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COMMODITY FUTURES TRADING COMMISSION

CFTC Whistleblower Office Poised to Make First Monetary Award in 2014, Director Says



By Stephen Joyce

April 1 — The number of tips alleging Commodity Exchange Act violations that were submitted to the Commodity Futures Trading Commission's nascent whistle-blower program has significantly increased since October, as information about the program continues to spread among market participants and others, CFTC Whistleblower Office Director Christopher Ehrman told Bloomberg BNA.

While the program hasn't made any monetary awards to any whistle-blowers to date, Ehrman said many high-quality tips have been investigated by the agency's enforcement division and that "a few awards" will probably be made before Sept. 30, the end of the current fiscal year. "I think that's where we're headed," he said.

Ehrman, the office's second director since the unit was created by Section 748 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub. L. No. 111-203), said his vision for his office is grounded in several individual tasks centered on enhancing its profile and exposure, while improving its outreach to actual or potential whistle-blowers. "It's a work in progress," he said.

The whistle-blower program is "going to gain traction over time, and it's an important focus of the overall enforcement program."

Stephen Humenik, Covington & Burling LLP

Practitioners interviewed for this report agreed. "It's a new program," said Stephen Humenik, of counsel at Covington & Burling LLP in Washington. "It's going to gain traction over time, and it's an important focus of the overall enforcement program. Because

there will be important resources directed to it, it will be used."

"The verdict is not in on the program's effectiveness yet," Wilmer Cutler Pickering Hale & Dorr LLP partner Dan Berkovitz said in a March interview. "It is still in the early stages of implementation. I think you have to look at this in a longer time frame to see how the program works," said Berkovitz, who was the CFTC general counsel when the agency's whistle-blower program was created.

Implementing the Statute

On Aug. 4, 2011, the commission voted 4-1 to approve a final rule implementing the part of Dodd-Frank creating the whistle-blower unit, following a May 25, 2011, vote by the Securities and Exchange Commission to set up its own whistle-blower program, which was also created by Dodd-Frank (43 SRLR 1658, 8/8/11)(43 SRLR 1113, 5/30/11).

The final rules require the CFTC to pay an award, subject to certain limitations, to eligible whistle-blowers who voluntarily provide the CFTC with original information about a violation of the Commodity Exchange Act that leads to the successful enforcement of a covered judicial or administrative action or a related action resulting in monetary sanctions exceeding \$1 million. Whistle-blowers are eligible to receive between 10 percent and 30 percent of the sanction.

The CFTC rules took effect Oct. 24, 2011.

At the time the final rule was approved, many regulated companies opposed it because it allowed, and still allows, whistle-blowers to bring tips directly to the CFTC's attention without first reporting the purported wrongdoing to a company's internal compliance team.

"We are still hearing from them," Ehrman said. "I think they're not as loud as they were before. The pitchforks and torches seem to have been set aside."

From Nothing, Something

Unlike the SEC, which had a rarely used and narrowly focused whistle-blower program in place before Dodd-Frank, the CFTC had to create its program from scratch.

BNA Snapshot

CFTC Whistleblower Office

Key Development: After Dodd-Frank required that office be created from ground up, CFTC may grant first award in fiscal 2014.

Next Steps: CFTC must complete annual report on CFTC Whistleblower Office activity to Congress; it is expected to be completed in early April.

Initially the office was placed within the CFTC's Office of the Executive Director, but in the summer of 2012, around the time Ehrman arrived as director, it was moved to the agency's enforcement division.

Ehrman, a staff attorney and a paralegal currently populate the CFTC Whistleblower Office, which is located at CFTC headquarters in Washington. Ehrman said he plans to post job openings for a deputy and an additional paralegal over the next few months, "because we're getting busier and busier and we're running out of resources."

While the director of the office enjoys a fair degree of autonomy, his office also has to operate within the agency's overall bureaucracy for administrative purposes.

Dodd-Frank requires the CFTC to submit a report to Congress each year no later than Oct. 30, detailing, among other items, the number of awards granted, the types of cases that resulted in awards, balances related to the Customer Protection Funds and audited financial statements.

