BETTER MARKETS

SEC REPORT

SEC's Whistleblower Program: A $5 Billion Success Story With a Bright Future

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INTRODUCTION

The SEC's whistleblower program was established in the Dodd-Frank Act of 2010, and in the decade since then, it has amassed an impressive record as an effective law enforcement tool. It essentially requires the SEC to pay whistleblowers an award of between 10% and 30% of any monetary sanction exceeding $1 million that the SEC obtains in an enforcement action that is based on original information provided by the whistleblower. It has incentivized those with critical and hard-to-uncover evidence about securities fraud to come forward notwithstanding enormous personal and financial risk. And it has been a resounding success by any measure. As a direct result of the Program, the SEC has been able to file scores of new enforcement actions; halt countless ongoing violations of law; prevent massive harm to investors; hold innumerable law violators accountable; and put hundreds of millions of dollars back in the hands of defrauded investors. Here's a snapshot of a few of the program's key achievements and milestones:

- ✓ Since the start of the "SEC Whistleblower Protection and Rewards Program" in 2011, the SEC has attracted more than 52,400 tips containing valuable market intelligence and information from individuals in 133 countries. From the program's inception to today, the number of whistleblower tips has grown by approximately 300%.
- ✓ This has resulted in the SEC's obtaining nearly $5 billion in monetary sanctions against fraudsters who violated securities laws and SEC rules, including more than $3.1 billion in disgorgement[1] of ill-gotten gains and interest.
- ✓ Of this $3.1 billion, more than $1.3 billion has been, or is scheduled to be, returned to harmed investors. This is directly due to whistleblowers who have provided the SEC with critical information that enabled it to identify and prosecute fraud and other violations.

There is good news on the rulemaking front: The SEC has declared its intention to roll back the most harmful Trump-era rule changes and in the meantime exercise its discretion and exemptive authority to nullify them.

Over the years, the program has faced obstacles, some from within the SEC. For example, the Supreme Court's decision in the *Digital Realty* case[2] narrowed the scope of the anti-retaliation provisions, leaving whistleblowers who report internally but not to the SEC more exposed to harsh consequences at the hands of their employing financial firms. And under the prior administration, the SEC issued a new rule that, while streamlining some aspects of the program, actually undermined its effectiveness in ways that violated the letter and spirit of the Dodd-Frank Act. While the ultimate fate and impact of the *Digital Realty* holding remains unclear, there is good news on the rulemaking front: The SEC has declared its intention to roll back the most harmful Trump-era rule changes and in the meantime exercise its discretion and exemptive authority to nullify them.

[1] Disgorgement refers to the requirement that wrongdoers surrender their ill-gotten gains, the money they have collected through their illegal activities. It serves justice by ensuring that wrongdoers cannot profit from their illegal schemes, and it also serves as a powerful deterrent against violations of law. Disgorgement typically goes hand in hand with the related remedy of restitution, which is the repayment of the wrongdoers' victims with the disgorged funds.

[2] *Digital Realty Trust, Inc. v. Somers,* 138 S. Ct. 767 (2018).

In this updated report, we again highlight the origins, mechanics, and extraordinary benefits of the SEC's whistleblower program, and we look ahead to its important role in enforcing the securities laws and holding wrongdoers accountable. As the SEC's Office of the Whistleblower explains:

> "Assistance and information from a whistleblower who knows of possible securities law violations can be among the most powerful weapons in the law enforcement arsenal of the Securities and Exchange Commission. Through their knowledge of the circumstances and individuals involved, whistleblowers can help the Commission identify possible fraud and other violations much earlier than might otherwise have been possible. That allows the Commission to minimize the harm to investors, better preserve the integrity of the United States' capital markets, and more swiftly hold accountable those responsible for unlawful conduct."[3]

