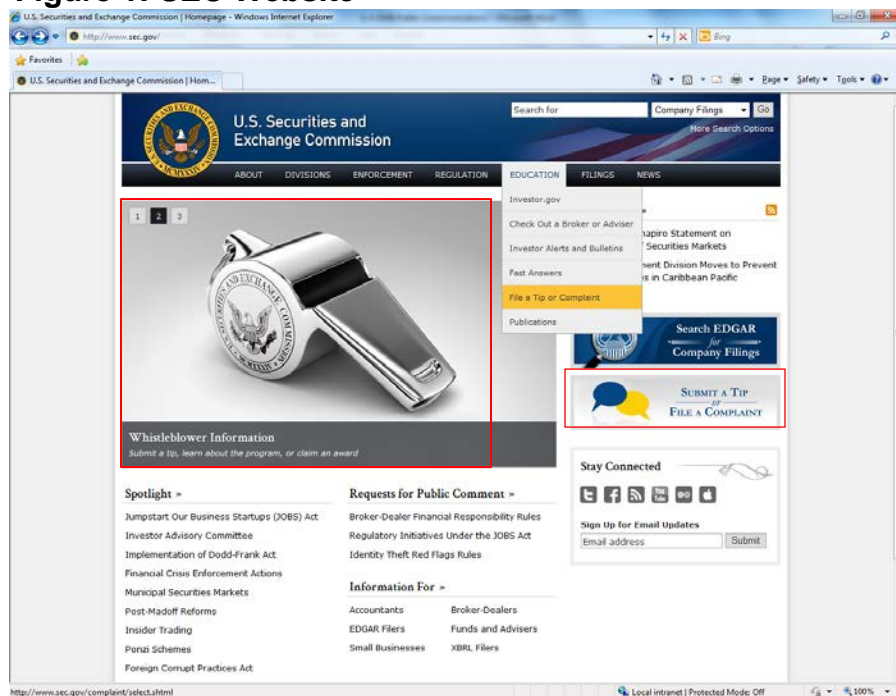
Recommendation 2:

The Division of Enforcement should ensure that the Office of the Whistleblower (OWB) assesses the key performance measures that are contained in their internal control plan and develop performance metrics where appropriate. These performance metrics should be added to OWB's internal control plan.

Access to OWB's Website from the SEC's Website

There are four or more possible ways the public can access OWB's website to learn about the whistleblower program or file a complaint with the SEC. The SEC's public website consists of two hyperlinks: (1) Submit a Tip File a Complaint, and (2) Large "whistle" image, as shown in Figure 1, that takes the public to OWB's website. The third way to reach OWB's website from the SEC's homepage is by using the search engine on the SEC's public website. OIG's use of the keyword "whistleblower" and the option "SEC Documents" in the search engine resulted in 397 options, the first of which led us to OWB's website. Finally, from the SEC's public website, the "Education" drop down menu has a "File a Tip or Complaint," option that takes the public to OWB's website. Overall, we found the quickest way to access OWB's website is by clicking on the "Whistle" hyperlink.