While the CFTC didn't submit a report by Oct. 30, 2013, an agency spokeswoman said in a March 31 statement that the report was delayed due to some key personnel departures, including that of Gary Gensler, the agency's former chairman, and David Meister, its former enforcement division director. The report is expected to be sent to Congress in early April, she said in her statement. The agency's initial report detailing its whistle-blower program and consumer education initiatives, issued in October 2012, contained information on the number of whistle-blower tips received since the program's inception and described the agency's consumer-protection improvement goals.

Modest Cost

Other elements of the CFTC whistle-blower program include the three-member Whistleblower Award Determination Panel that decides if and how much money to award whistle-blowers, and a Customer Protection Fund, established by Dodd-Frank to disburse approved whistle-blower monetary awards. The fund, replenished by monetary sanctions imposed by the CFTC enforcement division, held about \$275 million as of March 31.

The program has the potential to give the CFTC an effective enforcement tool at "a relatively modest cost to the agency," Norton Rose Fulbright LLP partner Terry Arbit, a former CFTC deputy general counsel for legislative and intergovernmental affairs, said in a statement sent to Bloomberg BNA.

The Government Accountability Office determined in Aug. 8, 2011, and Nov. 8, 2013, decisions, in response to CFTC queries, that the Customer Protection Fund may be used to pay the administrative and personnel costs of the CFTC Whistleblower Office, including travel expenses (45 SRLR 2149, 11/18/13).

"This spares the CFTC from having to fund these costs of the Whistleblower Program from its general appropriation," Arbit said in his statement. CFTC Whistleblower Office administrative expenses for fiscal 2013 totaled \$459,000 and are estimated to rise to \$750,000 in fiscal 2015, according to a March 5 Obama administration budget and performance plan for the CFTC (46 SRLR 456, 3/10/14).

First Awards on the Way?

Since the program began, the CFTC has issued 25 award determinations. Each determination denied whistle-blowers awards. That may change in the near future.

In fiscal 2013, which ended Sept. 30, the CFTC Whistleblower Office received 139 tips, complaints or referrals reported on Forms TCR, the document whistle-blowers file with the CFTC under the program. During the current fiscal year, Ehrman's office received 110 Forms TCR as of March 21, an annualized increase in whistle-blower tips of about 38 percent.

And while the March 5 Obama administration plan estimated about 20 claims for awards would result from whistle-blower tips, the CFTC received 28 such requests during the first half of fiscal 2014.

"Things are really ramping up now," Ehrman said.

Indeed, Ehrman said he hopes several awards can be made before Sept. 30. "I can see, hopefully, some real movement this year, before the fiscal year ends, with a few awards coming out," he said. "I'm pretty comfortable we're going to get out of the gate this year," he said.

Agency Award Predictions

The agency, the March 5 budget plan said, would pay \$10 million in awards no later than Sept. 30 and pay out another \$10 million in fiscal 2015.

Humenik predicted claims will probably exceed that estimate. "It seems like their numbers might be low," he said.

"Because no historical data exists to substantiate the estimated amount of whistleblower awards," the Obama administration report said, "the \$10 million amount above is simply a conservative placeholder amount to account for the possibility of large judgments in the period that may be associated with information provided by whistleblowers."

The quality of the whistle-blower tips his office receives is "very good," Ehrman said, further describing them as specific, timely, and credible. The CFTC Whistleblower Office collects and processes the tips before forwarding

them to the agency's enforcement division. The office does not review the allegations contained in the tips, though the office may advise the determination panel.

No Insight into Process

A key anticipated development in the program, practitioners said, will be what the CFTC discloses, or elects not to disclose, in any award final order.

"It will be interesting to see the first [award] and what it says and what it doesn't say," Humenik said. "I think there will be a reaction to it based on the perspective brought to the table, whether it's the defense bar or consumer advocacy groups."

"The orders that the Commission issues are typically very redacted to protect the confidentiality of the whistleblower. They will say that a person or persons met the requirements provided in the rules and were paid a certain amount of money. Identities and exact percentages are redacted," CFTC spokeswoman Donna Faulk-White said.

Humenik, who leads Covington's futures and derivatives practice from its Washington office and is a former CFTC enforcement division senior trial attorney, predicted the agency won't disclose a great deal of information in award determinations, and—to protect the whistle-blower's identity—determinations might not be publicly associated or linked with the CFTC enforcement action that led to the whistle-blower award, he said.

"More questions will be raised than answers simply because there's not a lot of information in that settlement order to begin with," said Humenik, who also served as a policy adviser to current CFTC member Scott O'Malia.