A SHORT HISTORY

The concept of incentivizing or enlisting private citizens to help the government enforce the law has a centuries-long history. One of the early landmark statutes was the False Claims Act, dating back to the Civil War, which was a response to unscrupulous contractors undermining the Union war effort and defrauding the U.S. government "by advertising sick or dead mules as healthy, boxes of sawdust as ammunition, and spoiled food as edible."[4] The False Claims Act outlawed such practices. It also allowed private citizens, known as "relators," to bring lawsuits against contractors that defrauded the government and to receive half the government's recovery. The FCA was later amended to set a maximum recovery for relators of up to 10% of the government's recovery, although that amount was later raised to up to 30% of the government's recovery as part of amendments made to the FCA to reduce corruption in government contracting.[5] Following the accounting scandals at Enron, WorldCom, and other companies, Congress passed the Sarbanes-Oxley Act ("SOX") to improve auditing and public disclosure. SOX also included provisions protecting whistleblowers from retaliation, although it didn't contain incentives to encourage whistleblowing.[6]

These were the limited tools in place that addressed whistleblowers when Congress responded to the financial crisis by passing the Dodd-Frank Act in 2010. Congress was motivated not only by the rampant misconduct that triggered and fueled the crisis but also by specific concerns about the SEC's failure to follow up on whistleblower reports of wrongdoing. Indeed, prior to the Dodd-Frank Act, the SEC actually displayed a casual, if not hostile, attitude toward whistleblowers. A prime example was the Madoff scandal, during which the SEC failed[7] to heed the repeated calls of whistleblowers who presented the SEC with compelling evidence that Bernie Madoff was running the largest Ponzi Scheme

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[3] SEC, Office of the Whistleblower (last accessed Jan. 13, 2021), https://www.sec.gov/whistleblower.

[4] Victor A. Razon, *Replacing the SEC's Whistleblower Program: The Efficacy of a Qui Tam Framework in Securities Enforcement*, 47 Pub. Cont. L.J. 335, 343 (2018).

[5] *Id.* at 343-44. The FCA was also amended to require that relators provide original information, in response to so-called "parasitic suits" in which relators claimed awards based on information already known to the government. *Id.*

[6] 18 U.S.C. § 1514A.

[7] *See* SEC Office of Investigations, *Investigation of Failure of the SEC to Uncover Bernard Madoff's Ponzi Scheme (Aug. 31, 2009)*, https://www.sec.gov/news/studies/2009/oig-509.pdf.

in history and ripping off countless investors. Indeed, the SEC could have stopped Madoff if it had acted on information provided to the agency by whistleblower Harry Markopolos (and others). The agency's enforcement and examination divisions were unable to detect or stop Madoff even though his illegal activities were conducted literally under their noses. Between May 2000 and December 2008—when Madoff confessed and surrendered to the FBI—Madoff's fraudulent fund grew from about $3 billion to $50 billion. During this same time, the SEC conducted at least five examination and enforcement investigations but did not detect, let alone stop, Madoff's massive fraud.

It was partly this failure that motivated Congress to create the whistleblower program at the SEC, which was established by the Dodd-Frank Act over vigorous objections from many in corporate America and even in the face of reservations harbored by some within the SEC itself. Nevertheless, in the Dodd-Frank Act, Congress included Section 922 requiring the SEC to establish a whistleblower program for rewarding and protecting whistleblowers.[8]

THE PROGRAM: HOW IT WORKS

As directed by Congress, in 2011 the SEC set up its whistleblower program.[9] The program incentivizes whistleblowers to provide useful information about wrongdoing by *requiring* the SEC to pay an award to anyone who voluntarily provides the SEC with original information that leads to a successful enforcement action in which the SEC obtains a significant monetary sanction of at least $1 million.[10] The award can be anywhere from 10% to 30% of the sanction, depending on the circumstances.[11] Whistleblowers can also receive an award stemming from a "related action," *i.e.,* an action brought by another government agency based on the same information that the whistleblower provided to the SEC, whether it is conveyed directly by the whistleblower herself or forwarded by the SEC.[12] By statute, awards are paid from the Investor Protection Fund, which in turn is funded by monetary sanctions imposed on wrongdoers.

