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Ninth Circuit Holds that Internal Whistleblowers Are Protected from Retaliation

On March 8, 2017, the United States Court of Appeals for the Ninth Circuit ("Ninth Circuit") held that individuals who make internal disclosures of potential securities law violations – like those who report wrongdoing directly to the Securities Exchange Commission ("SEC") – are protected as "whistleblowers" under the Dodd Frank Act ("DFA"). This decision, which follows the 2015 decision by the United States Court of Appeals for the Second Circuit ("Second Circuit") in *Berman v. Neo@Ogilvy LLC*, reinforces the need for companies to ensure that internal whistleblowers are adequately protected from retaliation.

DFA Whistleblower Protections

The DFA created broad protection for whistleblowers or employees who report potential misconduct. Pursuant to the DFA, employers may not "discharge, demote, suspend, threaten, harass, directly or indirectly, or in any other manner discriminate against, a whistleblower in the terms and conditions of employment." 15 U.S.C.A. § 78u-6(h)(1)(A). This definition is purposely broad and allows courts to make a "factual determination on a case-by-case basis" of whether allegedly retaliatory conduct is in fact retaliatory. *Ott v. Fred Alger Mgmt., Inc.*, 2012 WL 4767200, at *3 (S.D.N.Y. Sept. 27, 2012). Because the statute is broadly worded and designed to encourage careful factual adjudication, any employment action could be construed by an employee as potentially retaliatory. Moreover, because retaliation is a fact question, whether retaliation occurred generally cannot be determined on a motion to dismiss, and there are very few cases where employers have succeeded in dismissing on this basis at summary judgment. Therefore, companies face significant risks in taking any employment action that involves an employee who may qualify as a whistleblower.

Who is a Whistleblower?

The statutory definition of a "whistleblower" is narrower than the definition adopted by the SEC. A whistleblower is defined in the DFA as "any individual who provides . . . information relating to a violation of the securities laws to the [SEC]." 15 U.S.C. § 78u-6(a)(6). However, the anti-retaliation provision of the DFA arguably protects a broader category of individuals from retaliation. It states that an employer cannot "discharge, demote, suspend, threaten, harass, directly or indirectly, or in any other manner discriminate against, a whistleblower in the terms and conditions of employment" in retaliation for: (i) providing information to the SEC; (ii) initiating, testifying in, or assisting an SEC investigation or action; or (iii) making disclosures that are protected by the Sarbanes-Oxley Act ("SOX") or "any other law, rule, or regulation subject to the jurisdiction of" the SEC. 15 U.S.C. § 78u-

6(h)(1)(A). The SEC has stated that this creates an ambiguity because the anti-retaliation provision protects individuals who make internal reports pursuant to the SOX, even if the statutory definition of a "whistleblower" is narrower.[1] As a result, according to the SEC, there are two different definitions of a "whistleblower" in the rule implementing the DFA whistleblower provisions – a narrow definition that governs monetary awards and a broader definition that governs the anti-retaliation provisions.[2] Therefore, according to the SEC's interpretation of the DFA, whistleblower protections apply to individuals if they make disclosures that are protected under the SOX, which *includes* internal disclosures. 17 C.F.R. § 240.21F-2.

Nonetheless, companies have challenged whistleblower claims predicated on internal reports, arguing that based on the statutory definition of the term "whistleblower," internal whistleblowers are not protected from retaliation under the DFA. In deciding these challenges, courts have considered whether there is ambiguity in the DFA, and if so, how it ought to be resolved. Over time, a split of authority has developed regarding the correct way to interpret the language of the statute.

The United States Court of Appeals for the Fifth Circuit ("Fifth Circuit"), which was the first Court of Appeals to consider the question, held that "there is only one category of whistleblowers: individuals who provide information relating to a securities law violation to the SEC." *Asadi v. GE Energy (USA), LLC*, 720 F.3d 620, 625 (5th Cir. 2013). Finding the statutory language clear, the Fifth Circuit opted *not* to defer to the SEC's interpretation of the statute. *Id.* at 629-30. By contrast, the Second Circuit concluded in *Berman v. Neo@Ogilvy LLC* that "the pertinent provisions of [the DFA] create sufficient ambiguity to warrant . . . deference to the SEC's interpretive rule." 801 F.3d 145, 146 (2d Cir. 2015). The majority found an "arguable tension" between the statute's definition and its substantive whistleblower protection provisions, and decided to resolve the conflict in favor of protecting the internal whistleblower. *Id*. at 147.

