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Report from Washington

Supreme Court Considers Who Counts as a "Whistleblower" Under the Dodd-Frank Act's Anti-Retaliation Protections

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Introduction

On November 28, 2017, the U.S. Supreme Court heard oral arguments in *Digital Realty Trust, Inc. v. Somers*, No. 16-1276. *Digital Realty* asks the Court to consider if the anti-retaliation protections created by the Dodd-Frank Act ("Dodd-Frank") apply to an employee who makes internal disclosures of allegedly wrongful activity, but does not report the activity to the Securities and Exchange Commission ("SEC"), a question which has split the circuit courts.

Dodd-Frank was enacted by Congress in 2010 to "promote the financial stability of the United States by improving accountability and transparency in the financial system." To this end, Section 922 of Dodd-Frank, codified as Section 21F of the Securities Exchange Act of 1934, defined the term "whistleblower" and created new rewards and employment protections for securities whistleblowers.

Section 21F(a) defines a whistleblower as "any individual 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." 15 U.S.C. 78u-6(a)(6) (emphasis added). Section 21F's anti-retaliation provision goes on to prohibit employers from firing or penalizing employees who, among other things, "mak[e] disclosures that are required or protected under the Sarbanes-Oxley Act of 2002." In certain situations, Sarbanes-Oxley requires internal reporting before external reporting (*e.g.*, auditors must inform management of any potentially illegal acts and may only bring their concerns to the SEC after this internal reporting has occurred). In 2011, the SEC promulgated a rule construing Section 21F, which interpreted the term "whistleblower" to include employees who make only internal disclosures of potentially wrongful activity.

Background

Paul Somers was employed by Digital Realty as a Vice President from 2010 to 2014. Digital Realty is a real estate investment trust that owns, develops, and manages technology-related real estate, such as data centers. Somers alleges that he made several reports to the firm's senior management about possible securities law violations and that, in response, he was fired by the company. Somers did not report his concerns to the SEC before he was terminated. He sued Digital Realty, arguing that the firm violated the anti-retaliation protections created by Dodd-Frank when it fired him.

Digital Realty moved to dismiss the case, asserting that because Somers only reported the alleged violations internally and not to the SEC, he was not a "whistleblower" per Dodd-Frank and thus was not entitled to the Act's protections. The District Court for the Northern District of California denied Digital Realty's motion, concluding that tension between Dodd-Frank's "whistleblower" definition and its anti-retaliation provisions rendered the statute sufficiently ambiguous so as to require deference to the SEC's interpretation.

"The ordinary whistleblower is protected under Sarbanes-Oxley. He just has to have some exhaustion. And it's a shorter statute of limitations. And if you want to make it tougher, which [Congress does], it makes sense in a statute that's mostly about awards for reporting to the SEC to say it's where the SEC is directly involved."

— Justice Breyer

The District Court found that a "large majority" of courts that have considered Dodd-Frank's whistleblower provisions "have found ambiguity in the interplay between [the definition section and the anti-retaliation provisions]." The court then analyzed the statutory text, and concluded that Dodd-Frank's "narrow definition of whistleblower cannot easily be reconciled with [Section 21F's] seemingly expansive scope." The court therefore held that the SEC's regulation was entitled to *Chevron* deference. The *Chevron* doctrine requires courts to defer to an agency's interpretation of ambiguous language in a statute which the agency is charged with enforcing, unless the agency's interpretation is unreasonable. Following the denial of the motion to dismiss, Digital Realty was permitted to bring an interlocutory appeal.

Two circuit courts had previously considered the appropriate scope of Dodd-Frank's whistleblower protections before this case reached the appellate level. In *Asadi v. G.E. Energy (USA), L.L.C.*, the Fifth Circuit found for GE, holding that Dodd-Frank's definition of whistleblower "expressly and unambiguously requires that an individual provide information to the SEC to qualify as a 'whistleblower' for purposes of [Section 21F]." 720 F.3d 620, 623 (5th Cir. 2013). By contrast, two years later in *Berman v. Neo@Ogilvy LLC*, the Second Circuit concluded that the "tension" between Section 21F's definition of whistleblower and the anti-retaliation provisions is "as a whole sufficiently ambiguous to oblige us to give *Chevron* deference to the reasonable interpretation of the agency charged with administering the statute [*i.e.* the SEC]." 801 F.3d 145, 155 (2d Cir. 2015).

In *Digital Realty*, the Ninth Circuit agreed with the Second Circuit and affirmed, noting that the SEC regulation is "consistent with Congress's overall purpose to protect those who report violations internally as well as those who report to the government." 850 F.3d 1045, 1047 (9th Cir. 2017). Further, the court disagreed with the contention, raised by Digital Realty and in *Asadi*, that if Dodd-Frank is held to protect the same conduct that Sarbanes-Oxley does, this renders the Sarbanes-Oxley enforcement scheme moot. The court reasoned that the two schemes are sufficiently different, noting that "Sarbanes-Oxley lacks Dodd-Frank's double damage provision, has a shorter statute of limitations, and has more extensive administrative requirements." The court went on to describe circumstances in which the Sarbanes-Oxley protections "may be more attractive to the whistleblowing employee" than those offered by Dodd-Frank.

"It's quite possible… [Congress] forgot about this definitional provision, and they were meaning it more in the ordinary-language sense. But…it says what it says. And it says that it applies to this section. And you have to have a really, really severe anomaly to get over that."