In accordance with the statute, the program also creates protections and remedies for the benefit of whistleblowers. It prohibits employers from taking any action to discharge, demote, suspend, threaten, harass, or discriminate against whistleblowers for providing information to the SEC or assisting in an investigation. It further allows whistleblowers subjected to retaliation to file suit in federal court and seek reinstatement, double the amount of any backpay owed, and attorneys' fees. The program also protects whistleblowers who provide information they reasonably believe to relate to a possible violation of securities laws, without regard to whether the whistleblower is ultimately eligible for an award.[13]

[8] 15 U.S.C. § 78u-6. Section 23 of the Dodd-Frank Act also established a whistleblower program at the Commodity Futures Trading Commission. 7 U.S.C. § 26. The CFTC has promulgated rules for that program. 17 C.F.R. Part 165.

[9] 17 C.F.R. §§ 240.21F-1 through F-17.

[10] 17 C.F.R. § 240.21F-3(a).

[11] 17 C.F.R. § 240.21F-5(c).

[12] 17 C.F.R. § 240.21F-3(b).

[13] 17 C.F.R. § 240.21F-2(d). The SEC has brought actions against companies alleged to be retaliating against employees.

To administer the program, the SEC established the Office of the Whistleblower.[14] The mission of the Office of the Whistleblower, which is within the Division of Enforcement, is "to protect investors by administering an efficient, high-quality whistleblower program that is responsive to whistleblower needs and helps the Commission identify and stop securities laws violations."[15] The Office of the Whistleblower collects tips, provides resources to whistleblowers, and also, as required, issues an annual report to Congress on the whistleblower program.[16]

As explained in the 2021 report from the Office of the Whistleblower, the whistleblower program has allowed the SEC to recoup an enormous amount of money from wrongdoers.[17] Since the program began, the SEC has obtained orders for over $5 billion in monetary sanctions against whistleblowers. Because whistleblowers are awarded a percentage of the total sanction, this means whistleblowers themselves have received significant awards—214 individuals have received $1.1 billion as of 2021.[18] And indeed, many reports about whistleblower awards (including press releases from the SEC itself) focus on the often significant amounts successful whistleblowers receive. These reports highlighting that a whistleblower has received a significant award help publicize the program and incentivize more whistleblowers to come forward.

CORRECTING SOME MISCONCEPTIONS

Nevertheless, reporting on the size of the monetary awards received by whistleblowers may create some misconceptions about the program, including the belief that whistleblowers are receiving undeserved windfalls at the expense of taxpayers or, worse, ripped-off investors. However, these misconceptions ignore important facts about the whistleblower program and they are ultimately unfounded.

First, awards are conditioned on several mandatory assessments. As explained above, the SEC ***only*** rewards whistleblowers when:

1. They voluntarily provide ***original*** information to the Commission;
2. Their original information leads to a ***successful*** case;
3. That case results in a penalty or sanction of ***over $1 million;*** and
4. The Commission ***actually collects*** those sanctions.[19]

[14] SEC, Office of the Whistleblower: Welcome (last visited Jan. 13, 2022), https://www.sec.gov/whistleblower.

[15] SEC, Whistleblower Program: 2021 Annual Report to Congress (2021), https://www.sec.gov/files/2021_OW_AR_508.pdf.

[16] 15 U.S.C. § 78u-7(d). In addition to the Office of the Whistleblower's annual report, Section 922 required that the SEC's Office of Inspector General evaluate the Whistleblower Program. The OIG released this report in 2013, and generally found that the Whistleblower Program was performing as required and expected. SEC Office of the Inspector General, *Evaluation of the SEC's Whistleblower Program*, Report No. 511 (Jan. 18, 2013), https://www.sec.gov/about/offices/oig/reports/audits/2013/511.pdf.

[17] U.S. Securities & Exchange Commission, Office of the Whistleblower: Welcome (last visited Jan. 12, 2022), https://www.sec.gov/whistleblower.

[18] SEC, *Whistleblower Program: 2021 Annual Report to Congress (2021),* https://www.sec.gov/files/2021_OW_AR_508.pdf.

[19] 15 U.S.C. § 78u-6(b)(1).

