



## SECURITIES & FINANCIAL FRAUD

Enacted as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") on July 21, 2010, the SEC Whistleblower Program is designed to combat securities fraud by rewarding whistleblowers who report violations of the federal securities laws.

Under the SEC Whistleblower Program, an individual who voluntarily provides the SEC with original information regarding a securities violation may receive between 10 and 30% of the total monetary sanctions collected by the SEC, if the original information leads to a successful enforcement action with monetary sanctions over \$1,000,000.

The SEC Whistleblower Program has been effective in uncovering and combatting securities fraud. Since the inception of the Whistleblower Program, the SEC has awarded more than \$1.3 billion in awards to whistleblowers based on enforcement actions that resulted in more than \$6.3 billion in recoveries. In fact, in May 2023, the SEC awarded one whistleblower \$279 million whose information and assistance led to successful enforcement of SEC and related actions.

### **What Type of Fraud is Covered by SEC Whistleblower Program?**

The SEC Whistleblower Program applies to violations of the federal securities laws including the Securities Act of 1933, the Securities Act of 1934, and the Investment Company Act of 1940. Types of fraud covered by the SEC Whistleblower Program include insider trading, Ponzi schemes, stock manipulation, and financial report misstatements.

The SEC Whistleblower Program also rewards individuals who provide the SEC original information about violations of the Foreign Corrupt Practices Act ("FCPA"). The FCPA prohibits American companies and individuals from making payments to foreign officials for the purpose of obtaining, retaining, or directing business to any person.

In addition, with the rise of cryptocurrencies and digital assets in the financial market, the SEC has taken a more active role in combatting fraud involving cryptocurrencies. With the exception of Bitcoin (which is considered to be a commodity), the SEC considers most cryptocurrencies and digital assets to be securities and has taken enforcement actions against companies and individuals for fraud involving the offer and sale of cryptocurrencies and digital assets. These actions often involve fraudulent, unregistered securities sold through "initial coin offerings." The SEC has also taken enforcement actions against large cryptocurrency exchanges, including Coinbase and

Binance, for failing to properly register and operate as security exchanges, and in the case of Binance, for fraud.

According to the SEC Office of the Whistleblower's Annual Report to Congress, in 2022, the most common categories of fraud reported by whistleblowers were Manipulation (21%), Offering Fraud (17%), Initial Coin Offerings and Cryptocurrencies (14%), and Corporate Disclosures and Financials (13%).

### **Who Qualifies as a Whistleblower?**

An individual is eligible for an award under the SEC Whistleblower Program, if he or she voluntarily provides original information to the SEC about a possible securities violation and that information leads to a successful enforcement action. Corporations and organizations are not eligible to be whistleblowers under the program. However, an individual does not need to be a U.S. citizen or resident to be a whistleblower under the SEC Whistleblower Program.

Whistleblowers may qualify for an award even without direct knowledge of the fraud as they may base their report on independent analysis of public information.

The SEC considers a whistleblower's submission "voluntary" if the whistleblower provides the information to the SEC before the SEC or other relevant authority (such as Congress or FINRA) requests or demands information from the whistleblower (or whistleblower's attorney) relating to that submission. A submission is not considered voluntary if the whistleblower was already under a pre-existing legal or contractual duty to disclose the violation to the SEC.

For information to be original, it must be:

- (i) Derived from the whistleblower's knowledge or independent analysis;
- (ii) Not already known to the Commission from any other source, unless the whistleblower is the original source of the information;
- (iii) 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, unless the whistleblower is a source of the information; and
- (iv) Provided to the Commission for the first time after July 21, 2010.

To be an "original source", the whistleblower must either have originally provided the information that the SEC obtains from other sources regarding the alleged fraud or have information that is (1) derived from the whistleblower's independent knowledge or independent analysis and (2) that materially adds to information that the SEC has already obtained from other sources.

### **Can a Whistleblower Remain Anonymous?**

Yes. However, the whistleblower can only remain anonymous by authorizing an attorney to file a case on their behalf.

### **What Types of Fraud are Covered by the SEC Whistleblower Program**

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Whistleblower Program include:

**PONZI SCHEMES** – A type of investment fraud that involves the payment of purported returns to existing investors from funds obtained from new investors. Organizers often solicit new investors by promising high returns with little or no risk.

**PYRAMID SCHEMES** – A type of investment fraud where participants attempt to make money solely by recruiting new participants into the program.

Usually there is a promise of high returns for simply handing over your money to the program's organizers and getting others to do the same.

**MANIPULATION** – Intentional conduct designed to deceive investors by controlling or artificially affecting the market for a security. Methods include: (i) spreading false or misleading information about a company; (ii) improperly limiting the number of publicly-available shares of a company; and (iii) rigging quotes, prices or stock trades to create a false picture of the demand for a security.

**INSIDER TRADING** – Buying or selling a security in breach of a fiduciary duty or other relationship of trust and confidence, while in possession of material, nonpublic information about the security. This conduct also includes “tipping” such material, nonpublic information to others who then trade on that information.

**OFFERING FRAUD** – The SEC requires companies to register with the SEC and disclose important financial information, descriptions of a company's business operations, its management and the securities it is offering to the investing public. The failure to register with the SEC without a valid exemption form registration, or making material misstatements or omissions in registration documents constitutes offering fraud.

**VIOLATIONS OF THE FOREIGN CORRUPT PRACTICES ACT (FCPA)** – A company's failure to put internal controls into place to detect and prevent payments and gifts to officials from foreign governments in order to obtain advantageous business opportunities for the company in that country.

**ACCOUNTING FRAUD** -The intentional misrepresentation or alteration of accounting records regarding sales, revenues, expenses and other factors for a profit motive such as inflating company stock values, obtaining more favorable financing or avoiding debt obligations.

### **How to Make a Submission Under the SEC Whistleblower Program**

Unlike cases brought under the False Claims Act, whistleblowers do not file a complaint in federal court to initiate an SEC Whistleblower action. Instead, whistleblowers must provide the SEC with the details and evidence of the alleged securities violation by completing and filing an SEC Form TCR with the SEC Office of the Whistleblower.

If you would like to speak to a member of our whistleblower group about a potential whistleblower matter, please contact us to schedule a case evaluation. All case evaluations are confidential and free.