RECENT DEVELOPMENTS IN WHISTLEBLOWER CLAIMS UNDER SARBANES-OXLEY AND DODD-FRANK

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Whistleblower claims against employers have seen a dramatic increase in recent years. The Sarbanes-Oxley Act of 2002 has been reinvigorated as a result of statutory amendments in 2010 and a spate of decisions from the Administrative Review Board (“ARB”) that has significantly expanded the rights and remedies of individuals claiming retaliation for “blowing the whistle.” The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 creates new protections for employees who disclose securities law violations, including the opportunity to receive bounty awards and enhanced remedies for victims of retaliation. Courts are just beginning to interpret the scope of the Dodd-Frank retaliation provisions with somewhat inconsistent results.

Section I of this paper provides an overview of the Sarbanes-Oxley Act’s whistleblower provisions and highlights several recent ARB and court decisions that have significantly altered the SOX landscape. Section II summarizes the new whistleblower protections in Dodd-Frank and analyzes the first wave of decisions by the federal courts.

I. SARBANES-OXLEY AND WHISTLEBLOWER LAW

On July 30, 2002, President Bush signed the the Sarbanes–Oxley Act of 2002 (“SOX”) into law. Seeking to restore investor confidence in ailing financial markets reeling from a spate of highly publicized alleged corporate financial wrongdoings, the Act reforms the oversight of corporate accounting practices and addresses a range of corporate accountability issues. The legislative history of Sarbanes-Oxley also makes it clear that Congress was intent upon closing loopholes in existing state and federal laws that provide protection for whistleblowers. See 148 Cong. Rec. S6439-40, 107th Cong., 2d Session (2002). Congress clearly reacted strongly to Enron’s attempted retaliation against Sherron Watkins, the now-famous whistleblower, and sought to deter similar conduct in the future by making employers who perpetrate such acts subject to stiff civil liability and criminal penalties. Id.

Section 806 of Sarbanes-Oxley protects from retaliation employees of public companies who report any conduct that the employee reasonably believes constitutes a violation of: (1) federal criminal law provisions prohibiting mail, wire, bank or securities fraud; (2) any rule or regulation of the Securities and Exchange Commission (“SEC”); or (3) any provision of federal law relating to fraud against shareholders. 18 U.S.C. § 1514A(a)(1). The Act covers reports made to the employee’s supervisor or other persons with investigative or disciplinary responsibili

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2 See Pub.L. 107-204, 116 Stat. 745 (2002). Section 806 of SOX provides protections for whistleblowers. This section of SOX has since been amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act (discussed infra).
authority, as well as information or assistance provided to a federal regulatory or law enforcement agency. *Id.* Covered whistleblowers also include those persons who file, testify, participate in or otherwise assist in a proceeding relating to alleged corporate or shareholder fraud. *Id.*

To establish a claim for a violation of Section 806, an employee must prove by a preponderance of the evidence (1) that the employee engaged in protected activity; (2) that the employer was aware of the protected activity; (3) that the claimant suffered an adverse employment action; and (4) that the protected activity was a contributing factor in the adverse employment action.3 If the employee establishes this prima facie case, the employer may avoid liability “if it can prove by clear and convincing evidence that it would have taken the same unfavorable personnel action in the absence of that protected behavior.”4