These protections ensure that whistleblowers only collect awards when they offer information that is actually useful to a truly successful Commission enforcement action that actually results in a real monetary recovery. Among other things, this prevents the SEC from wasting money on "parasitic" whistleblowers, *i.e.,* those who collect money even though they provided information that was already known to the SEC, and therefore contributed little, if anything to the successful action. Similarly, it prevents unscrupulous actors from collecting awards for information they were obligated to provide in the first place. In other words, Section 922 and the rules the SEC finalized in 2011 contain ample protections to ensure that undeserving individuals cannot obtain status as a whistleblower and claim a significant award.[20]

Further protection against undeserved award amounts is contained in the factors the SEC uses to guide its discretion in determining how much to award any particular whistleblower, including:

1. the ***significance*** of the information provided by the whistleblower to the success of the covered judicial or administrative action;
2. the degree of ***assistance*** provided by the whistleblower and any legal representative of the whistleblower in a covered judicial or administrative action; and
3. the programmatic interest of the Commission in ***deterring violations*** of the securities laws by making awards to whistleblowers who provide information that leads to the successful enforcement of such laws.[21]

Whistleblowers provide immense benefits: They help halt violations of law that the SEC might never uncover, thus preventing hundreds or thousands of investors from suffering losses, and they help recover funds for the benefit of already-victimized investors.

These factors help further ensure that whistleblower award amounts depend on the real value of the information provided to the Commission and the public.

In addition, the awards must be judged in light of two other key factors. First, by and large, whistleblowers are not just receiving a windfall as a result of being in the right place at the right time. Whistleblowers face considerable risks and hardships which can be career-ending, result in the destruction of professional relationships, and cause significant financial hardship. It obviously requires the prospect of a substantial award to persuade most people to assume these enormous risks. Without adequate financial incentives, few people would come forward and undertake those burdens for the mere possibility of an award.[22]

[20] The Dodd-Frank Act included additional restrictions on whistleblower awards, including, for example, the provision that no award can be made "to any whistleblower who is convicted of a criminal violation related to the judicial or administrative action for which the whistleblower otherwise could receive an award under this section." *See* 15 U.S.C. § 78u-6(c)(2).

[21] 17 C.F.R. § 240.21F-6.

[22] This is an important point. A legitimate whistleblower can make a report of genuine wrongdoing and yet get no award whatsoever through no fault of their own. For example, if the amount the SEC ends up recovering is less than $1 million, or the SEC already knew the information, or the SEC brought an enforcement action as a result of the tip but lost due to a flawed litigation strategy, the whistleblower would recover nothing. In other words, award amounts need to be large enough to account for the (unknowable) possibility that legitimate whistleblowers will undertake enormous risk and end up with nothing.

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Contrary to another misconception, whistleblower rewards are neither funded by taxpayers nor paid at the expense of harmed investors. Instead, Congress explicitly provided that they would be paid from a segregated fund created by Congress and administered by the SEC called the Investor Protection Fund. This fund is replenished with penalties, sanctions, or disgorgement amounts that the SEC collects from wrongdoers but cannot otherwise distribute to investors.[23]

THE ENORMUS BENEFITS

Holding fraudsters accountable, halting violations of law, and helping investors recover losses are the primary goals of the Whistleblower Program. Whistleblowers perform a vital public service by revealing fraud and other illegal conduct. Much of this conduct is hard-to-detect by outsiders, including regulators who examine and inspect regulated entities. Whistleblowers provide ready-made, original information that helps regulators and law enforcement agencies initiate enforcement proceedings that often quickly halt illegal conduct and prevent significant future harm that would have escaped detection. For example, in January 2020, the SEC awarded a total of $322,000 to two whistleblowers whose information helped stop an ongoing fraud.[24] These actions also serve as a deterrent to those who would violate the law for their personal gain. Whistleblowers do this by identifying the specific individuals engaged in illegal conduct, providing specific documents (or telling the SEC where the evidence can be found), identifying illegal transactions, and providing detailed explanations that "connect the dots" for law enforcement.

