

# CREW | citizens for responsibility and ethics in washington

March 18, 2015

## BY HAND DELIVERY

The Honorable John Thune  
Chairman  
The Honorable Bill Nelson  
Ranking Member  
Committee on Commerce, Science  
and Transportation  
U.S. Senate  
254 Russell Senate Office Building  
Washington, DC 20510

The Honorable Fred Upton  
Chairman  
The Honorable Frank Pallone  
Ranking Member  
Energy and Commerce Committee  
U.S. House of Representatives  
2125 Rayburn House Office Building  
Washington, DC 20515

Dear Chairmen Thune and Upton and Ranking Members Nelson and Pallone:

Citizens for Responsibility and Ethics in Washington (CREW) requests that the Senate Committee on Commerce, Science and Transportation, and the House Committee on Energy and Commerce investigate the ways short sellers are manipulating the government regulatory process for personal financial gain. Publicly available data, as well as documents CREW obtained through Freedom of Information Act requests, indicate this is a growing problem, likely occurring more frequently than currently known.

Through our research we have identified at least three individuals who have misused the regulatory process for financial gain. Each is discussed below.

*William Ackman*

William Ackman and his hedge fund, Pershing Square Capital Management, have gone to unprecedented lengths to urge federal regulatory action against Herbalife, Inc., a company in which Mr. Ackman and his fund have maintained a significant short position. As the *New York Times* reported last year, Mr. Ackman has made an "extraordinary attempt to leverage the

corridors of power – in Washington, state capitols and city halls – for his hedge fund’s profit”<sup>1</sup> after making a \$1 billion bet against Herbalife that pays off only if the company’s stock plummets.

Knowing regulatory action against Herbalife would drive the stock price down, Mr. Ackman pulled out all the stops to push for such action. As Mr. Ackman himself said, he just needed to get any one of “the SEC, the FTC, the 50 attorney generals around the country, the equivalent regulators in 87 countries,” interested in investigating to succeed in driving the price down.<sup>2</sup>

To pressure state and federal regulators to investigate Herbalife, Mr. Ackman presented research to the New York field headquarters of the SEC, suggesting the commission conduct an investigation into whether Herbalife was misleading investors.<sup>3</sup> More troubling, his team organized letter-writing campaigns to the FTC as well as state attorneys general. Some who wrote letters later told the *New York Times*, they had no recollection of doing so.<sup>4</sup> Mr. Ackman enlisted allies, including the Hispanic Federation, the League of United Latin American Citizens, and the National Consumers League to write letters, keeping Pershing Square’s involvement quiet while, at the same time, issuing press releases to note each new group’s call for investigation.<sup>5</sup> In fact, the *Times* found, Mr. Ackman paid civil rights organizations at least \$130,000 to join his attack against the company.<sup>6</sup>

In addition, *ABC News* reported Mr. Ackman secretly agreed to pay Giovanni Bohorquez, a former Herbalife employee, \$3.6 million over ten years if he lost his job after providing negative information about the company.<sup>7</sup> Mr. Ackman used Mr. Bohorquez to “generate negative news reports about the company and prod state and federal agencies to investigate the company.”<sup>8</sup>

Further, Mr. Ackman’s lawyer, Steve Holley at Sullivan and Cromwell, regularly contacted Lois Greisman, the Associate Director of the Division of Marketing Practices at the

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<sup>1</sup> Michael S. Schmidt, Eric Lipton and Alexandra Stevenson, After Big Bet, Hedge Fund Pulls the Lever of Power, *New York Times*, March 9, 2014 (attached as Exhibit A).

<sup>2</sup> *Id.*

<sup>3</sup> *Id.*

<sup>4</sup> *Id.*

<sup>5</sup> Schmidt, Lipton and Stevenson, *New York Times*, Mar. 9, 2014.

<sup>6</sup> *Id.*

<sup>7</sup> Matt Mosk and Brian Ross, Bill Ackman’s Secret \$\$ Deal for Herbalife Whistleblower, *ABC News*, April 22, 2014 (attached as Exhibit B).