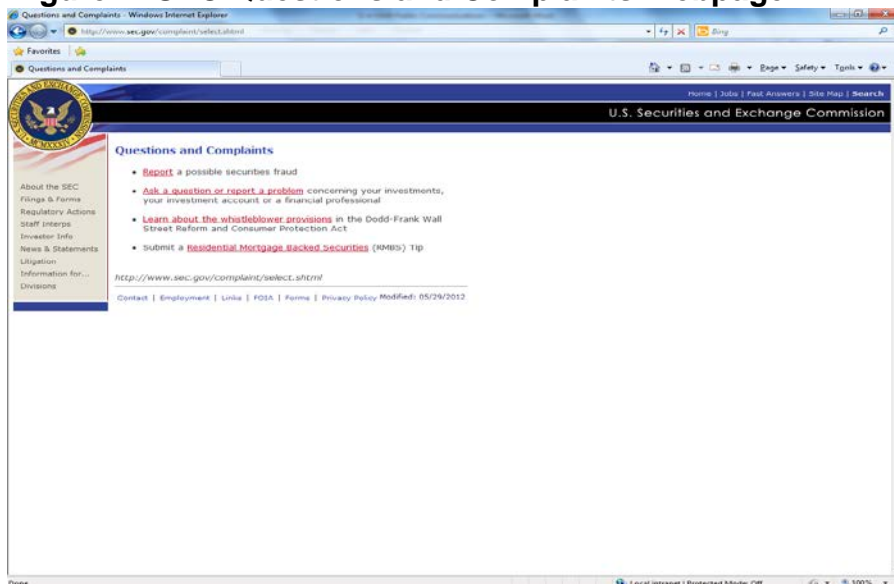
Figure 1: SEC Website



Source: <http://www.sec.gov>

When the hyperlink "Submit a Tip File a Complaint" is clicked from the SEC's website, the public is taken to a "Questions and Complaints" webpage which consists of four options regarding various SEC programs that can be accessed, as illustrated below in Figure 2.

Figure 2: SEC Questions and Complaints Webpage



Source: <http://www.sec.gov/complaint/select.shtml>

The third option “Learn about the whistleblower provisions,” feeds directly into OWB’s website. OWB’s website is shown in Figure 3.

Figure 3: OWB Website



Source: <http://www.sec.gov/whistleblower>

Management Comments




DIVISION OF
ENFORCEMENT

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
100 F Street, N.E.
Washington, DC 20549

MEMORANDUM

TO: Jon T. Rymer, Acting Inspector General, Office of Inspector General

FROM: Robert S. Khuzami, Director 

RE: Division of Enforcement's Response to the Office of Inspector General's Report on Audit No. 511 - *OIG's Evaluation of the SEC's Whistleblower Program*

DATE: January 16, 2013

I. Introduction

The Division of Enforcement (Enforcement) submits this memorandum in response to the draft report of the Office of Inspector General (OIG) on OIG Audit No. 511 entitled "*OIG's Evaluation of the SEC's Whistleblower Program*" (Report). We appreciate the opportunity to respond to the Report.

The Report included two recommendations for the Division of Enforcement; one related to the work of Enforcement's Office of Market Intelligence (OMI) and one related to the work of the Office of the Whistleblower (OWB). You requested that our response indicate whether we "concur or do not concur" with the recommendations. As described more fully below, we "concur" with both of the recommendations of the Report.

II. Recommendation Related to OMI

Recommendation 1: *The Office of Market Intelligence (OMI) should assess the manual triage process and establish key performance metrics that can be used to measure process performance. These performance metrics should be documented in OMI's written policies and procedures.*

Enforcement concurs with this recommendation, and is in the process of assessing the manual triage process to determine if key performance metrics can be established to measure process performance beyond those measures currently employed by OMI management. Enforcement is committed to the timely, effective, and responsible

handling of tips, complaints, and referrals (TCRs). Each year, the agency receives a high volume of TCRs of varying quality that allege a broad spectrum of possible violations of the federal securities laws and other possible improper conduct. The broad spectrum of alleged conduct requires OMI management to employ a number of measures to ensure that each TCR timely receives appropriate review and consideration by professional staff before disposition or assignment. OMI management continues to assess the manual triage process to ensure that Enforcement appropriately pursues all credible allegations of conduct that could violate the federal securities laws or conduct that could pose a risk of harm to investors.

III. Recommendation Related to OWB

Recommendation 2: *The Office of the Whistleblower (OWB) should assess the key performance measures that are contained in their internal control plan and develop performance metrics where appropriate. These performance metrics should be added to OWB's internal control plan.*

Enforcement concurs with this recommendation and supports OWB's work to assess the key performance measures contained in its internal control plan, including the development of performance metrics, where appropriate. Enforcement agrees that performance metrics related to OWB's internal controls may be of value to the whistleblower process, including review and assignment of whistleblower complaints in conjunction with OMI's manual triage process; timely communications with whistleblowers, where appropriate; and the administration of whistleblower award claims.

Audit Requests and Ideas

The Office of Inspector General welcomes your input. If you would like to request an audit in the future or have an audit idea, please contact us at:

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Office of Inspector General
Attn: Assistant Inspector General, Audits (Audit Request/Idea)
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