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Must whistleblowers provide information to the SEC to obtain protection under Dodd-Frank?

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The U.S. Supreme Court has agreed to resolve a circuit split regarding whether an employee who is terminated after reporting potential securities law violations to senior management, but not to the Securities and Exchange Commission, is covered by the anti-retaliation provisions of the Dodd-Frank Act.[1]

In the case, Paul Somers, a vice president at Digital Realty Trust, made several reports to senior management of possible securities law violations. He was fired shortly thereafter without ever reporting his concerns to the SEC.

The Dodd-Frank Act defines a whistleblower as one "who provides … information relating to a violation of the securities laws to the commission, in a manner established, by rule or regulation, by the commission."[2] This definition of whistleblower clearly requires the submission of information to the SEC.

The statute then goes on to discuss various provisions governing the granting of awards to whistleblowers before prohibiting retaliation against whistleblowers. The anti-retaliation section reads, in relevant part:

> No employer may discharge, demote, suspend, threaten, harass, directly or indirectly, or in any other manner discriminate against, a whistleblower in the terms and conditions of employment because of any lawful act done by the whistleblower —
>
> (i) in providing information to the commission in accordance with this section;
>
> (ii) in initiating, testifying in, or assisting in any investigation or judicial or administrative action of the commission based upon or related to such information; or
>
> (iii) in making disclosures that are required or protected under the Sarbanes-Oxley Act of 2002 (15 U.S.C.A. 7201 et seq.), this chapter, including section 78j-1(m) of this title, section 1513(e) of Title 18, and any other law, rule, or regulation subject to the jurisdiction of the commission.[3]

The question is whether the definition of whistleblower, which clearly requires disclosure to the SEC, also limits the third subdivision of the anti-retaliation provision to those who also report to the agency but are fired for other reasons.

Both the U.S. District Court for the Northern District of California and 9th U.S. Circuit Court of Appeals found that Somers could be a whistleblower even though he never provided information to the SEC.

The 2nd U.S. Circuit Court of Appeals and the SEC have also resolved the legal question similarly to the 9th Circuit, whereas the 5th U.S. Circuit Court of Appeals (and a dissenting judge in both the 2nd and 9th Circuits) have concluded that the third subdivision also requires submission of documents to the SEC.

The question is whether the definition of whistleblower that clearly requires disclosure to the Commission also limits the third subdivision of the anti-retaliation provision to those who report to the SEC.

SEC RULEMAKING

The SEC used its authority to issue rules to make it clear that the anti-retaliation provisions apply irrespective of whether the potential whistleblower gives information to the commission.

For purposes of the anti-retaliation provisions of its rule, the SEC grounds the definition of whistleblower in the Dodd-Frank Act's anti-retaliation provisions.

That is, you are a whistleblower if "you possess a reasonable belief that the information you are providing relates to a possible securities law violation" and you provide the information in one of the ways set out in Section 78u-6(h)(1)(A) where the whistleblowing provisions are codified.[4]

The SEC further noted that even if you do not qualify for an award — that is, you did not provide information to the SEC — you can still be a whistleblower for purposes of the anti-retaliation provisions.

THE *CHEVRON* DOCTRINE

Although none of the appellate courts start with a *Chevron* analysis, all reference the doctrine. Starting there provides a nice organizing principle for the various arguments.

In *Chevron USA Inc. v. Natural Resources Defense Council*, the Supreme Court created a two-part test to analyze the validity of an agency's construction of a statute it administers.

The first question is "whether Congress has directly spoken to the precise question at issue. If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress."[5]

If, however, "the statute is silent or ambiguous with respect to the specific issue, the question for the court is whether the agency's answer is based on a permissible construction of the statute."

Part one of the *Chevron* test — whether the provision at issue is ambiguous or whether Congress's intent is clear — is the contested one.

The first appellate decision to address the question of the scope of the SEC anti-retaliation provisions, the 5th Circuit's *Asadi v. GE Energy (USA),* found that there is no statutory ambiguity and rejected the SEC's expansive reading of the whistleblower protection provision.[6]

> Like the 2nd Circuit, the 9th Circuit in *Somers* concluded that a report to the SEC is not necessary to protect an employee from retaliatory activity.

This literal reading of the statute starts with the definition of whistleblower in Section 78u-6(a)(6), in which the requirement to provide information to the SEC is crystal clear.

In addition to the clear definition of whistleblower, the 5th Circuit emphasized the use of the word "whistleblower" at the beginning of the anti-retaliation provisions in Section 78u–6(h)(1)(A), as follows: "No employer may discharge, demote, suspend, threaten, harass, directly or indirectly, or in any other manner discriminate against, a *whistleblower*" (emphasis added).

