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## SEC Enriches Fraudsters, Lawyers as Secrecy Shrouds Tips Program



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### Listen

- SEC whistleblower decisions are inconsistent, cloaked in secrecy, often go to clients of agency ex-officials
- Program increasingly busy but has drawn ire of federal courts at times

An SEC whistleblower program designed to prevent another Bernie Madoff-type scandal often ignores its own rules, shields much of its work from the public, and has been a financial boon for law firms that hired former agency officials, a Bloomberg Law investigation has found.

Written into the Dodd-Frank financial reform law of 2010 and championed by Sens. Elizabeth Warren (D-Mass) and Chuck Grassley (R-Iowa), it was created to make sure tips about financial wrongdoing aren't ignored as they were before Madoff's \$64.8 billion Ponzi scheme.

By that measure, it's been successful: the Securities and Exchange Commission has gotten roughly 60,000 tips since 2012, and paid out more than \$1.3 billion in awards.

### [PODCAST: Has SEC Tips Program Stopped Next Madoff? No One Knows](#)

But the review of all 561 SEC final orders revealed a program operating in secrecy far beyond its legislative mandate to protect whistleblowers' identities. The agency won't disclose names of companies involved in fraud, hasn't identified all of the law firms that received money for their clients, and won't even report the office's annual budget.

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That makes it nearly impossible for Congress and the public to gauge what crimes are uncovered, the criteria used to determine which cases it takes and whether individual payments that can top \$100 million are justified.

"There is no public interest check on this program, and the secrecy makes it impossible to measure its success or to provide a check on what it's doing," said Reuben Guttman, a Washington attorney who has represented whistleblowers in medical, pension and pharmaceutical fraud cases. "The program calls out for massive congressional oversight."

Bloomberg Law examined court records, documents obtained through the Freedom of Information Act and interviewed more than a dozen attorneys. Among the findings:

- The whistleblower office awarded \$36 million in September to a person who was "culpable in the underlying scheme," according to the final order and delayed reporting the crime until after the criminal statute of limitations had expired. The five-year delay allowed the fraud to continue, costing victims millions of dollars.
- The SEC awarded \$1.2 million in 2020 to an informant who the staff alleged "planned" and "initiated" the multimillion-dollar fraud at the heart of the case.
- A D.C. Court of Appeals judge called some of the agency's rules among "the sloppiest regulations I have ever seen," and warned the commission to "get its act together."
- Law firms led by or employing two former high-ranking SEC officials—one who helped write the rules, another who led the program for five years—received at least \$205 million in awards for whistleblower clients.

The commission said in a written statement that it can waive requirements when deciding awards.

"Whether a waiver is appropriate in a particular case depends on the facts and the circumstances," SEC officials wrote in response to written questions. "There is no

special preference for claimants who are represented by counsel, including counsel who were former SEC attorneys.”

More than half of all payments to whistleblowers have been made in just the past 18 months. Since becoming SEC chairman in 2021, Gary Gensler has rolled back rules that allowed the commission to set caps on awards it deemed too large and shortened the time whistleblowers wait to be paid. The SEC also changed some rules in 2020 to make it easier to waive some filing requirements.

The agency stretches its rules at times and decisions can seem inconsistent or contradictory, said Sean McKessy, who ran the program from its inception in 2011 until 2016. He now handles SEC whistleblower cases at the law firm Phillips & Cohen.

“Rules on their own can be waived because the commission created them and they can enforce them the way they see fit,” McKessy said. “The statute is what it is, but it’s so broad it gives the commission a lot of discretion.”

## Connections

The SEC initially denied Bloomberg Law’s Freedom of Information Act request for a full accounting of which lawyers have received payouts on behalf of clients, saying it didn’t keep such records. On appeal it provided a partial list covering the first 10 years of the program, but only one month of data on the \$700 million awarded to informants since January 2021. The agency promised to provide more records in the future.

Jordan Thomas, a former SEC assistant chief litigation counsel who helped write program rules and opened his own whistleblower practice days before it went online, represented clients who received more than \$152 million of the first \$600 million awarded, according to the agency’s first FOIA response. Attorneys typically work on contingency fees ranging from 35% to 40%, according to lawyers who specialize in SEC and Justice Department whistleblower cases.

Thomas said in interviews that his success stems not from connections, but from his ability to identify and build cases based on his knowledge of what SEC investigators need. Still, he said understands why the agency is reluctant to release all the numbers.

“It would be indisputable evidence that my law firm, Phillips & Cohen, and a few others that got into this early are the dominating firms, and that would be coming right from the mouth of the SEC,” Thomas said. “I’m not beating my chest; it’s just a fact that it would hurt the program because it would send a signal, rightly or wrongly, that would essentially discourage the competition.”

