

## **Response to SEC Proposed Rule: Amendments to the Commission’s Whistleblower Program Rules, File Number S7-16-18**

We believe the SEC’s Whistleblower Program is an important avenue for individuals who want to aid regulators in their efforts to police the capital markets. This comment letter discusses our views on two areas within the operation of the Whistleblower Program that, if amended, we feel would make the program much more effective:

- (1) the prolonged delay by the Whistleblower Office to make preliminary and final determinations following applications for an award, and
- (2) credible evidence of illegal activities and large-scale frauds brought to the Commission are being overlooked and the whistleblower’s analysis is unused.

### **Delayed SEC Communications**

We believe the SEC’s efforts to amend the Whistleblower Program Rules should focus on providing a remedy for the extended length of time individuals wait between timely filing of a WB-APP form and receiving a preliminary and final determination from the SEC. Although whistleblowers have strict deadlines in which to file information and responses with the SEC Whistleblower Office, the SEC does not have any firm deadlines. Consequently, many whistleblowers have been waiting an inordinate amount of time to receive any determinations from the Whistleblower Office.<sup>1</sup>

Therefore, we support the statements of Kohn, Kohn & Colapinto, LLP contained in the public comment filed July 24, 2018, with regard to *Delay and the Summary Disposition Procedures*. Specifically, we would like to reiterate the following:<sup>2</sup>

“The most significant problem with the SEC’s current whistleblower program is not the rare instance where a whistleblower obtains a large reward, but rather the prolonged delay in processing reward applications. These delays can drag on for years and based on our direct experience, can be as long as four (4) years and running. It is simply unacceptable that the Commission can take the duration of an entire Presidential term to decide on an award in a whistleblower case, after the Commission has completed its investigation into the underlying misconduct and collected the sanctions from the wrongdoer. Moreover, because the Commission staff would have directly worked with the whistleblower and/or used the whistleblower’s “original information” to sanction the wrongdoer, the Commission should be in a position to expeditiously approve rewards.”

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<sup>1</sup> Rachel Louise Ensign and Jean Eaglesham, *SEC Backlog Delays Whistleblower Awards*, The Wall Street Journal, May 4, 2015 <https://www.wsj.com/articles/sec-backlog-delays-whistleblower-awards-1430693284>

*SEC Whistleblower Program Delays: What You Need to Know*, Katz, Marshall & Banks, LLP, December 21, 2015 <https://www.kmblegal.com/sec-whistleblower-blog/sec-whistleblower-program-delays-what-you-need-know>

Yves Smith, *SEC Knives Its Whistleblower Program*, Naked Capitalism, July 9, 2018

<https://www.nakedcapitalism.com/2018/07/sec-knives-whistleblower-program.html>

Dave Michaels, *SEC Whistleblower Payouts Slow Amid Deluge of Reward Seekers*, The Wall Street Journal, August 5, 2018 [https://www.wsj.com/articles/sec-whistleblower-payouts-slow-amid-deluge-of-reward-seekers-1533474001?mod=hp\\_lead\\_pos3](https://www.wsj.com/articles/sec-whistleblower-payouts-slow-amid-deluge-of-reward-seekers-1533474001?mod=hp_lead_pos3)

<sup>2</sup> Letter from Kohn, Kohn & Colapinto, LLP to SEC Chairman Jay Clayton, July 24, 2018, Re: File No. S7-16-18, Amendments to the SEC’s Whistleblower Program Rules <https://www.sec.gov/comments/s7-16-18/s71618-4107169-170275.pdf>

## Whistleblower Program Performance Metrics

A 2013 Evaluation of the SEC's Whistleblower Program by the SEC Office of Inspector General ("OIG") found the Office of the Whistleblower ("OWB") and the Office of Market Intelligence ("OMI")<sup>3</sup> deficient in established performance metrics:<sup>4</sup>

"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."

The Office of Inspector General report recommended the Division of Enforcement should ensure that:

- a) "the Office of Market Intelligence (OMI) assesses the manual triage process and establishes key performance metrics that can be used to measure process performance." and
- b) "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."

*In response, the Division of Enforcement concurred with both recommendations.*

Two years later, in 2015, Senators Charles Grassley and Elizabeth Warren requested an update on actions taken by the SEC following the Inspector General report and asked a series of important questions regarding performance metrics for the Whistleblower Program.<sup>5</sup>

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<sup>3</sup> The Office of Market Intelligence is responsible for the collection, analysis, and monitoring of the tips, complaints, and referrals the SEC receives.