A successful complaining party under Sarbanes-Oxley is entitled to a broad array of remedies to make that individual “whole.” Damages may include reinstatement (in a termination case), backpay with interest, special damages, attorneys’ fees, litigation costs and expert witness fees. 18 U.S.C. § 1514A(c). The Act, however, does not provide for the recovery of punitive or liquidated damages, and the caselaw is split as to whether emotional distress and other non-pecuniary compensatory damages are recoverable. *See Hanna v. WCI Communities, Inc.*, 348 F. Supp. 2d 1332 (S.D. Fla. 2004). Civil liability may flow not only to the employer, but also to any officer, employee, contractor, subcontractor or agent found to have engaged in retaliatory action. 18 U.S.C. § 1514A(a); *Kalkunte v. DVI Financial Servs., Inc.*, 2004-SOX-56 (ALJ Jul. 18, 2005), *aff’d in part, vacated in part on other grounds*, ARB Case Nos. 05-139, 05-140 (ARB Feb. 27, 2009); *Gallagher v. Granada Entmt. USA*, 2004-SOX-74 (ALJ Oct. 19, 2004). Also, under limited circumstances, criminal liability can attach to certain retaliatory acts under section 1107 of the Act. *See In re Compact Disc Minimum Advertised Price Antitrust Litig.*, 456 F. Supp. 2d 131 (D. Me. 2006).

A. **Recent Amendments to the Sarbanes-Oxley Act**

The Dodd-Frank Wall Street Reform and Consumer Protection Act, discussed further in Section II, *infra*, expanded the scope of SOX’s whistleblower protections in several key ways.

The statute of limitations was broadened from 90 to 180 days to file a complaint with the U.S. Department of Labor - OSHA.5 SOX plaintiffs are now entitled to a jury trial, which was an unsettled question under SOX caselaw.6

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3 *See Bechtel v. Administrative Review Bd.*, 710 F.3d 443, 447 (2d Cir. 2013).
4 *Id.* (quotation marks omitted).
Non-publicly traded subsidiaries of publicly traded companies are now covered by SOX, by amendment to the definition of “publicly traded company” to include any “subsidiary or affiliate whose financial information is included in the consolidated financial statements of such company.” Prior to this amendment, the Department of Labor took the position that employees of non-publicly traded subsidiaries were generally not covered by the Act absent a showing of a substantial nexus between the parent and subsidiary, significantly narrowing the scope of coverage.7

“Nationally recognized statistical ratings organizations” are now covered by SOX, so employees of these organizations will now have the benefit of SOX whistleblower protection.8

Pre-dispute arbitration agreements will no longer be enforceable under SOX (except perhaps in the collective bargaining agreement context), nor will the rights and remedies under SOX be capable of waiver by agreement. This means that employers will no longer be able to compel arbitration under SOX.9

B. Recent Case Law Developments

For many years, individuals claiming retaliation under SOX had limited success when claims were brought in federal court or proceeded through the Department of Labor (“DOL”) administrative process up through the Administrative Review Board (“ARB”). Recent developments have created a more whistleblower-friendly litigation environment. President Obama appointed a new five-member ARB, which has been issuing favorable decisions to whistleblowers and taken a more expansive view of SOX than in the past. The new ARB has been overturning prior precedents that more narrowly construed SOX, making it more difficult for employers to get cases dismissed at the early stages and otherwise defend SOX claims. Federal district courts and courts of appeals have generally continued this trend with several significant whistleblower-friendly decisions. Some of the more noteworthy ARB and court decisions are discussed below.


  The ARB in *Sylvester* reversed an ALJ’s decision granting the company’s motion to dismiss on several grounds. First, the ARB held that the heightened pleading standards applicable to federal court complaints as established in *Bell Atlantic Corp. v. Twombly*10 and *Ashcroft v. Iqbal*11 are inappropriate for SOX whistleblower claims and that SOX claims to the DOL require “no particular form of complaint,” except that they must be in writing and “should

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contain a full statement of the facts and omissions with pertinent dates, which are believed to constitute the violations.”

The ARB also concluded that the “definitive and specific” evidentiary standard for SOX complaints previously applied in ARB decisions was not an appropriate test and that complainants do not need to demonstrate that their complaints “definitively and specifically” related to a SOX enumerated violation. Rather, according to the ARB in Sylvester, “the critical focus is on whether the employee reported conduct that he or she reasonably believes constituted a violation of federal law.” Further, the ARB disagreed with the ALJ’s conclusion that complainants must expressly allege shareholder fraud as SOX was intended to address corporate fraud generally not just securities fraud. Finally, the ARB held that complainants need not plead, prove or approximate the elements of a fraud claim to sufficiently allege that they were engaged in protected activity under SOX.