— Justice Kagan

To resolve the circuit split and determine the applicable scope of Dodd-Frank's whistleblower protections, the Supreme Court granted Digital Realty's petition for a writ of certiorari on June 26, 2017.

Oral Argument Highlights

Oral argument focused primarily on two issues. First, the Court considered whether to apply Dodd-Frank's definition to both the Act's rewards and anti-retaliation provisions, as opposed to just the Act's rewards provisions. Second, the Court evaluated the extent to which it ought to defer to the SEC's promulgated regulation if the statutory language is indeed determined to be ambiguous.

Which Definition of "Whistleblower" Applies?

Digital Realty contended that the statutory definition applied, "by its plain terms," to the entirety of Dodd-Frank's whistleblower provisions. This reading, counsel for the company claimed, is "entirely consistent" with Congress's intent to increase the incentives for reporting violations of securities laws to the SEC. Moreover, the legislative history supports this view, as an earlier version of the anti-retaliation provisions "reached all employees," but was revised to apply just to "whistleblowers." Digital Realty noted that the Sarbanes-Oxley regime offers protections to employees who only make internal disclosures of potentially wrongful activity, and that Congress did not intend to render these protections superfluous with the enactment of Dodd-Frank. Citing the "elephant-in-a-mousehole" doctrine, Digital Realty argued that Congress would not have intended to create an "all-purpose anti-retaliation" regime through the use of ancillary provisions.

The United States, participating as *amicus curiae* to defend the SEC's regulatory definition, disagreed with Digital Realty, asserting that the statutory definition applied to Dodd-Frank's rewards provisions, while the ordinary meaning of "whistleblower" applied to the retaliation provisions. Further, there is a "unity of interest" among employees, employers, and the SEC in protecting and strengthening internal reporting and compliance. Counsel for Somers emphasized that Dodd-Frank must be read as being consistent with the entire securities law framework, which is designed to respond to the conduct of employers rather than the mechanism through which an employee discloses potentially wrongful conduct. Finally, Somers' advocate noted that Dodd-Frank was designed to strengthen, not contradict, the Sarbanes-Oxley regime, and that adopting petitioner's reading of the statute would frustrate this purpose.

The Justices evaluated the circumstances under which the Court should or could depart from Dodd-Frank's definition of "whistleblower." Justice Sotomayor noted she was "not sure there's a natural reading [or ordinary meaning]" of the word "whistleblower." Justice Gorsuch exclaimed that he was "just stuck on the plain language" of the text, wondering "how much clearer could Congress have been?" Chief Justice Roberts noted that, even if Congress inadvertently created an anomalous situation, the Court could not move beyond a clearly defined term unless a failure to do so would "make a mess of the whole thing." Justice Breyer questioned if Dodd-Frank creates an anomaly at all, noting that internal whistleblowers still get Sarbanes-Oxley protections. Based on the questions posed, many of the Justices appeared wary of setting aside the Dodd-Frank definition based on the supposedly anomalous situations described by Somers and the government.

How Much Deference Should the SEC's Opinion Receive?

The Justices also questioned the parties about why the SEC's promulgated rule defining whistleblower should be accorded *Chevron* deference. Justice Gorsuch, agreeing with Digital Realty, noted that when seeking public comment on its proposed rule, the SEC suggested it would be issuing a rule-making "with respect to whistleblowers *who report to the Commission*." However, the agency's final rule suggested, without any explanation, that reporting to the Commission would not be required for Dodd-Frank's anti-retaliation provisions to apply.

Counsel for Somers contended that the SEC "specifically asked for comments about whether to broaden or change the definition of whistleblower for the purposes of the anti-retaliation [provisions]." Respondent further noted that, in a public comment in response to the proposed rule, the Association of Corporate Counsel noted their assumption that internal

whistleblowers would also be covered by Dodd-Frank. The government added that under the "logical outgrowth test" adopted by the Supreme Court, an agency "proposing 'X' and getting 'not-X' is enough to satisfy" the requirements of the test.

However, some of the Justices seemed unconvinced by these arguments. Justice Breyer suggested that receiving notice that the SEC will be defining what counts as having provided information to the Commission "does not put people on notice that [the SEC is] going to apply [the definition] to people who don't provide information to the Commission," adding "I mean, that's English, I would think." After the government's logical outgrowth assertion, Justice Sotomayor asked, "Bottom line…how much are you relying just on *Chevron* deference here?" Given the skepticism expressed by the Justices, it is unclear that a majority of the Court believes the SEC's definition of "whistleblower" should be accorded deference in this case.

"I'm just stuck with the absence of any fair notice, an ipse dixit decision, without any reasons that wouldn't normally pass muster under the APA."

— Justice Gorsuch

Implications

The Court's decision in *Digital Realty* could have significant implications for corporate compliance and internal whistleblowers. In its 2017 Annual Whistleblower Report to Congress, the SEC indicated that over 80% of whistleblowers who received SEC awards under Dodd-Frank since 2012 first reported the alleged wrongdoing internally, and then made disclosures to the SEC. A holding that Dodd-Frank does not protect employees who only make internal reports could lead to an increase in the number of direct reports to the SEC, or could have a chilling effect on whistleblowing more broadly. Additionally, the Court's decision may also help clarify the extent to which the SEC's interpretations of Dodd-Frank, Sarbanes-Oxley, and other securities laws will receive deference from the courts.

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