<sup>4</sup> *Evaluation of the SEC's Whistleblower Program*, January 18, 2013, U.S. Securities and Exchange Commission Office of Inspector General Office of Audits <https://www.sec.gov/about/offices/oig/reports/audits/2013/511.pdf>

<sup>5</sup> Letter from Senator Charles Grassley and Senator Elizabeth Warren to the Securities and Exchange Commission, dated November 16, 2015, [https://www.warren.senate.gov/files/documents/SEC\\_Whistleblower\\_Letter\\_111615.pdf](https://www.warren.senate.gov/files/documents/SEC_Whistleblower_Letter_111615.pdf)

We believe it is essential the SEC Commissioners report publicly each quarter on all whistleblower cases, including the status, aging, and disposition of each case. Timely reporting from the Commissioners as the senior body overseeing the SEC is crucial to the credibility of the Whistleblower Program.

### **Intent of the SEC Whistleblower Program**

The Commission's example of "independent analysis" was the information collected by Harry Markopolos regarding the ongoing Ponzi scheme perpetrated by Bernard Madoff. As the Commission discussed, Harry Markopolos provided evidence of Madoff's fraud beginning in 2000. Markopolos' "independent analysis" had uncovered and documented the fraudulent dimensions of the scheme. However, Madoff was not charged by authorities until December 2008, but only after Madoff's sons approached authorities and told them Madoff admitted to the scheme.

Following the Madoff fraud and the financial crisis, the SEC Whistleblower Office was established at the direction of Congress to provide a *fast response* to actionable tips from those with knowledge of illegal activities. It was intended to *fast track* the response of the SEC to halt illegal schemes and protect investors and the markets.

When the first SEC whistleblower award was issued in 2012, then-Chair Mary Shapiro stated:<sup>6</sup>

"The whistleblower program is already becoming a success. We're seeing high-quality tips that are **saving our investigators substantial time and resources.**"

In a 2014 speech, Andrew Ceresney, then-Director of the SEC Division of Enforcement stated:<sup>7</sup>

"The program creates a powerful inducement for those aware of wrongdoing to break their silence and it has been very successful, even transformative, in its impact. **Whistleblowers have alerted us to conduct that we would otherwise have been unaware of, allowed us to expedite our investigations, and provided us with a detailed roadmap for misconduct.** The kind of evidence they provide us often cannot be obtained from other sources."

In 2015, then-Chair Mary Jo White spoke about the Whistleblower Program:<sup>8</sup>

"As the program has grown, not only have we received more tips, but we also continue to receive higher quality tips that are of **tremendous help to the Commission in *stopping ongoing and imminent fraud***, and lead to significant enforcement actions on a **much faster timetable than we would be able to achieve without the information and assistance from the whistleblower.**"

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<sup>6</sup> SEC Issues First Whistleblower Program Award, August 21, 2012

<http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171483972#.UjNEd9JONXE>

<sup>7</sup> Remarks at 31st International Conference on the Foreign Corrupt Practices Act, Andrew Ceresney, November 19, 2014 <https://www.sec.gov/news/speech/2014-spch111914ac>

<sup>8</sup> The SEC as the Whistleblower's Advocate, Chair Mary Jo White, April 30, 2015 <https://www.sec.gov/news/speech/chair-white-remarks-at-garrett-institute.html>

“To sum up, after nearly four years of experience, what is our assessment of the Dodd-Frank whistleblower program and how should companies be responding? First, we know that the regime does, in fact, create powerful incentives to come to the Commission with real evidence of wrongdoing that harms investors and it **meaningfully contributes to the efficiency and effectiveness of our Enforcement program.**”

Harry Markopolos provided valuable, original information which was insufficiently examined by the SEC and illustrates how *not* to handle whistleblower information. When a fraud continues for 8 years without adequate investigation, it results in 8 years of unnecessary harm to investors, capital formation and the reputation of the financial markets.

### **Conclusion**

As joint whistleblowers that continuously provided original information and extensive data analysis from 2012 through 2017, we filed 7 WB-APP forms beginning in January 2015 that remain pending and have not received a preliminary determination by the SEC. We have been waiting nearly 4 years for the SEC to issue a preliminary decision in connection with an enforcement action that was concluded and sanctions collected in 2014.

The continued success of the Whistleblower Program depends on transparency and regular (quarterly) reporting from the Commissioners. If the SEC made timely determinations it would encourage active whistleblowers to continue working with the program and hesitant whistleblowers to come forward. Making whistleblowers wait an indefinite amount of time for a determination will undermine the programs’ integrity and effectiveness.

The independent analysis provided to the SEC since 2012 by the whistleblowers authoring this comment letter contained highly detailed information and data regarding an ongoing large-scale fraud that is jeopardizing investor monies, publicly traded companies and the financial system itself. We feel the SEC even today with the Congressionally-mandated Whistleblower Program, is both failing to act promptly or expeditiously on valuable information detailing illicit activity. This failure is allowing risky and illegal behavior to continue and further permeate the capital markets.

While the Whistleblower Program has proven to be a positive tool to have at the disposal of the SEC since its’ conception, it is always wise to re-evaluate and improve on existing programs and methods to ensure that the processing of information reaps the most and best results. We ask for your consideration of our thoughts on these two issues to make the Whistleblower Program an even greater asset to the United States capital markets.

Thank you.