



September 18, 2018

Mr. Brent J. Fields  
Secretary  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549-1090

Re: Whistleblower Program Rules (Release No. 34-83557; File No. S7-16-18)

Dear Mr. Fields:

Better Markets<sup>1</sup> appreciates the opportunity to comment on the above-captioned proposal (“Proposal”) released for comment by the Securities and Exchange Commission (“SEC” or “Commission”).

By any measure, the statutorily mandated Whistleblower Program has been a wild success, yet the Commission is proposing changes that risk snatching defeat from the jaws of victory. When considering any changes to this program and risking that success, the Commission should deeply reflect on its failure to stop the egregious and historically costly Madoff Ponzi scheme notwithstanding high-quality, specific whistleblower information provided to the SEC on multiple occasions.

That failure, which harmed so many investors, was the primary motivation for Congress to enact very strong whistleblower provisions that would reward and protect meritorious whistleblowers. It was also the reason that the statute was so explicitly mandatory and limited SEC discretion. After all, the Madoff whistleblower, Harry Markopolos, approached the SEC multiple times and provided detailed analysis and concrete conclusions about Madoff’s scheme. It was as loud and clear a whistle as anyone could blow. Yet, the SEC not only ignored that whistleblower, it ridiculed him. We now know that Madoff’s decades-long fraudulent scheme was rudimentary and paper thin, which any minimally competent investigation would have uncovered.

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<sup>1</sup> Better Markets is a non-profit, non-partisan, and independent organization founded in the wake of the 2008 financial crisis to promote the public interest in the financial markets, support the financial reform of Wall Street, and make our financial system work for all Americans again. Better Markets works with allies—including many in finance—to promote pro-market, pro-business, and pro-growth policies that help build a stronger, safer financial system that protects and promotes Americans’ jobs, savings, retirements, and more.

The SEC's failure to act on such information was a dereliction of duty that cost investors billions of dollars and untold non-monetary harm. For example, in May 2000, when Mr. Markopolos first submitted detailed analysis to the SEC concluding that Madoff was a Ponzi scheme and implored the SEC to stop the fraud, Madoff was managed between \$3 billion and \$7 billion.<sup>2</sup> By the time of Madoff's confession in December 2008, according to the SEC's complaint, the fund had grown to the astronomical level of \$50 billion.<sup>3</sup> Just imagine how many investors' savings and lives would have been protected if the SEC had just done its job and taken appropriate action.

That is why, in creating the Whistleblower Program, Congress was methodical, specific and clear in limiting the SEC's discretion in implementation and execution of the Program. The SEC should act in this area only with the greatest humility and recognition that Congress specifically dictated that the Commission enact a comprehensive, rigorous and highly effective Whistleblower Program that maximally incentivizes whistleblowers to take the huge risk and sacrifice to report information to the Commission.

These specific proposed changes must be critically evaluated against two governing principles: will the changes make the Whistleblower Program even more user-friendly and attract an even greater number of whistleblowers with quality information to the Commission that would stop or deter serious investor harm? And, are the proposed changes in-line with Congress's specific intentions with regards to the Whistleblower Program, and the mandates and limitations Congress imposed on the SEC as it administers this Program?

Unfortunately, the Proposal taken as a whole, dismally fails these two fundamental tests. The Proposal would make the Whistleblower Program user-**unfriendly**, is contrary to Congress's intent, vision and express direction, and the changes are inconsistent with the purposes of the Whistleblower Program, as designed and enacted by Congress. In short, it puts investors needlessly at risk, increases the likelihood of fraud going unreported and therefore undetected, and makes missing future Madoff Ponzi schemes distinctly possible. The Commission should withdraw the Proposal and embrace and strengthen the Program.

## SUMMARY

- The Proposal, as a package, must not be approved as released. The amendments to the Whistleblower Program would arbitrarily, and contrary to Congress's will, send a chilling message to all whistleblowers: if you provide original information that leads to large sanctions, your award will be capped at 10%, the bare minimum required under by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank) – the Act that created the SEC Whistleblower Protection.

