Theranos Case Study: What Went Wrong?
Objectives

- Discuss how a young college dropout hoodwinked major venture capitalists
- Discover the 8 signs of trouble that were overlooked and resulted in a $9 Billion fraud scheme
- Explore these key questions
  - Would an effective compliance program cause the startup to fail or succeed?
  - What is the role of the compliance professional when faced with signs of fraud?
  - Is an industry that affects people’s lives held to a higher standard?
CHANGE THE WORLD WITH A DROP OF BLOOD
— Elizabeth Holmes

8 Signs of Trouble
Signs of Trouble #1

Secret Technology

- Walgreens executives were not allowed in the lab to examine data
- CMS surveyors were not aware of the secret lab
- Used “trade secrets” as their defense
- Employees worked in silos and were not permitted to share information with each other

Signs of Trouble #2

Smitten with the new female Steve Jobs

- Forbes estimated the value at $9 Billion ($9,000,000,000) despite absence of scientific studies
- Sales never topped $100 Million
- Powerful Board members (such as former Secretaries of State George Schultz & Henry Kissinger, former General of Armed Forces James Mattis [recently Secretary of Defense], & former senator Bill Frist) overlooked obvious shortcomings
- Graced the cover of New York Post, Wall Street Journal, and Time
- Sought after speaker
REVOLUTIONIZE HEALTHCARE!
- Elizabeth Holmes

Signs of Trouble #3

Culture of Retaliation

- Some employees doubted accuracy of results
- High turnover - employees were fired for disagreeing with Elizabeth Holmes
- Tyrant COO - Sunny Balwani
- Signed covenants upon termination
Signs of Trouble #4

Dazzled Investors

- Aggressive boasts were not challenged by investors
- Investors dazzled by Elizabeth & the potential innovation that could “change healthcare”
- Never demanded an answer to: Does this thing really work?"

ONE TINY DROP CHANGES EVERYTHING - Elizabeth Holmes
Signs of Trouble #5

Implied Endorsements

- Employees wrote flattering reports about company products
- Employees put logos of pharma companies on reports

Signs of Trouble #6

Rolled out Defective Machines

- Received millions from Walgreens to rollout testing
  - Diagnostic tools were not ready
  - Lied to Walgreens, rather than request more time
  - In 2013, opened 42 wellness centers in AZ, 2 in CA, & 1 in PA
- Passed off 3rd party testers as its own
  - Engineers modified standard testing machines to make them look like Theranos’s new “mini-Labs”
ALL THE SAME TESTS.
ONE TINY SAMPLE.

- Elizabeth Holmes

Signs of Trouble #7

Liar, Liar, Pants on Fire!

- Lied to reporters about how many tests could be performed
- Used those misleading articles to lure investors
- Wrote her own “peer-reviewed” article
- Hid relationship with COO
Signs of Trouble #8

No Compliance Professional

- No compliance committee until 2016
- Elizabeth had majority shares for votes and no one to check her – founder, chairwoman, & CEO
  - Total control by founder is not uncommon in Silicon Valley start-ups

Polling Question

- How would an effective compliance program have affected the startup’s success?
  - Greater chance of success
  - Greater chance of failure
  - No impact
  - I don’t know
Holmes explains the process:

A chemistry is performed so that a chemical reaction occurs and generates a signal from the chemical interaction with the sample, which is translated into a result, which is then reviewed by certified lab personnel.

Plaque on Holmes’s desk:

WHAT WOULD YOU DO IF YOU KNEW YOU COULD NOT FAIL?
Status as of January 2019

Holmes settled with the SEC for “massive fraud”
- Not required to admit wrongdoing
- Forced to surrender control of Theranos
- Banned from serving as a director or officer of any public company
- Return 18.9 million shares of stock
- Pay penalty of $500,000

Status as of January 2019

There is still a major criminal investigation by the FBI
Sunny Bulwani refused to settle and is awaiting trial
Elizabeth Holmes is currently soliciting investors for a new Silicon Valley start-up!
I DON’T KNOW
Elizabeth Holmes
-600+ times in 2017 deposition

What would you do?

What is the role of the compliance professional when faced with signs of fraud?

- “Conscience of the organization”
- Board reporting
- Outside legal counsel
Polling Question

- Is an industry that affects people’s lives held to a higher standard?
  - Yes
  - No
  - Maybe
  - I don’t know

Questions?

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