The 5th Circuit further emphasized that Congress chose to use the word "whistleblower" rather than a broader term such as "individual" or "employee," which makes clear that only those who provide information to the SEC are protected by the anti-retaliation provisions.

Given this perceived lack of statutory ambiguity, the court chose not to defer to the SEC's contrary interpretation under *Chevron* because it said Congress had directly spoken on the matter.

The 2nd Circuit, on the other hand, found the underlying statute ambiguous enough to find *Chevron* deference appropriate.[7] The gateway to finding this ambiguity is asking what effect subdivision 78u–6(h)(1)(A)(iii) has, given the existence of subdivisions (i) and (ii).

Put differently, what person will have reported to the SEC, and so will be a whistleblower under subsection 78u-6(a)(6), but will have been fired for whistleblowing reasons other than the provision of information to the SEC (subdivision i) or assistance to an SEC investigation (subdivision ii)?

The 5th Circuit in *Asadi* used the example of a midlevel manager who simultaneously reports a securities law violation to his CEO and to the SEC to argue that the third category of retaliation has unique meaning. If the CEO, unaware of the simultaneous report to the SEC, were to fire the manager, only the third category of protected activity would protect him.

While this hypothetical fact pattern theoretically harmonizes the anti-retaliation provision with the whistleblower definition, the 2nd Circuit and 9th Circuit found that few actual whistleblowers would be protected by subdivision (iii).

First, neither court found it very likely that employees would simultaneously report. Second, requirements governing auditors and attorneys obligate them to report internally before reporting externally.

For example, the Sarbanes-Oxley Act requires lawyers to report violations internally, and the SEC's Standards of Professional Conduct allow lawyers to break client confidences only in certain limited instances.

Likewise, the Sarbanes-Oxley Act and the Exchange Act require auditors to report internally; only if their reports are not addressed may they report to the SEC.

In short, the number of potential whistleblowers who would be protected by the third category of protected activity would be so vanishingly small that a literal reading would narrow the provision "to the point of absurdity."[8]

This analysis of the limited effect of the third subdivision led the 2nd Circuit to ask whether Congress could have intended such a limited reading of subdivision (iii).

The court, however, found no answer because the provision was added during the Conference Committee and no legislative materials clarify the intent behind it.

The 2nd Circuit then walked up to the line of finding that Congress intended the broader meaning but stopped short of going over it.

The court said it was "doubtful" that the conferees who accepted this last-minute addition expected it to have such a "limited scope" and, noting that if the court "had to choose between reading the statute literally or broadly to carry out its apparent purpose, [it] might well favor the latter course."

Instead of crossing that line, the 2nd Circuit concluded that the lack of clarity surrounding whether Congress intended subdivision (iii) to have the narrow effect it has when limited by the whistleblower definition created the sort of statutory ambiguity that requires a court to move to the second part of the *Chevron* framework and analyze whether the SEC's rulemaking was a reasonable interpretation.

Relying on its preceding discussion of the statutory provisions and legislative history, the court concluded that the SEC

regulation was reasonable and held that employees need not provide information to the SEC in order to benefit from the anti-retaliation provision in Section 78u-6(h)(1)(A)(iii).

Like the 2nd Circuit, the 9th Circuit in *Somers* concluded that a report to the SEC is not necessary for the third subdivision to protect an employee from retaliatory activity.

However, the *Somers* court grounded its conclusion on legislative intent, holding that the narrow reading of the anti-retaliation provision would "undercut congressional intent" and that a "strict application" of Dodd-Frank's definition of whistleblower "would, in effect, all but read subdivision (iii) out of the statute."

Having reached that conclusion, the 9th Circuit buttressed its conclusion by reference to the *Chevron* doctrine.

"Even if the word 'whistleblower' in the anti-retaliation provision creates uncertainty because of the earlier narrow definition of the term, the agency responsible for enforcing the securities laws has resolved any ambiguity and its regulation is entitled to deference," the court said.

This *Chevron* analysis is secondary in the 9th Circuit's view, however, as it concluded not just that the SEC's rule is reasonable, but that it is also correct.

As the court put it, "The regulation accurately reflects congressional intent that [Dodd-Frank] protect employees whether they blow the whistle internally, as in many instances, or they report directly to the SEC."

OTHER ISSUES

The 5th Circuit and 9th Circuit also include analysis of whether any whistleblower would use the anti-retaliation provisions of Sarbanes-Oxley if the anti-retaliation provisions of Dodd-Frank do not require reporting to the SEC.

The 5th Circuit argued that the Sarbanes-Oxley anti-retaliation provision would be rendered effectively moot because whistleblowers would choose the Dodd-Frank anti-retaliation framework.

The court explained Dodd-Frank allows the recovery of two times back pay rather than simply back pay, allows one to avoid filing a complaint with the secretary of labor and instead go straight to court, and has a longer statute of limitations.