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<sup>2</sup> See "Investigation of Failure of the SEC to Uncover Bernard Madoff's Ponzi Scheme." U.S. Securities and Exchange Commission, Office of Investigations. p.62. Available at <https://www.sec.gov/files/oig-509.pdf>.

<sup>3</sup> See SEC's Litigation Release No. 20834 (December 19, 2008). Available at <https://www.sec.gov/litigation/litreleases/2008/lr20834.htm>. This number was later revised-up to \$64.8 billion. (See "Madoff mysteries remain as he nears guilty plea." Reuters (March 11, 2009). Available at <https://www.reuters.com/article/us-madoff/madoff-mysteries-remain-as-he-nears-guilty-plea-idUSTR52A5JK20090311>).

- Congress never intended for the SEC to cap awards at minimum levels, and it certainly did not permit the SEC to use any award level, in terms of absolute dollar amounts, as a metric to analyze and determine an award. Simply put, the \$30 million threshold being set in the Proposal is an SEC construct that is contrary to Congress's will. Congress afforded sufficient discretion to the SEC to determine award levels, but this new proposed threshold and methodology goes impermissibly and arbitrarily beyond what Congress intended and permitted. This change taken with some of the other proposed so-called improvements would make the program less attractive, and thus subvert the purposes of the Whistleblower Program, as Congress designed and enacted, in the process exposing countless investors to continual harm.
- The Proposal would make it easier for the Commission to dismiss and disqualify otherwise meritorious whistleblower submissions. The interpretive guidance on "independent analysis" impermissibly narrows the definition of "original information" and would arbitrarily, and against Congress's express wish, disqualify original information provided by whistleblowers when that information, in addition to original analysis, contains information that the Commission could have inferred from public sources. In other words, according to the Proposal, when a whistleblower provides original information to the Commission that may contain a news article or other publicly available information, the Commission would argue that this whistleblower's information is unoriginal since bits and pieces of it are based on publicly available information which the Commission – in due time – would have gleaned and acted upon.
- The only positive aspect of the Proposal should be de-coupled from the Proposal and approved separately as a standalone provision. We agree that awards should extend over deferred prosecution agreements and non-prosecution agreements.

### **BRIEF DESCRIPTION OF THE PROPOSAL**

This comment letter focuses largely on two of the most important aspects of the Proposal, which are briefly described below.

1. The Proposal adds two additional considerations that the Commission and staff would use in determining award levels: (a) The Proposal recommends that the Commission adjust any whistleblower awards that are below \$2 million to be closer to the statutory maximum of 30% of the collected funds; and, (b) More importantly, the Proposal imposes heightened scrutiny in determining awards above \$30 million but stipulates that the award would not be less than the 10% statutory minimum.<sup>4</sup>

While the comments below focus on this second provision, we oppose both ideas based on the same principle: Congress did not authorize the Commission to apply any dollar amount threshold as a consideration for an award and did not intend for the Commission to reduce the incentive for whistleblowers to report fraud.

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<sup>4</sup> Release at 34748.

2. The Proposal provides an interpretive guidance as to the meaning of “independent analysis” within the definition “original information” by further limiting whistleblower’s use of public information (*i.e.*, news articles, testimony, etc.) in his or her submission.<sup>5</sup> This inappropriately provides the Commission with too much discretion and fails to give potential whistleblowers sufficient certainty, which will needlessly discourage them: the exact opposite of the intent of Congress. Allowing the Commission to dismiss and disqualify otherwise meritorious submissions due to an after the fact claim that it would have otherwise independently identified the information, done an investigation, connected all the dots, and brought a case is simply baseless speculation that introduces ambiguity into a very clear and unambiguous statutory scheme.

