

Whistleblower Award Update 2015

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There was not much activity from the SEC Office of the Whistleblower (OWB) in the months since it announced the highest whistleblower award to date in September 2014, but that changed in February when it issued a number of denials.

Awards:

In the Matter of the Claim for Award, Exchange Act Rel. No. 72947. On August 29, 2014, the SEC issued its first award under the Dodd-Frank Act to an employee who performed audit and compliance functions. The employee, who had compliance responsibilities, received an award of \$300,000. Generally, information provided to an individual with compliance responsibilities is not considered “original.” Such an employee is entitled to an award, however, if they first report the misconduct to the company and it subsequently fails to take action within 120 days. See 17 C.F.R. §§ 240.21F-4(b)(4)(iii)(B),v(v). This exception applied to the claimant because he reported the conduct to his supervisor 120 days prior to submitting it to the Commission.

In the Matter of the Claim for Award, Exchange Act Rel. No. 73174. In September 2014, the SEC announced a record-breaking whistleblower award of \$30 million. The significance of this award was discussed in a previous blog post.

In the Matter of the Claim for Award, Exchange Act Rel. No. 74404. The SEC did not announce its next whistleblower award until March 2015. This award was the first ever to a former corporate officer who learned of a violation as a result of another employee reporting misconduct through corporate and compliance channels. Typically, officers who learn about fraud through another employee or through a compliance process are not eligible for an award under the whistleblower program. See 17 C.F.R. § 240.21F-4(b)(4)(iii)(A). However, the SEC’s bounty rules provide an exception that makes an officer eligible for an award if he or she provides the information to the SEC more than 120 days after other responsible personnel possessed the information and failed to adequately act on it. See 17 C.F.R. § 240.21F-4(b)(4)(v)(C). The former corporate officer fell within that exception and the SEC awarded the officer between \$475,000 and \$575,000 for reporting original, high-quality information regarding misconduct under the Dodd-Frank Act.

Denials:

In the Matter of Pipeline Trading Systems LLC, Notice of Covered Action 2011-194. Pipeline Trading Systems LLC (“Pipeline”) and two of its top executives agreed to pay \$1 million for the company’s failure to disclose to customers that a majority of orders placed on its “dark pool” trading platform were filled by a trading operation affiliated with Pipeline. The SEC denied the claimant an award because he did not meet the definition of a “whistleblower” under the Exchange Act. (Denial Order Aug. 15, 2014).

In the Matter of the Claim for Award, Exchange Act Rel. No. 72947. On August 29, 2014, the SEC denied an award to a second claimant because the information provided did not lead to the successful enforcement of the covered action and did not contribute to the ongoing investigation.

SEC v. James Roland Dial, Case No. 4.12-CV-01654 (S.D. Tex. 2012), Notice of Covered Action 2012-66. The defendants caused Grifco International Inc. to issue more than 13 million unrestricted securities to themselves and then sold the securities shortly after into a rising artificial market (caused by their dissemination of false and misleading information). The defendants were ordered to pay disgorgement and prejudgment interest. The SEC denied the claimant an award because (1) claimant did not provide “original information” within the meaning of Section 21F(a)(1) of the Exchange Act and Rule 21F-4(b)(1)(iv), (2) the information provided by claimant did not lead to successful enforcement of a covered judicial or administrative action within the meaning of Section 21F(b)(1) of the Exchange Act and Rules 21F-3(a) and 21F-4(c), and (3) claimant was not a “whistleblower” within the meaning of Section 21F(a)(6) of the Exchange Act and Rule 21F-2 because he did not provide information relating to a possible violation of the federal securities laws in accordance with the procedures set forth in Rule 21F-9(a) under the Exchange Act. (Denial Order Feb. 13, 2015).

SEC v. Harbert Management Corporation, HMC-New York, Inc. and HMC Investors, LLC, 12-cv-5029 (S.D.N.Y. 2012), Notice of Covered Action 2012-89. Here, the SEC denied the claimant an award because (1) he did not provide information that led to the successful enforcement within the meaning of Section 21F(b)(1) of the Exchange Act and Rules 21F-3(a)(3) and 21F-4(c), and (2) he failed to submit information in the form and manner that is required under Rules 21F-2(a)(2), 21F-8(a) and 21F-9(a) & (b) of the Exchange Act. (Denial Order Feb. 13, 2015).

SEC v. Kenneth Ira Starr, 10 civ 4270 (S.D.N.Y. 2010), Notice of Covered Action 2012-129. On March 3, 2011, Starr was sentenced to 90 months in prison, ordered to pay more than \$30 million in restitution, and ordered to forfeit more than \$29 million in connection with his misappropriation of investor funds in connection to a series of cases filed against him by the government, which included charges of money laundering, wire fraud, fraud by an investment advisor, and misappropriation of client funds. This specific action arose from Starr’s misappropriation of at least \$8.7 million of his clients’ money. The SEC denied the claimant an award because he or she did not provide information that led to the successful enforcement within the meaning of Section 21F(b)(1) of the Exchange Act and Rules 21F-3(a)(3) and 21F-4(c). (Denial Order Feb. 13, 2015).

SEC v. George Wesley Harris, No. 3:09-cv-01809-M (N.D. Tex. 2009), Notice of Covered Action 2011-206. The Northern District of Texas entered a \$4.8 million judgment against Harris and his co-defendants for operating a fraud scheme that promised returns for investing in oil drilling projects in Texas and New Mexico. The SEC denied the award because (1) claimant did not provide information that led to the successful enforcement within the meaning of Section 21F(b)(1) of the Exchange Act and Rules 21F-3(a) and 21F-4(c), and (2) claimant also did not provide the Commission with original

information within the meaning for Section 21F(b)(1) of the Exchange Act because Claimant's submission was not derived from claimant's independent knowledge or independent analysis. The SEC further noted that the claimant made a false statement on the Form WB-APP, which was signed under penalty of perjury, by stating he or she was "the 44th President of the United States." (Denial Order Feb. 13, 2015).

The OWB denied two other claims, one on February 13, 2015, and one on February 16, 2015, in orders that make it impossible to tell the name or nature of the underlying action. Both claims were denied, however, because the information provided by the whistleblowers did not provide information that led to the successful enforcement of an action within the meaning of Section 21F(b)(1) of the Exchange Act and Rules 21F-3(a)(3) and 21F-4(c). Specifically, the information did not (1) cause the Commission to (i) commence an examination, (ii) open or reopen an investigation, or (iii) inquire into different conduct as part of a current Commission examination or investigation under Rule 21F-4(c)(1) of the Exchange Act; or (2) significantly contribute to the success of a Commission judicial or administrative enforcement action under Rule 21F-4(c)(2) of the Exchange Act.

Finally, the Second Circuit upheld the SEC's denial of an award to a whistleblower who provided information to the SEC before the enactment of the Dodd-Frank Act in July 2010. *Styker v. S.E.C.*, No. 13-4404-ag, 2015 U.S. App. LEXIS 3765 (2d Cir. Mar. 11, 2015). The whistleblower submitted information from 2004-2009 to the SEC, which eventually led to a \$24 million settlement with Advanced Technologies Group. The Second Circuit rejected the whistleblower's argument that the SEC went beyond its congressionally mandated authority, and it deferred to the SEC's interpretation of the law that information submitted prior to July 2010 does not qualify for an award. *Id.* at *8-9.

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