Since the establishment of the Whistleblower Program in 2011, the SEC has received thousands of high-quality tips and hard to obtain evidence from whistleblowers about possible securities law violations, information which in many cases would not have otherwise been obtained. This information expands the Commission's knowledge base and provides insight into fraudulent activities harmful to U.S. investors, enabling the SEC to optimally target its limited enforcement and examination resources.

Whistleblowers also provide important information about violations of law even when the activities are taking place or being planned in countries where the SEC lacks jurisdictional authority. While most of the information and data come from insiders, analysts, investors, and others based in the United States, the SEC has also received submissions from individuals living in 133 other countries. The international scope of the program has helped the SEC acquire information that it otherwise would not be able to obtain given its jurisdictional limitations.

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[23] In Section 922, Congress explicitly prohibited the SEC from taking into account the balance of the Investor Protection Fund when determining award amounts. This is further evidence that Congress's overriding concern in passing Section 922 was incentivizing whistleblowers.

[24] *See* SEC Press Release, *SEC Awards Whistleblowers Whose Information Helped Stop Fraud* (Jan. 22, 2020), https://www.sec.gov/news/press-release/2020-15.

This trove of information has enabled the agency to initiate new proceedings as well as develop existing investigations. Of those whistleblowers who received awards in fiscal year 2021, nearly 56 percent provided original information that ***caused the SEC to open a new investigation.***[25] Whistleblowers also provide missing pieces of information that can serve a decisive role in an already-open investigation. More than 44 percent of whistleblowers who received awards in 2021 provided original information and analysis that significantly contributed to ***an existing case***.[26] For example, in March 2020, the SEC awarded $450,000 to a whistleblower who provided information relating to an investigation that was already ongoing, because the whistleblower's information "helped focus an ongoing investigation on the violations that were ultimately charged."[27] As required by statute, these cases all resulted in the SEC's collecting fines, sanctions, penalties, or disgorgement of at least $1 million, *i.e.,* they all resulted in a significant recovery of money. By providing the SEC with information that the agency did not already have leading to a significant and successful enforcement action, at the very least each of these whistleblowers saved the SEC (and by extension taxpayers), a government agency with limited resources, a significant amount of investigative time and money. Almost certainly, many of these tips led to enforcement actions that would not have even been initiated absent the information, and many tips ensured that enforcement actions succeeded that would otherwise would have failed or produced more modest results.

By providing the SEC with information that the agency did not already have leading to a significant and successful enforcement action, each of these whistleblowers saved the SEC significant investigative time and money.

Ultimately, in the 10 years since the SEC made its first whistleblower award, the SEC has imposed sanctions and penalties totaling more than $5 billion—including more than $3.1 billion in disgorgement of ill-gotten gains and interest—from fraudsters and others who violated the securities laws and SEC rules.[28] From these amounts, the SEC has returned or is scheduled to return almost $1.3 billion to harmed investors. So, by amply rewarding whistleblowers—as mandated by Congress—victimized investors have received or will receive $1.3 billion that they likely would never have recovered. And because many of the frauds would likely have gone undetected much longer without the help of the whistleblowers, their assistance averted even greater investor harm.

UNDERMINING THE $5 BILLION SUCCESS STORY, WITH HOPE FOR THE FUTURE

Unfortunately, despite the Whistleblower Program's demonstrable success in attracting hard-to-obtain information and helping the Commission effectively protect investors and promote market integrity, many in the industry have been hostile to the whistleblower program and have sought to undermine it—efforts that have, unfortunately, met with some success.

[25] SEC, *Whistleblower Program: 2021 Annual Report to Congress* 24 (2021), https://www.sec.gov/files/2021_OW_AR_508.pdf.

[26] *Id.*

[27] SEC Press Release, *SEC Awards $450,000 to Whistleblower* (Mar. 30, 2020), https://www.sec.gov/news/press-release/2020-75.