## COMMENTS

### Congress Did Not Authorize the Commission to Set Any Dollar Thresholds and Determine Award Levels Using Any Dollar Thresholds as Part of its Award Consideration

In designing the SEC and CFTC Whistleblower Programs, Congress studied various successful and unsuccessful federal whistleblower rewards and bounty programs, including SEC’s own “insider trading-only” whistleblower program. The universal lesson drawn from that study was that those programs that amply and predictably reward whistleblowers are successful. Those that create hurdles, are not user-friendly, and are stingy with their rewards are subsequently ignored by whistleblowers, and hence those regulators are deprived of the high-quality information that the whistleblowers would provide, which would complement and augment the regulator’s capabilities. Therefore, Congress created the SEC Whistleblower Program intending it “to be used actively with ample rewards to promote the integrity of the financial markets.”<sup>6</sup>

Congress also recognized – after hearing expert testimony and talking to whistleblowers and their representatives – that whistleblowers “often face the difficult choice between telling the truth and the risk of committing ‘career suicide,’” and decided that the program should “amply reward[] whistleblower(s) between 10% and 30% of monetary sanctions that are collected based on the ‘original information’ offered by the whistleblower.”<sup>7</sup> Congress purposefully decided against setting either a minimum or maximum dollar threshold and instead, opted for percentage-based formula that would be pegged to the collected penalties and sanctions derived out of the contributions of the whistleblower’s information. In conceptualizing the SEC Whistleblower Program, Congress looked to the very successful whistleblower bounty program at the Internal Revenue Service, that, too, has awards set similarly to a 15-30% range, and **not to any**

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<sup>5</sup> Release at 34730.

<sup>6</sup> See the Senate Banking Committee Report that accompanied Senate’s passed version of the Dodd-Frank Act, which served as the “base-text” for the purposes of Dodd-Frank’s bicameral legislative conference. S. Rep. No. 111–176 at 110–12 (2010).

<sup>7</sup> *Id.* p.111.

**dollar threshold.** Of course, the whistleblower does not get any reward if none are collected from the violator.

Congress was so focused on ensuring the SEC Whistleblower Program will amply incentivize and reward whistleblowers that it created a separate, permanent fund at the Treasury for this very purpose. This “Investor Protection Fund” holds upwards of \$300,000,000 million in reserve to be used to amply reward whistleblowers (and an unrelated program for SEC’s Inspector General). The Fund is replenished, up to its \$300,000,000 limit, from monetary sanctions (including any sanctions collected due to a whistleblower’s original information) and various disgorgement funds under SEC’s control **that are unused or undistributed to investors.** However, as the clearest indication of Congress’s intent to not limit the dollar amount a whistleblower can receive, Congress wrote an additional, very specific provision into the funding mechanism of the Investor Protection Fund that would serve as a backstop to the Fund and guarantee that any particular whistleblower is maximally rewarded, even if that award exceeds the Fund’s \$300,000,000 reserves.<sup>8</sup>

After considerable debate both internally and with then-SEC staff working for Chairman Mary Shapiro and the SEC’s Office of General Counsel, the staff of the Senate Committee on Banking wrote into the bill a provision (that remained unchanged through the legislative process) that would guarantee that a whistleblower would receive all he or she is due (within the 10-30% range) of the collected sanctions without regards to the actual dollar amount. This provision stipulates:

“If the amounts deposited into or credited to the Fund...are not sufficient to satisfy an award...there shall be deposited into or credited to the Fund an amount equal to the unsatisfied portion of the award from monetary sanction collected by the Commission in the covered judicial or administrative action on which the award is based.”<sup>9</sup>

This provision simply says that if the Fund does not have enough reserve to satisfy a particular whistleblower award, then the SEC must take a portion of the collected sanctions that is designated for a disgorgement fund or other distribution (*i.e.*, is meant for investors) and award the whistleblower. In other words, a whistleblower’s portion must be satisfied before anyone else, including investors. This of course makes sense: there would be no money but for the whistleblower and there would be no whistleblower but for the incentive of the reward.

To further emphasize Congress’s clear intent, the Committee report accompanying Senate’s version of the Dodd-Frank Act wrote:

“Whenever a whistleblower or whistleblowers tip leads the SEC to collect sanctions and penalties that are determined to be distributed to victims of the fraud, the intent of the Committee is to reward the whistleblower prior to or at

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<sup>8</sup> See 15 U.S.C. 78u-6(g)(3)(B).