- *Wiest v. Lynch*, 710 F.3d 121 (3d Cir. 2013)

In *Wiest*, the Third Circuit applied *Chevron* deference to the ARB’s rejection of the “definitive and specific” standard, relying on *Sylvester* in holding that a reporting employee’s communication is protected under SOX if it reflects a subjective and objectively reasonable belief that the employer’s conduct relates to an existing or prospective violation of one of the provisions enumerated in Section 806.

Wiest was a former accountant for Tyco Electronics Corporation who questioned expense requests for various company events. After Tyco began investigating Wiest for alleged misconduct, he went on medical leave and was later terminated. Wiest sued under SOX and state law, alleging that he had been discharged for reporting improper expenditures. The district court dismissed the complaint, concluding that Wiest had failed to allege that his complaints to Tyco definitively and specifically related to a violation of a law or rule enumerated in Section 806. The Third Circuit reversed, holding that the ARB’s “reasonable belief” standard was entitled to *Chevron* deference. Thus, an employee must establish both a subjective, good faith belief that the employer violated a provision listed in SOX, and that this belief was objectively reasonable – i.e., that “a reasonable person with the same training and experience as the employee would believe that the conduct implicated in the employee’s communication could rise to the level of a violation of one of the enumerated provisions in Section 806.”

The Third Circuit also disagreed with the district court’s holding that an employee’s communication must allege the elements of a securities fraud violation. The Third Circuit found *Sylvester*’s rejection of such a requirement to be reasonable, concluding that a “whistleblower’s communication need not ring the bell on each element of one of the stated provisions of federal law to support an inference that the employer knew or suspected that the plaintiff was blowing the whistle on conduct that may fall within the ample reach of the anti-fraud laws listed in § 806.” To hold otherwise, the court said, “would eviscerate § 806,” noting that an employee might not have sufficient information to form a judgment on each element of a fraud claim yet still have “knowledge of facts sufficient to alert the employer to fraudulent conduct.” The Third Circuit also rejected the district court’s holding that an employee’s communication must reflect a
reasonable belief in an existing violation, endorsing Sylvester’s contrary conclusion that Section 806 also protects communications about prospective violations that the reporting employee believes are likely to occur. Applying the Sylvester standard, the Third Circuit found that Wiest had pleaded sufficient facts to show that some of the communications at issue were protected under Section 806, and reversed the district court’s dismissal as to these communications.

- *Lockheed Martin Corp. v. Administrative Review Bd.*, 717 F.3d 1121 (10th Cir. 2013)

In *Lockheed Martin*, the Tenth Circuit rejected a narrow interpretation of SOX that would have limited the protections of Section 806 to reports of conduct relating to fraud against shareholders.

Complainant Andrea Brown worked as a communications director for Lockheed from 2000 to 2008. In May 2006, Brown filed an anonymous ethics complaint against her supervisor, Vice President of Communications Wendy Owen, alleging that Owen had engaged in misconduct in connection with a pen pal program between Lockheed employees and U.S. soldiers deployed in Iraq. Brown alleged that Owen had engaged in sexual relationships with soldiers, sent pornography to soldiers, and used company funds to buy a laptop and other gifts for soldiers and to take soldiers to expensive hotels in limousines for sexual encounters. Brown believed that these costs were being passed on to the government as Lockheed’s customer, and “became concerned Owen’s actions were fraudulent and illegal and that there could be media exposure which could lead to government audits and affect the company’s future contracts and stock price.” In December 2006, Owen became aware that Brown had been behind the complaint. Subsequently, Brown received a lower performance evaluation. In March 2007, Brown began reporting to Judy Gan, the Senior Vice President of Communications, who had a negative attitude towards Brown and told her that she was not the right person for her position and that there would be a reduction in staff. In June 2007, Owen called Brown and told her that her job had been posted on the Internet and that she should get her resume together. Brown applied for the position but withdrew her application after Gan called her, told her she was not qualified for the position, and criticized her for applying. Lockheed hired David Jewell for the position. Jewell solicited Owen’s advice about the position and employees and was told that Brown had received imperfect evaluations in the past. Subsequently, Brown was asked to vacate her office and work from home or use a visitor office that doubled as a storage room. Brown was also denied permission to attend a conference she had previously attended at which she was to receive an award, told she or another employee would be laid off, and demoted. Brown then suffered an emotional breakdown and took medical leave.