[28] *Id.*

Many in corporate America were vigorously opposed to the inclusion of Section 922 in the Dodd-Frank Act, and the industry has continued to attempt to undermine the SEC's Whistleblower Program. A significant setback came with the Supreme Court's decision in *Digital Realty Trust, Inc. v. Somers*.[29] In that case, urged on by industry groups such as the Chamber of Commerce,[30] the Supreme Court held that Section 922's anti-retaliation provisions only applied to whistleblowers who make a report to the SEC, not those who have only reported misconduct internally.[31] This leaves whistleblowers who attempt to address compliance concerns internally, without reporting to the SEC, exposed to retaliation.

In 2020, the SEC itself, under the prior administration, finalized a number of amendments to the whistleblower rules, some of which were designed to undermine the efficacy of this highly successful program, without a persuasive legal or investor protection justification. For example, the SEC announced, in the rulemaking process, that it had a pre-existing discretion to consider the dollar amount of an award when making an award determination and to adjust the amount downward. In other words, the SEC claimed for itself the ability to lower the dollar amount awarded to a whistleblower, even if a whistleblower met the statutory criteria justifying a larger award. This was contrary to the letter and spirit of Section 922, which contains no provision authorizing the SEC to reduce award amounts based solely on a dollar amount. As Commissioner Allison Lee pointed out in her dissent from the 2020 amendments, the factors Congress directed the SEC to consider all relate to the "the merits of a whistleblower's conduct or the value of the information she provides," while the potential size of the award does not.[32] This threatened to undermine the effectiveness of the Whistleblower Program, since it "inject[ed] an arbitrary wildcard into what was a sensible, merits-linked calculus," increasing the potential variability of awards and introducing more risk into the decision to become a whistleblower.[33]

Other aspects of the 2020 amendments were problematic. The rule narrowed the circumstances under which an award could be made based on a "related action." Section 922 uses mandatory language—the "Commission shall . . . pay an award"—to describe the Commission's obligation to make an award to a whistleblower whose information leads to a recovery by another government agency. Nevertheless,

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[29] 138 S. Ct. 767 (2018).

[30] Brief amicus curiae of Chamber of Commerce of the United States of America, *Digital Realty Tr., Inc. v. Somers,* 138 S. Ct. 767 (2018) (No. 16-1276).

[31] 139 S. Ct. at 772-73.

[32] SEC Commissioner Allison Herren Lee, *Statement: June Bug vs. Hurricane: Whistleblowers Fight Tremendous Odds and Deserve Better (Sept. 23, 2020)*, https://www.sec.gov/news/public-statement/lee-whistleblower-2020-09-23.

[33] *Id.* As Commissioner Lee cogently explained, this provision masqueraded as an improvement to the 2018 proposal but was far from an enhancement. In the 2018 proposal, the SEC argued that the 2011 rules left it without the ability to reduce awards based on dollar amounts that the agency might deem excessive. Accordingly, the SEC proposed to establish a rule that would give it discretion, where an award could involve a sanction of over $100 million, to reduce the award amount if the Commission determined that the amount exceeded what was "reasonably necessary to reward the whistleblower and to incentivize similarly situated whistleblowers." Better Markets staunchly opposed this proposed rule amendment. *See* Better Markets Comment Letter on Whistleblower Program Rules (Sept. 18, 2018), https://bettermarkets.org/sites/default/files/Better%20Markets%20CL%20to%20SEC%20on%20Whistleblower%20Program%209-18-18.pdf. The final 2020 amendments removed that offending provision from the rule itself—seemingly an improvement—but the accompanying release insisted that the SEC always had the authority to reduce awards based on dollar amount. The SEC thus claimed the same problematic, extra-statutory discretion it had proposed in 2018, but without the limitation that the discretion would only be exercised where a sanction could exceed $100 million, surreptitiously ***expanding*** a provision it purported to remove from the final rule. SEC Commissioner Allison Herren Lee, *Statement: June Bug vs. Hurricane: Whistleblowers Fight Tremendous Odds and Deserve Better* (Sept. 23, 2020), https://www.sec.gov/news/public-statement/lee-whistleblower-2020-09-23.