<sup>9</sup> *Id.*

the same time as paying such victims, recognizing that were it not for the whistleblower's actions, there would have been no discovery of the harm to the investors and no collection of any sanctions for their benefit."<sup>10</sup>

There can be no doubt that Congress maximally prioritized awarding whistleblowers, even if it meant victims of the fraud would receive marginally less. In other words, Congress specified that the whistleblower must be paid **before** investors, in full (as determined within the statutorily set range of 10-30%), and if this award happened to be more than the reserves of the Investor Protection Fund, that is if the award was more than \$300,000,000, then Congress stipulated that the unsatisfied portion of the award must come from the funds that are apportioned for the investors.

With this clear instruction Congress expressed its unequivocal belief that for maximum investor protection, Congress must reward those who provide the Commission actionable information that lead to detection and stopping of fraud and other investor harm. Congress also saw in its wisdom that to maximally attract whistleblowers, thus reducing the severity of investor harm from ongoing fraud or most effectively deter future fraud by sanctioning violators, Congress needed to send the strongest possible message to whistleblowers by placing their awards and interest ahead of all other consideration.

The Proposal undermines Congress's clear intentions and subverts the purposes of the Program as Congress designed and enacted. By giving itself the discretion to apply dollar threshold as a criterion for an award, the Commission introduces uncertainty, unpredictability, arbitrariness and stinginess into the widely successful program. And the Commission does all of these using the least convincing argument: In the view of this Commission, whistleblowers should be content by the dollar threshold proposed in their Proposal. In addition to being speculative, this Commission is substituting its judgment for the judgment of Congress.<sup>11</sup>

Given Congress's in-depth and considered study of these issues and in contrast to the SEC's history of failure regarding Madoff and other whistleblowers, the Commission should not even think of substituting its judgment here. Moreover, if this Commission were authorized to make such determinations, it raises the inevitable question of what tomorrow's Commission might think of the dollar threshold. Will this proposed level be too high for their liking? That is one of the many good reasons Congress did not authorize the Commission to make such decisions and decided against setting dollar limits at all. Congress intended the Whistleblower Program to be structured as set forth in the statute and expected the Commission to implement it as clearly and unambiguously directed. The Commission should not attempt to supplant its views with the considered judgments of Congress.

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<sup>10</sup> See S. Rep. No. 111-176 at 112 (2010).

<sup>11</sup> The Proposal goes through some length to justify the \$30 million threshold number. The Proposal includes analysis that serves as justification and determination that \$30 million is sufficient income for a lifetime for any whistleblowers. We do not observe the Commission applying similar rigor in generally regulating executive compensation or, at a minimum, the kind of compensation that often leads to reckless risk-taking. The Commission is yet to approve any of the executive compensation clawback provisions of the Dodd-Frank Act. If executives are permitted to earn unlimited compensation – even if this compensation is due to dangerous risk-taking or outright fraud – then whistleblowers who stop fraud and protect investors should be rewarded as appropriately as Congress determined.



The Commission's Interpretation of Independent "Analysis" is Also Contrary to Congress's Express Intent and Understanding, and Would Impermissibly Disqualify Otherwise Meritorious Submissions and Result in More Fraud and Investor Victims

Needlessly introducing another ambiguity that will discourage whistleblowers, again contrary to express Congressional intent, the Commission is suggesting that it is no longer willing to reward whistleblowers who, in addition to their expertise and knowledge, also rely on publicly derived information, and include that information as part of their total submission to the Commission for a reward. In sum, if this provision of the Proposal is approved as released, the Commission would disqualify analysts from becoming whistleblowers.

The Commission is arguing that a "whistleblower's examination and evaluation of publicly available information does not constitute "analysis" if the facts disclosed in the public materials on which the whistleblower relies and in other publicly available information are sufficient to raise an inference of the possible violations alleged in the whistleblower's tip. This is because, where the violations that the whistleblower alleges can be inferred by the Commission from the face of public materials, those violations are not "reveal[ed]" to the Commission by the whistleblower's tip or any purported analysis that the whistleblower has submitted. Rather, in order for a whistleblower to be credited with providing "independent analysis," the whistleblower's examination and evaluation should contribute "significant independent information" that "bridges the gap" between the publicly available information and the possible securities violations."<sup>12</sup>

