

SEC Whistleblower Program Begins Paying Awards

Steve Berman on Aug. 31, 2012

2012 is quickly shaping up to become The Year of the Scandal on Wall Street – a tall order considering the run of disrepute we've seen from the past decade. One would think that after just four years since the financial crisis that nearly brought our country to its knees, we would have learned some lessons about greed, malfeasance and outright fraud perpetrated on the American people by major financial institutions and publicly traded companies.

One would think. But that's not the way it is playing out.

Take JPMorgan Chase. In May, it stunned investors when it announced the investment house had suffered a \$2 billion loss in trading of complex derivatives called credit-default swaps. If the term credit-default swap sounds familiar, that's because credit-default swaps on home loans played a leading role in causing the recession. I would have hoped JPMorgan's traders would have learned their lesson the first time around.

Then, a week later, Facebook's IPO effectively botched the largest IPO in recent memory, seeding more uncertainty and doubt with already skittish investors. From the start, the offering was delayed and plagued by trading delays and other technical difficulties. Shortly after the IPO, Facebook's stock began to fall, finally settling near 50 percent of its initial value.

Even worse, news reports suggested that Facebook's lead underwriters reduced forecasts for earnings, but rather than making information public, selectively disclosed the information to key investors. Those claims will now be tested in court in a class-action lawsuit filed on behalf of investors who were allegedly left out of the loop.

Now to June: several regulatory agencies announced more than \$450 million in fines against Barclays Bank for attempting to manipulate the London Interbank Offered Rate, or Libor, a key benchmark used to set interest rates on loans in the United States and internationally. While this sounds ethereal and complex, the scandal most likely affected the interest rates the average US consumer paid on mortgages, car loans or even credit cards, costing us billions of dollars in inflated interest rates.

These three scandals suggest that our financial sector is still plagued by corruption, patronage, and secrecy, the factors that brought our economy to the brink just a few years ago.

Once we staggered back from that near economic collapse, lawmakers clamored that we needed to do more in terms of oversight, arming organizations like the SEC with the tools necessary to hold these rogue actors in check.

It was good in theory, but doomed in practice.

The truth is that – no matter how well intentioned the policies – the SEC lacks the funding and personnel to prosecute even a small fraction of the fraud on Wall Street, let alone prevent it. Metaphorically, they are outgunned, and outnumbered.

I am hopeful, however, because the SEC now has a new tool to prosecute fraud – millions of honest, well-intending Americans.

The SEC's new whistleblower program, established last year, offers rewards to those who report fraud and wrongdoing to the agency. These rewards can be significant, totaling up to 30 percent of the funds the government recovers after an SEC enforcement action.

And the program is working - after many appeals and procedural hurdles, the SEC finally announced the first whistleblower award under the program. The whistleblower, who chose to remain anonymous, will receive \$50,000 as a reward for providing information regarding violations of the securities laws.

That might not seem like a lot of money in the grand scheme of things, but the announcement is much more than that – it is the proof-of-concept, a warning if you will, to every CEO that is considering using creative accounting to explain away a loss, or brokerage-house executive who is pondering trading on information he or she received *sub-rosa*. The warning is that if you plan to commit fraud, you better be very good at covering your tracks because now instead of just having to fool an understaffed agency, now you need to deceive every honest person in your organization who now has the power and the incentive to hold you accountable.

My prediction is two-fold.

First, I believe we will see a spate of announcements regarding prosecutions of bad actors, all from laudable actions of whistleblowers. This new program will shine the light of public scrutiny, and scurry they will.

Second, I firmly believe that, thanks to this program, we will see a slow but steady improvement in the behavior by Wall Street, in large part by this virtual oversight.

Whistleblowers should be cautious, however. I would advise any potential whistleblower to speak with an experienced attorney before talking with the SEC. The SEC is receiving several tips each day, and a private whistleblower attorney can help develop your claim so that the SEC is more likely to take your case. You can learn more about our whistleblower practice at www.hb-whistleblower.com.