out of concern for whistleblowers' getting "two bites at the apple," the SEC finalized a provision that, despite the mandatory nature of the statute, purported to give the SEC discretion to deny a whistleblower an award stemming from a related action based on a vague new standard. The amendment provided that if the whistleblower could potentially receive an award from a whistleblower program at another agency and the SEC determined that the other whistleblower program had "the more direct or relevant connection to the action,"[34] then it could decline to make an award. This new test failed to account for the nature of the other whistleblower award program, meaning that whistleblowers whose tips were forwarded to another agency might be subject to a whistleblower program less favorable than the SEC's, unnecessarily and arbitrarily introducing even more risk into the process.[35]

Yet another problem with the amendments was the accompanying interpretive guidance regarding how the SEC will determine whether a tip constitutes "independent analysis" that justifies an award. Section 922 provides that "original information" includes information that is derived from the "independent knowledge ***or analysis***" of the whistleblower.[36] The SEC's interpretive guidance imposed extra-statutory and restrictive conditions on when independent analysis qualifies as original information. Under the guidance, to qualify as "independent analysis," a whistleblower's submission must provide evaluation, assessment, or insight beyond what would be reasonably apparent to the Commission from publicly available information. Furthermore, in making that determination, the Commission considers whether the whistleblower's conclusions derive from multiple sources (including sources that are not readily identified and accessed by a member of the public without specialized knowledge, unusual effort, or substantial cost) and whether the sources collectively raise a strong inference of a potential securities law violation that is not readily inferable by the Commission from any of the sources individually.[37]

Again, this is contrary to the text and intent of Section 922, which does not impose these restrictions on the nature of the independent analysis that can support an award. More alarmingly, the interpretive guidance, particularly the provision requiring that the sources raise a strong inference of illegal conduct that is not "reasonably inferable" by the SEC from the sources individually, ignores the history of Section 922. Specifically, Section 922 was at least partially motivated by the SEC's failure to detect Bernie Madoff's brazen fraud. Yet as detailed by the SEC's inspector general, that debacle included the SEC's failure to heed multiple obvious red flags, including those raised in publicly available sources.[38] In light of this context, it is highly unlikely that Congress intended the SEC to condition whistleblower awards on whether, in hindsight, it thinks the illegal conduct was "reasonably inferable."

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[34] 17 C.F.R. § 240.21F-3(b)(3)(1).

[35] SEC Commissioner Allison Herren Lee, *Statement:*
June Bug vs. Hurricane: Whistleblowers Fight Tremendous Odds and Deserve Better (Sept. 23, 2020), https://www.sec.gov/news/public-statement/lee-whistleblower-2020-09-23.

[36] 15 U.S.C. § 78u-6(a)(3).

[37] Whistleblower Program Rules, 85 Fed. Reg. 70,898, 70,929 (2020).

[38] SEC Office of Investigations, *Investigation of Failure of the SEC to Uncover Bernie Madoff's Ponzi Scheme* 80-81 (Aug. 31, 2009), https://www.sec.gov/files/oig-509.pdf.

Better Markets vigorously opposed both the 2018 proposal and the 2020 final rule.[39] In addition, because of the severe flaws in the 2020 amendments, a prominent whistleblower attorney filed a lawsuit challenging the rule. As the plaintiff asserted, based on a decade of experience representing whistleblowers, there was "no doubt that the Final Rule will reduce the number of individuals who will become SEC whistleblowers," especially among "the most senior, salaried, and tenured executives on Wall Street."[40] Better Markets voiced strong support for that lawsuit.[41]

Fortunately, under new leadership, the SEC has again recognized the importance of the Whistleblower Program, and it has taken steps to ameliorate some of the potential harm caused by the 2020 amendments.[42] Specifically, on August 2, 2021, Chair Gary Gensler announced he was directing staff to reconsider the problematic elements of the rule, and on August 13, 2021, the SEC published a policy statement indicating it would:

Due to the enforcement efforts made possible by the whistleblower program, investors have more confidence in the securities markets.