A better outcome for the regulated community would be the release of a detailed description of the enforcement action and the whistle-blower's actions, Humenik said. Additional information about such cases could help drive compliance because companies then would know the types of violative behavior the CFTC is trying to curtail through enforcement actions, he said.

The CFTC rules state that whistle-blowers have 90 days from the date a final order is posted on the CFTC website to file a claim for an award. Any final order issued by the CFTC relating to an award may be challenged in federal appellate court not more than 30 days after the final order of the CFTC is issued, the rules state.

SEC Program Comparison

Comparisons between the whistle-blower programs at the CFTC and SEC should consider their material differences in scope and size, Ehrman and others said. The SEC program not only was set up before the CFTC program but covers many more possible violative activities; the CFTC program applies only to violations of one law. "Their footprint is significantly larger than ours," Ehrman said.

Also, Ehrman said the CFTC's enforcement function does not have the resources to match the SEC enforcement division. "If we had a significantly larger enforcement division, things would be moving along quicker," he said.

CFTC whistle-blower cases may also take more time to develop because of the complexity of the activities the CFTC oversees—complicated derivatives products—relative to some services and products supervised by the SEC, Ehrman said. That means it is possible that cases the CFTC began to investigate immediately following implementation of the program will be completed in the near term.

While the CFTC final rule explicitly stated that it tried to hew closely to the SEC final rule, there are a few differences between the two programs. First, both rules contain anti-retaliation provisions in an effort to protect whistle-blowers from being punished by employers; however, the CFTC will not join a whistle-blower in any judicial proceeding while the SEC may, Ehrman said.

Second, the SEC rule prohibits anyone from impeding the flow of data from a whistle-blower to the SEC, and the SEC's rule states it may launch an enforcement action against any entity that tries to impede that information flow, including permanently barring a lawyer who drafts a document to effectuate such an impediment from practicing before the SEC. While the CFTC "takes a dim view" of such practices, the CFTC would not be likely to duplicate the SEC's strategy, Ehrman said.

It's possible that a single violative action could fall within the jurisdiction of both CFTC and SEC whistle-blower programs. Lawyers had differing views about whether an award could or would be granted by both the SEC and CFTC when it involved the same violation.

Standing Up Agency

Ehrman spent 14 years at the SEC before assuming his current CFTC responsibilities July 16, 2012. At the SEC, he worked as an enforcement division staff attorney, senior counsel, branch chief and an assistant director. His work at the SEC "translated perfectly to what I do here at the CFTC," he said. Ehrman has also worked in the private sector as a lawyer.

During his first days at the commission Ehrman said he tried to "speak less and listen more" to acclimate to his new agency, especially after spending 14 years at the SEC. First tasks included assuring the adequacy of existing policies and procedures and then speaking to internal and external groups to familiarize them with the program and its aims, a task that continues.

"Getting the word out," as Ehrman calls it, has included not only visiting the agency's regional office in Chicago and appearing as a panelist at conferences but attending trade shows as well, where he occasionally hands out whistles. About once a month, he hosts for CFTC personnel a breakfast of coffee and bagels.

Ehrman isn't satisfied with his office's Web page and is currently working with the agency's technical specialists to revamp the site. "I'm not happy with where that is, so I'm now working with our tech folks to build a separate, free-standing page that will be connected to the CFTC website to really make it a kinder, friendlier, more commercial looking page than we have now," he said.

The office's first director, Vincente Martinez, was named to that post Jan. 6, 2012. A staff attorney and paralegal were hired along with Martinez as the initial CFTC Whistleblower Office employees; Martinez subsequently left to become the SEC Office of Market Intelligence chief in January 2013.

Ehrman said the increase in tips and anticipated awards illustrate that the program, though in its infancy, is enjoying some success. And while the anticipated expansion of his office's staff may be sufficient for the time being, those additional resources will not be enough for what he has envisioned for his agency's whistle-blower efforts over the longer term.

"We have enough, but we need more for where we're going," he said.

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For More Information

A detailed description of the CFTC's whistle-blower rules is at <http://www.gpo.gov/fdsys/pkg/CFR-2012-title17-vol1/pdf/CFR-2012-title17-vol1-part165.pdf> or <http://www.cftc.gov/ucm/groups/public/@whistleblowernotices/documents/file/whistleblowerrules17cfr165.pdf>

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