Alex Platt, a University of Kansas law professor who specializes in securities regulations, has been studying the program for two years while fighting the SEC to obtain records. He said secrecy and apparent advantages for former insiders are hurting the program.

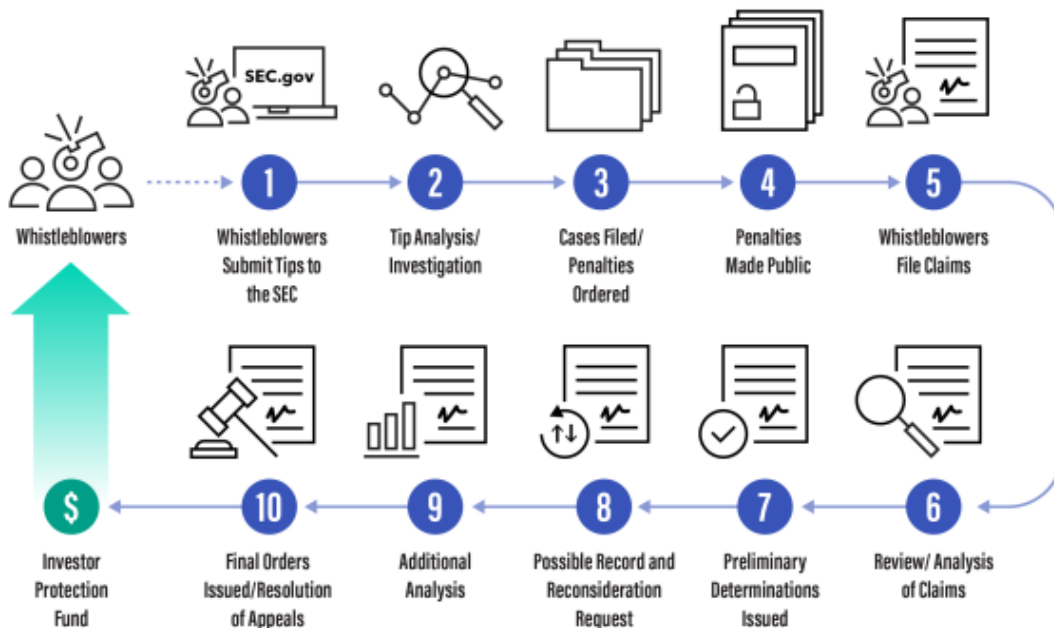
“Yes, they must protect the whistleblower, but it would also be a public service to let potential informants know what type of investigations they take,” Platt said in an interview. “If you have a program that is so complex or so specialized that the same

group of attorneys are getting most of the cases, then the program isn't working properly."

If the SEC were to receive the Madoff tips today, Platt wrote of the program earlier this year, would the result be different?

"The answer is: we don't know."

## How The Process Works



Source: SEC Annual Report to Congress 2021

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Graphic: Jonathan Hurtarte/Bloomberg Law

## 'A Lot of Discretion'

Insiders, whether hourly employees, contractors, or corporate executives, have long played a crucial role in helping the government and investors stop corporate corruption. The False Claims Act administered by the Department of Justice allows individuals who know of fraud to file federal lawsuits on behalf of the government.

Last year the DOJ recouped \$5.6 billion in fraud from defense contractors, medical providers and others. As with the SEC program, the whistleblowers are awarded 10% to 30% of any money recovered or fines paid, minus attorney fees.

That's where the similarities end, according to attorneys and former prosecutors who have worked with both programs.

FCA cases are filed in federal court and subject to supervision both by the DOJ and federal judges. The whistleblower's name eventually will become public, and courts must approve all settlements, fines, dismissals, and attorneys' fees.

The SEC's whistleblower program is far less accountable. The agency in its early years identified some corporate wrongdoers, but hasn't identified a company in any final order since 2017.

A 2018 lawsuit filed by a claimant in the case of Teva Pharmaceutical Industries Ltd. contended that the agency began redacting more information from public disclosures to hide the slow pace of its investigations, rather than to protect whistleblowers, after The Wall Street Journal used the agency's public notices to show long delays in paying informants. Teva paid a fine of more than \$500 million, but the whistleblower waited years without hearing anything from the SEC, according to the complaint.

The agency said in a statement to Bloomberg Law that confidentiality extends to "any information that either identifies, or could reasonably be expected to identify, a whistleblower."

## **Tips and Claims**

About 12,000 tips came in the last fiscal year. They first go through an internal screening process that is supposed to select only the best for full investigations, which can last five years.

A separate group of attorneys review the records once the investigation is completed and makes a decision on which whistleblowers get paid. The agency has 13 full-time and three temporary attorneys who determine how much each claimant should get. The SEC refused to provide more detailed information on how decisions are made.

