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CLIENT ALERT

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BLOWING THE WHISTLE ON WHISTLEBLOWER PROTECTION: Supreme Court to Review Scope of Whistleblower Protection Under Dodd-Frank Act

On November 28, the United States Supreme Court will hear oral argument to determine whether federal law protects whistleblowers who report securities violations internally to their employers without making a report directly to the United States Securities and Exchange Commission ("SEC").

In response to the 2008 economic crisis, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act[1] ("DFA") to ensure the stability of the financial industry and to provide increased consumer protection. Part of the DFA provides incentives and protections for employees who report their employers to the SEC for potential securities violations.[2]

Of particular importance is the DFA's anti-retaliation provision, which prohibits employers from taking adverse employment action against employees who make reports to the SEC.[3] The DFA is silent on whether this protection extends to employees who opt to report violations internally without also going to the SEC. The DFA defines "whistleblowers" only as persons who provide information "to the Commission."[4] This apparent restriction has divided the United States Circuit Courts of Appeal,[5] but will now be addressed by the Supreme Court in Digital Realty Trust, Inc. v. Somers, (No. 16-1276).

Paul Somers was an employee of Digital Realty Trust, Inc. ("Digital Realty") from 2010 to 2014, working as a Vice President of Portfolio Management in both Europe and Singapore. Before his termination in 2014, Somers reported his Singapore boss to senior management, but not the SEC, for potential violations of the Sarbanes-Oxley Act ("SOX").[6] Somers had accused his boss of "eliminat[ing] internal controls over certain corporate actions," and other violations of SOX, including "hiding seven million dollars in cost overruns on a

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[1] 124 Stat. 1376.
[2] *See* 15 U.S.C. § 78u-6, which was added as Section 21F to the Securities Exchange Act of 1934.
[3] *See* 15 U.S.C. § 78u-6(h)(1)(A).
[4] 15 U.S.C. § 78u-6(a)(6).
[5] *See, e.g.*, Asadi v. G.E. Energy (USA), L.L.C., 720 F.3d 620 (5th Cir. 2013) (rejecting SEC interpretation that DFA was meant to protect whistleblowers who make disclosures internally or to the SEC); Berman v. Neo@Ogilvy LLC, 801 F.3d 145 (2d Cir. 2015) (adopting SEC's interpretation that whistleblowers who make disclosures internally are protected under DFA).
[6] 116 Stat. 745. SOX, enacted in response to major corporate scandals in 2002, is considered the predecessor to the DFA. Like the DFA, it seeks to create stability in the financial industry by regulating corporate action and protecting consumers.

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development in Hong Kong."[7] After being terminated, Somers brought a claim against Digital Realty in federal court for violating the anti-retaliation provisions of the DFA,[8] which states, in part, that employers may not take adverse employment action against employees who make "disclosures that are required or protected under the Sarbanes-Oxley Act."[9]

At the trial court level, the focus of both parties' arguments was whether Somers qualified as a "whistleblower" under the DFA. Somers claimed that he was wrongfully terminated in retaliation for internally reporting his boss's alleged violations of SOX and that the DFA's anti-retaliation provision provided him recourse. Digital Realty moved to dismiss Somers's claim, arguing that Somers had no standing to sue under the DFA because he never reported his allegations to the SEC and therefore did not qualify as a "whistleblower."

The District Court for the Northern District of California ruled in favor of Somers, deferring to an SEC rule[10] interpreting the DFA's anti-retaliation provision to include protections for whistleblowers who report only internally. The SEC rule and its corresponding commentary, promulgated in 2011, provide clarity on "whistleblower" qualification under the DFA by analyzing the interplay between the DFA and SOX. The rule's commentary states that an individual qualifies as a whistleblower for the purpose of the DFA's anti-retaliation protection, regardless of how the DFA itself defines "whistleblower," if the individual makes a report in accordance with the DFA's anti-retaliation provision. Because the provision explicitly affords protection to individuals who report violations of SOX, and SOX provides protection to employees who make reports only internally, the DFA must also provide whistleblower protection for internal whistleblowers. As such, the District Court ruled that Somers had standing to bring a wrongful termination claim under the DFA.

Digital Realty appealed the District Court's decision, arguing that the District Court erred in deferring to the SEC's rule, which it alleged was misguided. The United States Court of Appeals for the Ninth Circuit affirmed the District Court's decision, however, stating that the SEC rule is "consistent with Congress's overall purpose to protect those who report violations internally as well as those who report to the government," and that Congress's intent is "reflected in the language of the specific statutory subdivision [of the DFA], which explicitly references internal reporting provisions of Sarbanes-Oxley and the Securities Exchange Act of 1934."[11]

The Supreme Court granted certiorari to Digital Realty and will hear the case in a few weeks, though the scale tips heavily in Somers's favor. The District Court's deference to the SEC's interpretation of the DFA was based on a framework established in a landmark Supreme Court case, Chevron

[7] Somers v. Digital Realty Trust, Inc., 119 F. Supp. 3d 1088, 1092 (N.D. Cal 2015).
[8] Somers brought several other claims as well, including discrimination and defamation. Digital Realty moved to dismiss only the charges related to the DFA.
[9] 15 U.S.C. § 78u-6(h)(1)(A)(iii).
[10] 17 CFR 240.21F-2(b)(1)(ii); *See also* Securities Whistleblower Incentives and Protections (Adopting Release), 789 Fed. Reg. 34300, 3401-3404 (June 13, 2011).
[11] Somers v. Digital Realty Trust, Inc., 850 F.3d 1045, 1047 (9th Cir. 2017).

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U.S.A., Inc. v. NRDC, 467 U.S. 837 (1984). In that case, the Supreme Court created an administrative law principle that requires courts to defer to an agency's interpretation of an ambiguous statutory provision, as long as the interpretation is reasonable, meaning the interpretation is not "arbitrary, capricious, or manifestly contrary to the statute." The interpretation need not be the only or best interpretation, just reasonable.

Furthermore, the practical effect of a ruling for Digital Realty could be problematic for the financial industry as a whole. Corporate accountability, both inside and outside of America's financial institutions, is of paramount "front page" importance. Internal whistleblowing is a valuable tool for all interested parties. A ruling for Digital Realty would take much of the bite out of the DFA's whistleblower provision. As one commentator has stated, "The results would be catastrophic, not only for the employees who lose their jobs trying to do the right thing, but also for investors who must rely upon the accuracy of numerous internal corporate disclosures when making investment decisions, and corporations which have created extensive compliance programs designed as an early reporting system protecting the company from fraud."[12]

The Supreme Court's decision will have a meaningful impact one way or another and is a must-watch for employers and employees in the financial industry. Employees should be aware of the current incentives and protections afforded to them under the DFA, and how Digital Realty may change those benefits, while employers should be cognizant of how Digital Realty could impact their internal compliance practices.

[12] Stephen Kohn, Digital Realty Trust v. Somers May Kill Corporate Compliance, Law360 (Sep. 21, 2017, 1:14 PM), https://www.law360.com/articles/964208/digital-realty-trust-v-somers-may-kill-corporate-compliance.

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