Brown brought a complaint with OSHA alleging violations of SOX. An administrative law judge held that she had engaged in protected activity, that she had suffered adverse employment actions including constructive discharge, and that her protected activity was a contributing factor in the constructive discharge. The ALJ awarded Brown reinstatement, back pay, medical expenses, and $75,000 in non-economic compensatory damages. The ARB affirmed.
On appeal to the Tenth Circuit, Lockheed argued that despite the ALJ’s finding that Brown reasonably believed Owen had committed mail or wire fraud, Brown’s report was not protected under Section 806 because Owen’s conduct did not relate to fraud against shareholders. The Tenth Circuit rejected this argument, finding it inconsistent with the plain language of the statute: “The plain, unambiguous text of § 1514A(a)(1) establishes six categories of employer conduct against which an employee is protected from retaliation for reporting: violations of 18 U.S.C. § 1341 (mail fraud), § 1343 (wire fraud), § 1344 (bank fraud), § 1348 (securities fraud), any rule or regulation of the SEC, or any provision of Federal law relating to fraud against shareholders. Because 18 U.S.C. §§ 1341, 1343, 1344, and 1348 are all clearly provisions of federal law, Lockheed’s reading of the statute would render their enumeration in § 1514A(a)(1) wholly superfluous” in violation of basic principles of statutory construction. The Tenth Circuit also concluded that even if the statute were ambiguous, the ARB’s interpretation was permissible and thus entitled to *Chevron* deference.

The Tenth Circuit also noted that the ARB in *Sylvester* had repudiated the “definitive and specific” evidentiary standard for SOX complaints, but did not reach this issue because it found there was substantial evidence to support the ARB’s conclusion that Brown’s report was definitively and specifically related to the federal mail and wire fraud statutes. The court also held that the ARB’s finding that Brown’s complaint was a contributing factor in her constructive discharge was supported by the administrative record. The court cited the temporal proximity between Brown’s report and the adverse employment action, rejecting Lockheed’s argument that too much time had elapsed between Brown’s May 2006 complaint and January 2008 termination, noting that “the relevant time frame is not when the constructive discharge occurred, but when the conduct leading up to the discharge began. The Tenth Circuit also upheld that ARB’s application of the “cat’s paw” theory of liability, finding that the evidence supported the finding that Owen “poisoned” Gan and Jewell’s opinion of Brown.


The plaintiff in *Sharkey* brought to the bank’s attention her belief that a J.P. Morgan client was engaging in criminal activity and recommended based on an investigation that the bank sever its relationship with the client. The bank rejected Sharkey’s recommendation and terminated her employment. Sharkey then filed a SOX complaint with the DOL, which found in the bank’s favor and she subsequently filed an action in federal court. J.P. Morgan argued that Sharkey’s actions did not constitute protected activity because she reported illegal activities by a third party (client), not by the bank itself. The court observed that while there are no prior decisions on whether reporting fraud by a third party is protected activity, the broad purposes of SOX and the Dodd-Frank Act support a finding that reports of third-party fraud are protected under SOX.