<sup>8</sup> *Id.*

FTC, with emails attaching articles and blog posts critical of Herbalife – many of which appear to have been ginned up by Mr. Ackman or his supporters.<sup>9</sup>

Using these same manipulation tactics, Mr. Ackman also persuaded Rep. Linda Sanchez (D-CA) and Sen. Edward J. Markey (D-MA) to send letters to the FTC and SEC requesting investigations of Herbalife.<sup>10</sup> Similarly, state attorneys general in Nevada, Connecticut, and California received numerous letters from various non-profits and local politicians – with nearly identical language – demanding investigations into Herbalife.<sup>11</sup>

Additionally, on at least one occasion, a government official appears to have given advance information to *New York Post* reporter Michele Celariar, who has provided Mr. Ackman and his battle against Herbalife favorable coverage. In response to its FOIA request of the FTC, CREW received an email from agency attorney Christine Todaro, commenting on an attached article by Ms. Celariar discussing a meeting scheduled between the FTC and Hispanic organizations to discuss Herbalife. Ms. Todaro stated, “I find it interesting that the story says Jessica may attend because I didn’t tell Sally until that morning.”<sup>12</sup> “Jessica” is identified in the *Post* piece as Jessica Rich, the director of the FTC’s Bureau of Consumer Protection.<sup>13</sup>

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<sup>9</sup> See e.g., Email from Steven Holley to Lois Greisman, November 13, 2013 (attaching blog post by Brent Wilkes, Executive Director of the League of United Latin American Citizens critical of Herbalife); email from Steven Holley to Lois Greisman, October 28, 2013 (attaching post on website *Seeking Alpha* by Matt Stewart – who also was shorting Herbalife – agreeing with Mr. Ackman’s claim that Herbalife is a pyramid scheme); email from Steven Holley to Lois Greisman, October 17, 2013 (attaching post by Dan McCrum on the *Financial Times*’ blog *Alphaville*, regarding the a California court’s denial of a motion to dismiss in *Bostick v. Herbalife*, a lawsuit against Herbalife by a former salesman); email from Steven Holley to Lois Greisman, October 15, 2013 (explaining California court decision); email from Steven Holley to Lois Greisman, October 14, 2013 (attaching post by Dan McCrum on *Alphaville* criticizing Herbalife’s distribution network); email from Steven Holley to Lois Greisman, September 25, 2013 (attaching post by Dan McCrum on *Alphaville* regarding the FTC and Herbalife); email from Steven Holley to Lois Greisman, August 16, 2013 (attaching post by Dan McCrum on *Alphaville* regarding Herbalife’s distribution network); email from Steven Holley to Lois Greisman, June 18, 2013 (attaching Pershing Square press release on Herbalife); email from Steven Holley to Lois Greisman, June 6, 2013 (attaching and explaining letter detailing “serious economic harm being inflicted on U.S. consumers by Herbalife); email from Steven Holley to Lois Greisman, May 10, 2013 (attaching article from Israeli website *Haaretz* regarding Herbalife’s recruitment of distributors there); email from Steven Holley to Lois Greisman, March 27, 2013 (attaching article published on *The Verge* regarding lead generation businesses associated with Herbalife); email from Steven Holley to Lois Greisman, March 19, 2013 (attaching post by Matt Stewart on *Seeking Alpha* claiming Herbalife is not a legitimate business); email from Steven Holley to Lois Greisman, February 7, 2013 (attaching statement of gross compensation for Herbalife’s distributors and critical commentary on *Seeking Alpha*) (emails collectively attached as Exhibit C). Mr. Holley also sent Ms. Greisman at least two letters, one on June 5, 2013 enclosing the complaint in *Bostick*, and one on October 1, 2013, enclosing a bankruptcy petition filed by an Herbalife distributor and his wife) (letters, without enclosures, attached as Exhibit D).

<sup>10</sup> Schmidt, Lipton and Stevenson, *NY Times*, Mar. 9, 2014.

<sup>11</sup> *Id.*

<sup>12</sup> Email from Christine Todaro to Lois Greisman, Janet Ammerman, Monica Vaca and Roberto Anguizola, Re: FYI: NY post story re Herbalife, July 15, 2013 (attached as Exhibit E).

<sup>13</sup> Michele Celariar, Groups, FTC to Talk Herbalife Probe, July 12, 2013 (attached as Exhibit F).

