

Expert Analysis

## Whistle-Blower Bounties May Encourage Residential Mortgage-Backed Securities Fraud Reporting

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The False Claims Act, 31 U.S.C. § 3729, which has been around since the Civil War, permits whistle-blowers with information about fraud perpetrated upon the U.S. government to bring civil fraud suits on behalf of the United States and share in the recovery. While much attention is paid to the multibillion-dollar payments the Department of Justice has recovered in suits against big pharmaceutical companies, whistle-blowers are increasingly targeting financial services companies with FCA *qui tam* suits. For example, when the DOJ announced the settlement with five of the nation's largest mortgage servicers, a group of whistle-blowers walked away with more than \$46 million. And, in a civil fraud lawsuit against a mortgage lender announced earlier this year, a single whistle-blower earned \$31.6 million.<sup>1</sup> These staggering amounts will surely motivate other whistle-blowers and put wind in the sails of the plaintiffs' bar.

But the FCA is not the only federal law the DOJ is using to pursue financial fraud. Moreover, it is not the only federal law that rewards people who report financial fraud to the DOJ. Increasingly, the DOJ has brought claims against financial institutions under the Financial Institutions Reform, Recovery and Enforcement Act of 1989.<sup>2</sup> FIRREA has been cited with increasing frequency in the DOJ's civil fraud suits against financial institutions following the economic crisis.<sup>3</sup>

FIRREA authorizes the DOJ to sue for civil penalties when a person violates certain enumerated criminal laws, including mail, wire and bank fraud. Penalties can be awarded up to \$1 million per violation or \$5 million for a continuing violation, and a court can award greater penalties when the amount of the gain or loss from the fraud is higher than that.<sup>4</sup> Unlike the FCA, FIRREA does not require the federal government to be the victim of the fraud. This factor gives FIRREA a broader reach than the FCA.

Given the DOJ's increasing use of FIRREA in financial fraud cases, it is unsurprising that both the agency and the plaintiffs' bar have been raising awareness of a previously obscure federal law designed to encourage people to come forward with

information that can lead to such cases. The Financial Institutions Anti-Fraud Enforcement Act of 1990, enacted the year after FIRREA, entitles a whistle-blower to share in the government's recovery in a FIRREA lawsuit.<sup>5</sup> The DOJ's Financial Fraud Enforcement Task Force recently made it a point to publicize FIAFEA in connection with its newly established Residential Mortgage-Backed Securities Working Group, which is tasked with investigating "those responsible for misconduct attributable to the mortgage crisis through the pooling and sale of residential mortgage backed securities."<sup>6</sup>

On its Stop Fraud website, the DOJ invites people to report RMBS fraud that violates FIRREA by submitting evidence in the form of sworn statements.<sup>7</sup> Although the task force also cites the FCA as a possible remedy to address RMBS fraud, FIRREA seems the far more natural fit for such cases since fraud involving mortgage securities is more likely to victimize private investors than the federal government.

The rewards available under FIAFEA are significantly smaller than those available under the FCA. Under the FCA, a plaintiff can receive between 15 percent and 25 percent of the government's recovery in cases where the United States intervenes, and between 25 percent and 30 percent in cases where intervention is declined.<sup>8</sup> Such awards are comparable to those available under the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, to individuals who report securities fraud to the Securities and Exchange Commission. Such persons can receive between 10 percent and 30 percent of the SEC's recovery.<sup>9</sup>

Under FIAFEA, awards are not as generous: The whistle-blower is entitled to between 20 percent and 30 percent of the first \$1 million recovered, between 10 percent and 20 percent of the next \$4 million recovered and between 5 percent and 10 percent of the next \$5 million recovered.<sup>10</sup> Thus, whistle-blower awards in FIRREA suits are effectively capped at \$1.6 million (*i.e.*, 30 percent of \$1 million [\$300,000] plus 20 percent of the next \$4 million [\$800,000], plus 10 percent of the next \$5 million [\$500,000]). The cap applies even if more than one whistle-blower provides information leading to a recovery — in that event, the U.S. attorney general apportions the award between the whistle-blowers at his discretion.<sup>11</sup>

Despite the DOJ's recent resurrection of FIRREA as an enforcement tool in financial fraud cases, the agency hasn't announced any whistle-blower awards for reporting a violation. But the DOJ's rediscovery of FIRREA and its recently announced pursuit of RMBS fraud cases suggests it's still early. It remains to be seen how the courts and the DOJ will apply these whistle-blower provisions, and whether FIAFEA whistle-blower awards will inspire reporting of RMBS fraud as effectively as the FCA inspired reports of health care fraud.

Regardless of how the statute is applied in practice, the availability of seven-figure rewards for reporting financial fraud to the DOJ gives whistle-blowers more incentive to notify outside authorities rather than management. Such incentive make it essential for companies to develop, maintain and monitor compliance programs that not only respond quickly, credibly and effectively to internal reports of fraud, but that also promote robust internal auditing capable of spotting and fixing problems before the whistle is blown.

## NOTES

<sup>1</sup> Stipulation and Order of Settlement and Release Between the United States of America and the Relator, *United States v. Citigroup Inc.*, No. 11-Civ.-5473 (S.D.N.Y. Feb. 15, 2012) at 2.

<sup>2</sup> 12 U.S.C. § 1833a.

- <sup>3</sup> See, e.g., *United States v. Bank of Am. Corp. et al.*, No. 1:12-cv-00361 (D.D.C. Mar. 12, 2012); *United States v. CitiMortgage Inc.*, No. 1:11-cv-05473 (S.D.N.Y. Feb. 16, 2012); *United States v. Allied Home Mortgage Corp.*, No. 1:11-cv-05443 (S.D.N.Y. Nov. 4, 2011); *United States v. Bank of N.Y. Mellon Corp.*, No. 1:11-cv-06969 (S.D.N.Y. Oct. 4, 2011). See also, Andrew Schilling, *Understanding FIRREA's Reach: When Does Fraud 'Affect' a Financial Institution?* BNA BANKING REPORT, 99 BBR 186 (July 24, 2012).
- <sup>4</sup> 12 U.S.C. § 1833a(b)(1), (2) & (3).
- <sup>5</sup> 12 U.S.C. § 4205.
- <sup>6</sup> <http://www.stopfraud.gov/iso/opa/stopfraud/2012/12-ag-120.html>.
- <sup>7</sup> <http://www.stopfraud.gov/rpt-ag.html>.
- <sup>8</sup> 31 U.S.C. § 3730(d).
- <sup>9</sup> [http://www.sec.gov/about/offices/owb/owb-faq.shtml#P21\\_5971](http://www.sec.gov/about/offices/owb/owb-faq.shtml#P21_5971).
- <sup>10</sup> 12 U.S.C. § 4205(d)(1)(a)(i).
- <sup>11</sup> 12 U.S.C. § 4205(d)(2).



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