A few months after *Sharkey*, the ARB reached a similar conclusion in *Funke v. Federal Express Corp.*, 2007-SOX-43 (ARB July 8, 2011), holding that an employee of Federal Express who reported suspected fraud by a Federal Express customer engaged in protected activity under SOX. The ARB also took an expansive view of its jurisdiction, holding that even though the
complainant had abandoned her third-party fraud claim on appeal, the claim was not waived before the ARB, as the ARB “is not necessarily bound by the legal theory of any party in determining whether a violation has occurred.”


The ARB in *Menendez* established a new and broader standard for what constitutes an adverse employment action under SOX. The ARB held that an employer’s action may rise to the level of adverse if it is “more than trivial,” even if the employee suffers no tangible employment harm.

Anthony Menendez worked for Halliburton as Director of Technical Accounting Research & Training. Menendez raised concerns about Halliburton’s accounting practices with the SEC and made a complaint to his company’s Audit Committee via email. The email contained Menendez’s name and contact information. Upon receiving the email complaint to the Audit Committee, Halliburton’s general counsel sent a litigation hold notice via email to members of company management and co-workers of Menendez. The email identified Menendez as having filed a complaint with the SEC. Menendez alleged that after co-workers became aware of his complaint, he was ignored and ostracized. He also claimed that he had an expectation that his identity would be kept confidential, even though he did not file his complaint anonymously and never specifically requested anonymity.

After leaving Halliburton several months later, Menendez filed a SOX complaint alleging retaliation, specifically that Halliburton had breached his confidentiality in disclosing his identity to other employees. An ALJ dismissed Menendez’s complaint on, among other grounds, that Halliburton’s breach of confidentiality did not qualify as an adverse employment action.

On appeal, the ARB disagreed, concluding that the ALJ had applied too strict a standard in requiring Menendez to show that he suffered “tangible job consequences” as a result of the breach of confidentiality. The ARB adopted the standard set in a 2010 decision applying a statute with similar wording to SOX (AIR 21) in which the ARB held that the term adverse action “refers to unfavorable employment actions that are more than trivial, either as a single event or in combination with other deliberate employer actions alleged.” *See Williams v. American Airlines*, 2007-AIR-004 (ARB Dec. 29, 2010).

The ARB also distinguished the standard applied in Title VII cases as established by *Burlington Northern & Santa Fe Railway Co. v. White*, 548 U.S. 53 (2006). According to the ARB, the Title VII standard, in which a plaintiff must show conduct that would dissuade a reasonable worker from making or supporting a charge of discrimination, is derived from different and narrower statutory language than the retaliation provisions of SOX. Thus, Menendez establishes a new standard for adverse actions under SOX and suggests that breach of an employee’s right to confidentiality can constitute an adverse employment action under SOX.
The ARB remanded for a determination of whether Menendez’s protected activity was a contributing factor in the adverse action, and if so, whether Halliburton could establish by clear and convincing evidence that it would have taken the same action absent Menendez’s whistleblowing. On remand, the ALJ determined that Halliburton had proved by clear and convincing evidence that it disclosed Menendez’s identity for legitimate business reasons and dismissed the complaint. Anticipating possible reversal, the ALJ also entered an alternate finding that Halliburton had failed to prove its affirmative defense and awarding Menendez damages.

Upon review, the ARB reversed the ALJ’s main holding. The ARB acknowledged that “in a strictly literal sense, the exposure of a whistleblower’s identity is always ‘caused’ by his whistleblowing,” but emphasized that “this seemingly circular logic is supported by sound policy reasons,” namely, protecting anonymity to promote reporting violations of law. As to Halliburton’s affirmative defense, the ARB held that the ALJ had applied the wrong standard by holding Halliburton to the lesser burden of showing that it acted for a “legitimate business reason,” as opposed to requiring a showing that it would have taken the adverse action even absent the protected activity. The ARB held that the evidence was insufficient as a matter of law to support a finding that Halliburton had proven its affirmative defense. The ARB affirmed the ALJ’s alternate award of $30,000 in damages for emotional distress and reputational harm and also awarded Menendez costs and attorney’s fees as the prevailing party.