This disagreement over interpretation has played out similarly at the district court level. *Compare Egan v. TradingScreen, Inc.*, 2011 WL 1672066, at *5 (S.D.N.Y. May 4, 2011) ("The contradictory provisions of [the DFA] are best harmonized by reading [the DFA's] protection of certain whistleblower disclosures not requiring reporting to the SEC as a narrow exception to [the DFA's] definition of a whistleblower as one who reports to the SEC.") *with Wagner v. Bank of Am. Corp.*, 2013 WL 3786643, at *5 (D. Colo. July 19, 2013) *aff'd*, 571 F. App'x 698 (10th Cir. 2014) ("[T]he plain language of the statute compels the conclusion that" the plaintiff cannot claim whistleblower protection for internal disclosures.). However, it is worth noting that a majority of the district courts that have considered this issue have held that internal disclosures should be protected. *See Connolly v. Remkes*, 2014 WL 5473144, at *5 (N.D. Cal. Oct. 28, 2014) (noting that a "large majority of district courts" have found that ambiguity in the DFA justified deferring to the SEC's interpretation).

The *Somers* decision from the Ninth Circuit is the most recent addition to this split of authority. Deciding the question after the district court certified it for interlocutory appeal pursuant to 28 U.S.C. § 1292(b), a divided Ninth Circuit panel echoed the *Berman* decision. It held that in light of the purpose of the SOX and the DFA, the clear meaning of the language at issue, and well-settled principals of statutory interpretation, "[the] DFA's anti-retaliation provision unambiguously and expressly protects from retaliation all those who report to the SEC and who report internally." *Somers v. Digital Realty Trust Inc.*, No. 15-17352, slip op. at 6-10 (9th Cir. Mar. 8, 2017). Thus, the court held that the SEC rule "accurately reflects Congress's intent to provide broad whistleblower protections," and it is entitled to deference from the court. *Id*. at 12. Though the *Somers* court acknowledged that the Fifth Circuit in *Asadi* held otherwise, it found that reading the whistleblower provision any other way would produce an absurd result; it would leave employees who are mandated under the SOX to report internally *before* reporting to the government entirely exposed to retaliation, and would "in effect, all but read subdivision (iii) out of the statute." *Id*. at 10. Of note, however, Judge Owens dissented from the opinion, and articulated his agreement with the Fifth Circuit in *Asadi* and the dissenting opinion in *Berman* that whistleblowers do not include those who report internally. *Id*. at 13.

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1 *See Interpretation of the SEC's Whistleblower Rules Under Section 21F of the Securities Exchange Act of 1934*, Release No. 34-75592 (Aug. 4, 2015)

2 *Id*.

The Impact of Somers

Following *Somers*, it is clear that an "intercircuit disagreement" has developed. No. 15-17352, slip op. at 10 (9th Cir. Mar. 8, 2017). Until the Supreme Court steps in to resolve the question of whether whistleblower protections extend to individuals who make internal disclosures, the question of potential retaliation liability under the DFA will remain uncertain. Consequently, companies must remain cognizant of both interpretations of the law, and ought to carefully structure in-house compliance procedures to ensure that internal whistleblowers are protected from retaliation. Additionally, when confronting questions involving whistleblowing and possible retaliation, companies should seek legal advice to ascertain potential liability under the DFA.

Authors

Robert Houck
Partner
T: +1 212 878 3224
E: robert.houck
@cliffordchance.com

Christopher Morvillo
Partner
T: +1 212 878 3437
E: christopher.morvillo
@cliffordchance.com

Edward O'Callaghan
Partner
T: +1 212 878 3439
E: edward.ocallaghan
@cliffordchance.com

Robert Rice
Partner
T: +1 212 878 8529
E: robert.rice
@cliffordchance.com

Daniel Silver
Partner
T: +1 212 878 4919
E: daniel.silver
@cliffordchance.com

Benjamin Berringer
Associate
T: +1 212 878 3372
E: benjamin.berringer
@cliffordchance.com

Rochelle Swartz
Associate
T: +1 212 878 8505
E: rochelle.swartz
@cliffordchance.com