It has rejected claims because applicants hadn't followed program rules while approving claims under similar circumstances.

For example, the law says the program can only make awards to people who provide original information that leads directly to a sanctions of \$1 million or more.

But in March the commission overruled staff and awarded about \$14 million to someone who SEC lawyers ruled "was not a whistleblower within the meaning of the statute" and that the claimant's information did not lead to the success of the investigation.

It disagreed with some staff conclusions, and wrote it was in the "public interest" to waive the 30-day requirement for filing. The whistleblower waited four years.

## Number of Whistleblower Tips

From Fiscal Year 2012, the first year for which we have full data, to FY 2021, the number of whistleblower tips received by the commission has grown by about 300%.



Source: SEC Annual Report to Congress 2021

Bloomberg Law

Graphic by Jonathan Hurtarte/Bloomberg Law

## Making Sense

McKessy, who headed the program for five years, said while some of the inconsistent decisions may look bad to the public, they are almost always based on the facts at hand.

McKessy pointed to the example of a financial firm employee who reported an ongoing fraud to a regulatory agency, which spent two years investigating and brought no charges. The informant then filed an SEC whistleblower complaint, which upheld the allegations, fined the company, and recouped money for defrauded investors, McKessy said.

“Our rule said it wasn’t a voluntary submission to us because the other agency had already investigated, and unfortunately, we probably can’t pay this guy,” McKessy said. But he lobbied the commission to waive the rules, and the informant was awarded the bounty.

In March, the D.C. Circuit Court of Appeals ruled that some agency regulations covering the criteria for awarding or denying claims were so “genuinely ambiguous” that courts have no choice but to defer to the agency’s judgment. The ruling cited the Supreme Court standard set in 2019 in *Kisor v Wilkie*, which said when the Department of Veterans Affairs rules were so muddled that courts couldn’t override certain decisions.

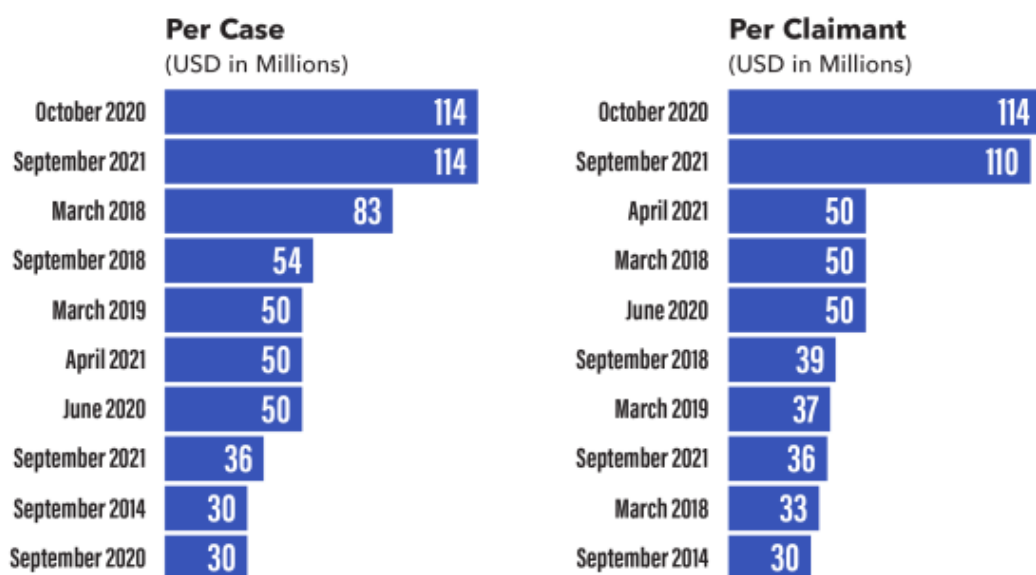
The appeals court said the agency’s decision was “reasonable” and let it stand.

“Are rules like this reviewed by the SEC general counsel? It would seem to me an agency like the SEC would want to do everything it could to make sure its regulations are clear,” D.C. Circuit Court of Appeals Judge David S. Tatel said during a January hearing. “This has got to be one of the sloppiest regulations I have ever seen.”

“You need to take at least from me a message back to the commission that they need to get their act together on these kinds of things,” Tatel said. “More importantly they need to have clarity in their regulations.”

## Top 10 SEC Whistleblower Awards

Below are the top 10 highest awards made since the inception of the SEC's whistleblower program, both by case and by award amount paid to individual claimants.



Source: SEC Annual Report to Congress 2021

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Graphic: Jonathan Hurtarte/Bloomberg Law

## Tight Circle

The program as crafted by Congress and SEC officials let tipsters report financial wrongdoing anonymously and then get between 10% and 30% of any money the agency recovered. It has made awards to more than 270 whistleblowers from a special fund set up by Congress. Any money recovered goes first to the fraud victims and what's left is earmarked for the program.