The 9th Circuit found that the Sarbanes-Oxley framework was not moot because a whistleblower might prefer the Sarbanes-Oxley scheme since the secretary of labor might take up the whistleblower's claim on their behalf.

This would allow the whistleblower's claim to be litigated at much less cost to the whistleblower, and the Sarbanes-Oxley anti-retaliation framework allows for the recovery of special damages, including emotional distress damages not available under the Dodd-Frank framework.

Ultimately, while both the 5th Circuit and 9th Circuit include this argument as part of their rationale, the effect on the Sarbanes-Oxley's anti-retaliation framework seems unlikely to be the issue on which the Supreme Court bases its decision.

Rather, the key issue is whether the third anti-retaliation category so limits the provision's effect as to create ambiguity about whether Congress intended the restricted definition of whistleblower to govern this third category.

In addition, the cases raises two other issues that may find their way into the Supreme Court's analysis. Both the 2nd Circuit and 9th Circuit cite Chief Justice John Roberts' opinion in *King v. Burwell,* 135 S. Ct. 2480 (2015), for the proposition that the definition of whistleblower need not be determinative.

This citation to *King* was the only thing that occasioned a unique comment beyond Judge John Owens' basic statement of agreement with the 5th Circuit's opinion in his one-paragraph dissent in *Somers*: "In my view, we should quarantine *King* and its potentially dangerous shapeshifting nature to the specific facts of that case to avoid jurisprudential disruption on a cellular level. *Cf. John Carpenter's The Thing* (Universal Pictures 1982)."

Should the justices decide that the statute means precisely what it says, will any justice comment on this use of *King*?

Another issue on which the case may provoke interesting commentary is the status of the *Chevron* doctrine itself.

In *City of Arlington v. FCC*, the Supreme Court examined whether *Chevron* deference extends even "to an agency's interpretation of a statutory ambiguity that concerns the scope of the agency's statutory authority (that is, its jurisdiction)."[9]

The court, in an opinion authored by Justice Antonin Scalia and joined by Justices Elena Kagan, Sonia Sotomayor, Clarence Thomas and Ruth Bader Ginsburg, determined that it did.

Justice Stephen Breyer filed a concurring opinion, while Justices Roberts, Anthony Kennedy and Samuel Alito dissented. Of course, Justice Scalia has now been replaced by Justice Neil Gorsuch, and their views on *Chevron* deference appear to differ dramatically.

Justice Gorsuch, back when he was Judge Gorsuch, filed an opinion that said the *Chevron* doctrine should be discarded because it allows a nonjudicial branch of government to say what the law is.

He called *Chevron* "no less than a judge-made doctrine for the abdication of the judicial duty" that appears to "qualify as a violation of the separation of powers."[10]

While Chief Justice Roberts' dissent in *City of Arlington* did not argue that *Chevron* should be abandoned, Justice Scalia

claimed that the dissent's argument was "a massive revision of our *Chevron* jurisprudence" and that the ultimate target of the jurisdictional/nonjurisdictional dichotomy was *Chevron* itself.

Will Justice Gorsuch's open rejection of *Chevron* deference affect other justices? Even if it does, *Somers* seems an unlikely case to end *Chevron* deference because, even if all of the justices in the *City of Arlington* dissent agreed with Gorsuch, five votes seemingly still exist to uphold the doctrine.

While these three issues are interesting subplots, the outcome of *Somers* will almost certainly turn on whether the Supreme Court justices believe the extremely limited effect of the third anti-retaliation provision creates statutory ambiguity.

If they do, then the justices will likely defer to the SEC's regulation under *Chevron*. If they do not, then the clear statutory language will prevent *Chevron* deference, and all potential whistleblowers will have to provide information to the SEC to benefit from Dodd-Frank's anti-retaliation provisions.

NOTES

[1] *Somers v. Digital Realty Trust Inc.*, 850 F.3d 1045 (9th Cir. 2017), *cert. granted*, 137 S. Ct. 2300 (No. 16-1276).

[2] 15 U.S.C.A. § 78u-6(a)(6) (West).

[3] *Id.* at § 78u-6(h)(1).

[4] 17 C.F.R. § 240.21F-2(b)(1).

[5] 842 U.S. 837, 842–43 (1984).

[6] 720 F.3d 620, 630 (5th Cir. 2013).

[7] *Berman v. Neo@Ogilvy LLC*, 801 F.3d 145, 159 (2d Cir. 2015).

[8] *Somers*, 850 F.3d at 1049.

[9] 569 U.S. 290 (2013).

[10] *Gutierrez-Brizuela v. Lynch*, 834 F.3d 1142, 1152, 1154 (10th Cir. 2016) (Gorsuch, J., concurring).

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