This hyper-technical reading and baseless claims and speculation are inconsistent with the intent of Congress to do whatever is necessary to incentivize and reward whistleblowers to take huge personal and professional risks to report fraud and protect investors. This is, frankly, a good example of why Congress determined that it would be inappropriate and unwise to delegate much discretion to the Commission in connection with the Whistleblower Program, and further speaks to the Congressional foresight in including a provision that affords judicial review that whistleblowers can seek over almost all of SEC's determinations as it relates to the Whistleblower Program.<sup>13</sup>

The Commission is speculatively claiming that if a whistleblower was able to infer wrongdoing from publicly available information, then the Commission, too, would in due course see, recognize, and analyze this public information and arrive at the same conclusion that investor harm is being perpetrated, and would commence its own enforcement proceedings without needing any help from whistleblowers. This "go-it-alone," "we-got-this, thanks" attitude would be laughable if it was not so serious. The SEC failed to see, recognize, analyze, and act on specific whistleblower information presented to it repeatedly regarding Bernie Madoff's decades-long Ponzi Scheme that cost investors more than \$60 billion. This benighted attitude reflects a broken culture the Dodd-Frank Act aimed to fix by mandating the Whistleblower Program. Congress envisioned that by rewarding and protecting whistleblowers, the Commission would attract valuable contributions, which would in turn augment SEC's own regulatory reach and capabilities

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<sup>12</sup> Release at 34730.

<sup>13</sup> See 15 U.S.C. 78u-6(f).

and help detect and stop fraud that otherwise would go either undetected or, at a minimum, cause more harm to investors for a longer period.

When defining “original information,” Congress specified that so long as the submitted information “is 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,” then the submission should qualify as original information. Obviously, the key determinative word here is “exclusively.”

In the Committee Report, Congress elaborated on the definition of “original information:” Congress intended original information to mean that which is:

“derived from the independent analysis or knowledge of the whistleblower, and is not derived from an allegation in court or government reports, and is not **exclusively** from news media. In circumstances when bits and pieces of the whistleblower’s information were known to the media prior to the emergence of the whistleblower, and that for the purposes of the SEC enforcement [and related actions] the critical components of the information was supplied by the whistleblower, the intent of the Committee is to **require the SEC** to reward such person(s) in accordance with the degree of assistance that was provided.”<sup>14</sup>

With this language, Congress clearly instructed the SEC to not disqualify a submission that contained public information. The exact opposite is true: Congress wanted and instructed the SEC to welcome analysts-*cum*-whistleblowers and reward those who submit original information that leads to recoveries. One of those very kinds of analysts was Harry Markopolos, who neither worked for Madoff nor was any other kind of an insider. Mr. Markopolos was a Certified Financial Analyst who, based on his expertise and publicly available information, conducted rigorous and accurate analysis that demonstrated Madoff’s fraud. If the Commission adopts the “original information” interpretation as released, the Commission would disqualify future Markopoloses and analysts like him, proving that the Commission is acting inconsistent with the statute and Congressional intent.

Finally, Congress did not authorize the SEC to apply the “we too could have figured this out on our own by reading the newspaper” principle to assess the originality of the whistleblower’s submission, or the extent of the independent-ness of the analysis. Quite the contrary, Congress instructed to the SEC to welcome and appreciate the submissions of whistleblowers, and reward them appropriately, even if those submissions include some public information. Frankly, given the Commission’s history with Madoff and others, it should not speculate how flawless it would be in seeing, recognizing, analyzing, and acting on even entirely publicly available information of fraud.

## **CONCLUSION**

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<sup>14</sup> See S. Rep. No. 111–176 at 111 (2010) (emphasis added).



We end where we started: The Whistleblower Program is a wild success as Congress intended and designed it to be. The SEC needs to recognize that, accept it, and let the Program continue to work.

With too much to do and being under-resourced and understaffed, the Commission should be incredibly reluctant to even attempt to “fix” something that is working so well for investors and our markets. If anything, the Commission should be striving to make the Whistleblower Program even more whistleblower and investor-friendly, not ignoring Congress’s express intentions and clear instructions. This Proposal violates the express provisions of the statute and intent of Congress. It should not be approved.

Sincerely,



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