1. Consider using its exemptive authority to provide awards based on related actions that involve another agency's whistleblower program, without regard to whether the other whistleblower program has a more direct and relevant connection to the action, where there is concern the whistleblower will not receive an adequate award from the other program; and
2. Make clear that the SEC will consider dollar amounts "only in connection with provisions of the rules that explicitly contemplate the use of such discretion to raise awards."[43]

This is encouraging. However, it is vital that the SEC follow through on revisiting and repealing the problematic aspects of the 2020 amendments. The composition and leadership of the SEC will of course change over time, and absent a rule change and revised guidance, a future SEC could readily begin denying awards or lowering award amounts based on those restrictive provisions.

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[39] Better Markets Comment Letter on Whistleblower Program Rules (Sept. 18, 2018), https://bettermarkets.org/sites/default/files/Better%20Markets%20CL%20to%20SEC%20on%20Whistleblower%20Program%209-18-18.pdf; Better Markets Press Release, *SEC's Actions on Whistleblower Program Are Contrary to Congress's Express Intent and Will Make Successful Program Investor- and Whistleblower-Unfriendly* (Sept. 23, 2020), https://bettermarkets.org/newsroom/sec-s-actions-whistleblower-program-are-contrary-congress-s-express-intent-and-will-make/.

[40] See Complaint, ¶¶ 99-108, *Thomas v. SEC,* 21-cv-108 (D.D.C. Jan. 13, 2021).

[41] Stephen Hall, *et al*., Better Markets blog, *Lawsuit Challenging SEC Whistleblower Rule Is "On Target"* (Jan. 15, 2021), https://bettermarkets.org/newsroom/lawsuit-challenging-sec-whistleblower-rule-target/.

[42] The degree of harm inflicted by the September 2020 rule amendments is difficult to gauge but they were at least short-lived. The November 2020 election results, the promise of new SEC leadership, and the *Thomas* lawsuit all portended a rollback of the offending provisions. The SEC's public announcement in August 2021 confirmed that they would be in effect suspended pending a rewrite.

[43] Procedures for the Commission's Use of Certain Authorities Under Rule 21F– 3(b)(3) and Rule 21F–6 of the Securities Exchange Act of 1934, 86 Fed. Reg. 44,604 (Aug. 13, 2021). In light of these actions to revisit the 2020 amendments, the lawsuit challenging those amendments has been held in abeyance. *See* Order on Joint Motion to Stay, *Thomas v. SEC*, 21-cv-108 (D.D.C. Aug. 10, 2021).

CONCLUSION

The SEC Whistleblower Program has profoundly improved the SEC's ability to detect, punish, and deter securities fraud while helping injured investors recover their losses. As a result, the SEC is more effectively pursuing its three-part mission of protecting investors, maintaining the integrity of the securities markets, and facilitating capital formation. Due to the enforcement efforts made possible by the whistleblower program, investors have more confidence in the securities markets. That in turn helps ensure that investors can safely invest in markets and reap the returns they offer, while entrepreneurs and companies have access to the capital they need to start and grow their businesses. Fortunately, the Commission has committed to maintaining a robust whistleblower program and reversing earlier rule changes and guidance that undermined the program in important respects. With those steps, the whistleblower program will remain on track as a robust and effective law enforcement tool to be used against those who would violate the law and prey on others for personal gain.

BETTER MARKETS

Better Banks | Better Businesses
Better Jobs | Better Economic Growth
Better Lives | Better Communities

Better Markets is a public interest 501(c)(3) non-profit based in Washington, DC that advocates for greater transparency, accountability, and oversight in the domestic and global capital and commodity markets, to protect the American Dream of homes, jobs, savings, education, a secure retirement, and a rising standard of living.

Better Markets fights for the economic security, opportunity, and prosperity of the American people by working to enact financial reform to prevent another financial crash and the diversion of trillions of taxpayer dollars to bailing out the financial system.

By being a counterweight to Wall Street's biggest financial firms through the policymaking and rulemaking process, Better Markets is supporting pragmatic rules and a strong banking and financial system that enables stability, growth, and broad-based prosperity. Better Markets also fights to refocus finance on the real economy, empower the buyside, and protect investors and consumers.

For press inquiries, please contact us at press@bettermarkets.com or (202) 618-6430.

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