This is not the first time Mr. Ackman has enlisted outside assistance to drive down a company's stock price for his personal financial benefit. In deposition testimony, Mr. Ackman, then running the hedge fund Gotham Partners, explained to the SEC he had released an advance copy of a report he had prepared on MBIA Inc. to the *Wall Street Journal* "to expose the facts in MBIA. And we thought that would lead to – we would profit by virtue of the investment we had taken."<sup>14</sup> Mr. Ackman also reached out to the New York State Insurance Department believing the agency "might shut down MBIA and that would certainly help our investment."<sup>15</sup> To the same end, Mr. Ackman sent an email to Alice Schroeder, then a well-respected insurance industry analyst at Morgan Stanley. Mr. Ackman testified he believed if he could convince Ms. Schroeder he was right about MBIA, "it would be very valuable" to him, stating "It would help me a lot if someone – some third party, particularly someone perceived as more objective than I am, adopted our views."<sup>16</sup> According to Mr. Ackman, Ms. Schroeder responded cautiously, leaving him a voice mail saying she was averse to being part of a market manipulation scheme.<sup>17</sup>

It now appears that Mr. Ackman's campaign against Herbalife is the subject of a Department of Justice inquiry. Last week, the *Wall Street Journal* reported federal prosecutors have conducted interviews and issued subpoenas aimed at determining whether people hired by Mr. Ackman made false statements about Herbalife to federal regulators to instigate government investigations into the company and lower its stock price.<sup>18</sup>

The SEC's response to a FOIA request submitted for "records of certain investment/trading activity" regarding Pershing Square, Herbalife and/or Mr. Ackman from December 1, 2012 through February 15, 2013,<sup>19</sup> suggests the SEC also may be investigating Mr. Ackman for his actions with respect to Herbalife. The agency relied on FOIA exemption 7(A), a provision allowing agencies to withhold records compiled for law enforcement purposes, to withhold responsive documents.<sup>20</sup> While Mr. Ackman and Pershing Square may have engaged in illegal market manipulation, an issue appropriate for both DOJ and SEC investigation, the question of whether Mr. Ackman – among others – has attempted to manipulate federal regulators and even members of Congress to move the price of stock in which he has an interest should be of concern to this Committee and the Congress as a whole.

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<sup>14</sup> Deposition of William Ackman, In the Matter of Gotham Partners Management Company, LLC, p. 215, June 5, 2003 (relevant pages attached as Exhibit G).

<sup>15</sup> *Id.* at 221.

<sup>16</sup> *Id.* at 260.

<sup>17</sup> *Id.*

<sup>18</sup> Christopher M. Matthews, Prosecutors Interview People Tied to Ackman in Probe of Potential Herbalife Manipulation, *Wall Street Journal*, March 12, 2015 (attached as Exhibit H).

<sup>19</sup> Letter from SEC FOIA Branch Chief Dave Henshell to Jeffrey Gardner, March 18, 2013 (attached as Exhibit I).

<sup>20</sup> *Id.*

*Steven Eisman*

In 2011, CREW brought to the attention of the SEC and the Department of Education short seller Steven Eisman's efforts to influence government action against the for-profit college industry to drive down their stock price. As CREW explained, in June 2010, Mr. Eisman, then a hedge fund manager for FrontPoint Financial Services Fund, presented a scathing attack on the for-profit education industry in testimony before the Senate Committee on Health, Education, Labor and Pensions.<sup>21</sup> After Mr. Eisman's testimony, the stock price of for-profit colleges fell – just as it had several weeks earlier when Mr. Eisman criticized the industry at the Ira Sohn conference.

At the time, the Department of Education was considering a so-called “gainful employment regulation,”<sup>22</sup> which if enacted would have resulted in a significant decline in the stock value of for-profit colleges. Through Freedom of Information Act requests, CREW discovered that beyond his congressional testimony, Mr. Eisman had been working with Education officials on the proposed regulation. For months, Mr. Eisman and others at FrontPoint corresponded with Education officials, sometimes providing news clips and other times offering substantive analysis of the for-profit industry to suggest specific regulatory language.<sup>23</sup>

Like Mr. Ackman, Mr. Eisman formed alliances with non-profit organizations, enlisting them to urge government action. These groups, which significantly influenced Education, kept Mr. Eisman abreast of developments. As a result of his relationship with the non-profits, Mr. Eisman may have received an advance copy of the regulations prior to their July 23, 2010 release, but almost certainly was aware they were about to be released.<sup>24</sup>

As someone neither regulated nor affected by the regulations, it appears Mr. Eisman injected himself into the agency's process for the sole purpose of advancing his personal financial interests. Several members of Congress, including Sen. Charles Grassley (R-IA) and former Sens. Tom Coburn (R-OK) and Joseph Lieberman (I-CT), called for investigations into the Education Department's relationship with Wall Street.<sup>25</sup>

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<sup>21</sup> Letter from CREW Chief Counsel Anne Weismann to Robert Khuzami, Director, Division of Enforcement, SEC, Feb. 9, 2011 (attached as Exhibit J).