- Vannoy v. Celanese Corp., 2008-SOX-00064, ARB Case No. 09-118 (ALJ July 24, 2013)

The ARB in Vannoy held that an employee’s admitted theft of confidential business documents from his company’s computer system may, depending on the circumstances, be protected activity under SOX.

Matthew Vannoy worked for Celanese in reconciling problems with the company’s corporate employee expense reimbursement system. He complained to management and to the IRS as part of its bounty program about expense reimbursement issues with respect to employee charges on company credit cards. During an investigation of a separate employee complaint regarding Vannoy, Celanese discovered that he had sent a document to his domestic partner’s personal email account containing the social security numbers of 1,600 current and former employees. Vannoy later claimed that while he was aware of the employer’s confidentiality policy, he took the data to support his IRS report.

Vannoy was terminated after twice refusing to participate in the investigation of his concerns regarding expense reimbursements. Thereafter, he brought a SOX retaliation claim. The ALJ dismissed the case on Celanese’s motion for summary judgment, holding that Vannoy did not engage in protected activity and that he was terminated for violating the company’s confidentiality policies.

The ARB reversed and remanded. The ARB held that Vannoy’s complaints to management and the IRS could constitute protected activity. To the extent Vannoy took
employee data as part of his efforts to facilitate his complaint to the IRS, SOX is intended to protect all “lawful” conduct to disclose misconduct. The ARB went on to state that since no criminal charges were brought against Vannoy for misappropriating the social security numbers, his conduct must have been lawful.

The ARB recognized that there is “a clear tension between a company’s legitimate business policies protecting confidential information and the whistleblower bounty programs created by Congress to encourage whistleblowers to disclose confidential company information in furtherance of enforcement of tax and securities laws.” In light of this tension, the ARB remanded the case to the ALJ for hearing on whether the information produced by Vannoy was the type of “original information” that Congress intended to protect and whether the manner of transmission was protected under SOX. Notably, the ARB did not instruct the ALJ to engage in any type of balancing of the employer’s need to protect its confidential information against the whistleblower’s right to gather evidence to support a SOX claim, as is typically done in Title VII and other discrimination cases involving this issue.

On remand, the ALJ determined that Vannoy’s conduct was protected activity. The ALJ found no support for Celanese’s argument that Vannoy had acted unlawfully, noting that he had not been charged or convicted of any crimes. The ALJ also found that Vannoy’s sole purpose in removing the confidential data was to support his whistleblower complaints, and thus his actions constituted protected activity under SOX. The ALJ also held that Vannoy’s protected activity was a contributing factor in his termination and that Celanese had failed to establish by clear and convincing evidence that it would have terminated Vannoy even absent the protected activity. The ALJ awarded Vannoy approximately $355,000 in back pay and front pay, $25,000 in emotional distress damages, and costs and attorney’s fees.

In contrast to the these recent decisions favoring employees, the First Circuit recently held in a case of first impression that SOX’s whistleblower protections do not extend to employees of private companies that are contractors or subcontractors of public companies. In Lawson v. FMR LLC, 670 F.3d 61 (1st Cir. 2012), cert. granted, 133 S. Ct. 2387 (2013), plaintiffs brought retaliation claims against their former employers, private companies that provided investment and management services for Fidelity mutual funds (collectively, the “Fidelity Management companies”), alleging that they were discharged for raising questions about accounting methodologies and concerns about inaccuracies in statements for certain Fidelity funds. Plaintiffs’ employers were subsidiaries of FMR LLC, a publicly traded company. The Fidelity Management companies moved to dismiss arguing that SOX’s whistleblower protections do not encompass employees of private companies that are contractors or subcontractors of publically-traded companies. The district court denied the motion.