One of those SEC officials involved in the program's creation was Jordan Thomas. He left the agency days before the program went live in 2011 to set up what he called the nation's first whistleblower practice at Labaton Sucharow. He spent a decade there, helping win more money for his clients than any firm in the country, before forming his own practice in 2022.

His four new partners are all former SEC officials, including Richard Levine, the SEC associate general counsel for legal policy until 2016.

Thomas said their understanding of how the agency identifies and investigates whistleblower claims helps them build cases in ways SEC officials can't.

Thomas' attorneys and clients don't need a warrant to tape phone calls in certain states or gather documents and can build powerful cases before even filing an SEC complaint, making it more appealing for agency investigators. He said his law firm accepts only about a dozen clients per year and has spent hundreds of thousands of dollars hiring experts and readying cases.

A March 26, 2019, case illustrates Thomas' ability to break through the throng of tips and get access to SEC attorneys.

Thomas met with SEC staff even before his client filed a formal complaint. They responded by elevating the not-yet-filed allegation to a "Matter Under Inquiry," according to the final order.

His two clients eventually received \$50 million, even though one of them "unreasonably delayed" reporting the crimes while investors continued to be bilked, according to the final decision.



Lawyer Jordan Thomas (R) is pictured with one of his whistle blower clients, former Deutsche Bank financial analyst Eric Ben-Artzi, who publicly refused an \$8 million award from the Securities and Exchange Commission for exposing improper accounting.

(Photo by Pascal Perich/Contour by Getty Images)



## Calling Old Friends

McKessy's law firm, Phillips & Cohen, has won awards of at least \$50 million for clients since he joined, it said in releases after each award. It received about \$43 million when he headed the program.

McKessy plays up his connections as a way to lure new clients. Former colleagues still at the SEC ask him "all the time" to send good cases their way, he said in an interview. They discuss cases when he returns to his old offices for retirement parties and other events and he also calls former subordinates directly if he has a good case.

Asked if that gives him an unfair advantage, McKessy hesitated and then said:

"I'd say, probably yes. ... That's one of the reasons I think people would want me to be their counsel. They know that I'm known throughout the SEC, that I can make these phone calls."

McKessy said there are also many times "where I can't find a taker," for cases he thinks are strong.

Washington attorney Jason Zuckerman, who represents several whistleblowers, said SEC investigators tend to turn to trusted lawyers they've dealt with before. With thousands of tips pouring in, it's only natural that they would want to work with people whose information and research has proven reliable, he said.

"On a human level, would you pick up a phone call from someone you've dealt with before whose information is credible, or someone random?" Zuckerman said. "I don't know if there is a monopoly on it, but there is credibility with people who have won a number of awards. It's almost triage; they respond to us, and we bring only the best cases."

## Balancing Act

Although protecting the informants is critical, several attorneys said the agency could do that while making more information available. That would improve the program's impact and reputation, they said.

"For the first 10 years, having this unregulated system, like a gold rush, may have been the best way to get the program up and running," said Platt, the University of Kansas law professor. "But now they are entering phase two, and need to change. The SEC is a disclosure agency, this is what they do. Why not impose those same disclosure policies on their own program?"

South Carolina attorney Richard Harpootlian, who handles False Claims Act cases, said Congress must step in because the agency has shown it can't self-regulate.

"They need to revisit the statute; it clearly needs to be cleaned up and the Senate is the place to do that," Harpootlian said.

Warren and Grassley have the sophistication and understanding to fix this, he said.

“I am just not sure people understand how secretive and out of control things have gotten.”

*Data Editor Alex Cohen and former reporter Valerie Bauman contributed to this article.*

## ***How We Did It***

*Bloomberg Law spent five months reviewing all 561 final orders made during the history of the Securities and Exchange Commission’s whistleblower program, cross-checking the facts against court records and agency documents, and attempting to get details about the award payments through a Freedom of Information Act request.*

*The agency initially denied a February request for records on payments made to lawyers representing whistleblowers, saying it had no records responsive to the request. Bloomberg Law then appealed after learning the SEC had given some of those records to University of Kansas law professor Alex Platt several months earlier.*

*The SEC eventually gave Bloomberg Law the same limited records it gave Platt, providing partial information on 10 years of cases but leaving out all payments to lawyers made since January 2021, an 18-month stretch that included more than half of all money given out in the program’s history. The agency subsequently provided one month of additional records and said it would provide additional installments later.*

*Bloomberg Law also interviewed a dozen attorneys, including Justin Thomas and Sean McKessy. Some defended the program; others who said its secrecy undercut its credibility.*

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