<sup>22</sup> Mr. Eisman and others urged Education to adopt a regulation that would have made students at for-profit institutions eligible for federal student loans only if Education determined their career programs would prepare them for gainful employment in an occupation with expected pay scales that would establish a debt-to-earning ratio of eight percent or less.

<sup>23</sup> Letter from CREW Chief Counsel Anne Weismann to Secretary of Education Arne Duncan, January 19, 2011 (attached as Exhibit K).

<sup>24</sup> *Id.*

<sup>25</sup> Ben Protess, Grassley Questions Education Agency's Ties to Hedge Funds, *New York Times*, July 28, 2011.

*Martin Shkreli*

In July 2012, CREW requested an investigation into another short-seller, Martin Shkreli, then chief investment officer of the hedge fund MSMB Capital Management, for manipulating the market price of the stocks of biotechnology and pharmaceutical industries.<sup>26</sup> Despite lacking any scientific or medical background, Mr. Shkreli submitted a citizen petition to the FDA asking the agency not to approve a New Drug Application developed by the biotech firm Neoprobe (now Navidea Biopharmaceuticals, Inc.) for a lymph node mapping agent. Mr. Shkreli admitted he stood to gain financially from a decline in the company's stock price.<sup>27</sup>

Mr. Shkreli sought to influence the FDA to advance his personal financial interests on other occasions as well. In September 2010, while shorting Arena Pharmaceutical's stock, Mr. Shkreli asked an advisory committee to consider a slide show presentation he had prepared claiming the company's weight loss drug, Lorcaserin, had not been properly tested. Similarly, in December 2010, also while shorting the company's stock, Mr. Shkreli sent a presentation via email to 12 FDA officials, including the commissioner, asking the agency to deny approval of MannKind's insulin drug, Afrezza, arguing the trials had failed to demonstrate its efficacy.<sup>28</sup> Mr. Shkreli acknowledged financial conflicts of interest, recognizing he would have benefited financially if the FDA adopted his point of view.<sup>29</sup>

It has been reported Mr. Shkreli is under investigation for possible securities law violations.<sup>30</sup>

Conclusion

Wall Street investors, always aware government action could impact their investments, have relied in the past on their lobbyists, Freedom of Information Act requests, and even political intelligence to provide them with insights that give them an advantage in the financial markets. Increasingly, however, they are injecting themselves directly into government processes – sometimes openly and sometimes stealthily -- in the hope of manipulating the outcome to their financial advantage.

Americans already believe both Wall Street and Washington are rigged to the benefit of the rich and powerful and the detriment of nearly everyone else. Watching billionaire hedge fund managers utilize their vast resources to instigate government investigations to increase their

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<sup>26</sup> Letter from CREW Executive Director Melanie Sloan to United States Attorney Preet Bharara, July 9, 2012 (attached as Exhibit L).

<sup>27</sup> *Id.*

<sup>28</sup> *Id.*

<sup>29</sup> *See Id.*

<sup>30</sup> Christie Smythe, Retrophin Founder Said Probed Over Securities Dealings, *Bloomberg*, January 7, 2015 (attached as Exhibit M).

The Honorable John Thune, Bill Nelson, Fred Upton and Frank Pallone  
March 18, 2015  
Page 7

wealth can only lead to even further decreased confidence in the country's financial markets and government leaders. We urge you to investigate the conduct of Mr. Ackman and others and consider how to deter investors more broadly from abusing government processes.

Thank you for your consideration.

Sincerely,

A handwritten signature in black ink, appearing to read 'Anne Weismann', with a long horizontal flourish extending to the right.

Anne Weismann  
Interim Executive Director

Encls.

cc: The Honorable Charles Grassley  
Chair, Senate Judiciary Committee