The First Circuit reversed holding that the term “employee” as used in 18 U.S.C. section 1514A(a) refers only to employees of public companies. In so deciding, the court considered the plain language of the provision, as well as the title of section 806, which reads, “Protection for Employees of Publicly Traded Companies Who Provide Evidence of Fraud,” and the caption for section 1514A(a), which reads, “Whistleblower protection for employees of publicly traded companies.” In addition, the court noted that Congress used broader language elsewhere in SOX
where it intended to regulate non-public entities. The court further relied on legislative history and contrasted section 1514A(a) with the language of other federal statutes that explicitly extend whistleblower protection to employees of contractors. Finally, the court declined to give deference to the positions of the SEC and the DOL, which argued in favor of an expansive interpretation of the term “employee”.  

The Supreme Court granted certiorari in the case and heard oral argument on November 12, 2013. The Court’s decision will likely clarify the scope of SOX’s whistleblower protections.

II. DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT OF 2010

On July 21, 2010, President Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”). The legislation covers a wide range of topics in an effort to address the causes of the financial crisis of 2008 and 2009 that created vast turmoil and dislocations in the financial markets.

With respect to whistleblowing, the legislative history of the Dodd-Frank Act explains that “whistleblowers often face the difficult choice between telling the truth and the risk of committing ‘career suicide.’” It cites Madoff whistleblower Henry Markopolos’s congressional testimony that “[w]histleblower tips were 13 times more effective than external audits” at uncovering “fraud schemes in public companies.”

Thus, the Dodd-Frank Act includes significant new whistleblower incentives and protections, including the creation of SEC and Commodity Futures Trading Commission (CFTC) whistleblower programs, expansion of current whistleblower protections under the Sarbanes-Oxley Act of 2002, and a new whistleblower cause of action for employees performing tasks related to consumer financial products or services. The legislation “aims to motivate those with inside knowledge to come forward and assist the Government to identify and prosecute persons who have violated securities laws and recover money for victims of financial fraud.”

Significantly, the Dodd-Frank Act creates alternative paths for whistleblowers to assert their rights, often with different and conflicting rights and procedures. Enabling regulations to the SEC’s Whistle-blower Program became effective on August 12, 2011 and are codified at 17 C.F.R. Parts 240 and 249.

12 But see Spinner v. David Landau & Associates, 2010-SOX-029 (ARB May 31, 2012) (extending SOX coverage to accountant for a private firm that performed services for publicly traded companies).
15 Id.
16 Id.
A. Dodd-Frank Act Whistleblower Incentives

The Dodd-Frank Act provides powerful monetary incentives for whistleblowers to report securities and commodity law violations to the SEC and CFTC, as well as strong protections for doing so. Sections 748 and 922 of the Dodd-Frank Act provide that whistleblowers who provide the respective Commissions with original information about violations of securities or commodity laws to be awarded a share of between 10% and 30% of monetary sanctions ultimately imposed by the Commissions in actions where sanctions exceed $1 million.

Section 924(d) of the Dodd-Frank Act directs the SEC to establish a separate office to administer the SEC’s whistleblower program. The Office of the Whistleblower (OWB) is required to report annually to Congress on the office’s activities, whistleblower complaints, and the SEC’s response. In order to qualify for an award, whistleblowers must submit tips, complaints, and referrals to the OWB via e-mail, fax, or the SEC’s website, using Form-TCR.

The OWB issued its first full-year report in November 2012. During fiscal year 2012, the OWB received 3,001 whistleblower TCR forms from individuals in all 50 states, the District of Columbia, Puerto Rico, and 49 other countries. The most common categories of complaints were Corporate Disclosures and Financials (18.2%), Offering Fraud (15.5%), and Manipulation (15.2%). In fiscal year 2013, the OWB received 3,238 whistleblower TCRs, again with submissions from all 50 states, as well as the District of Columbia, the U.S. territories of Puerto Rico, Guam, and the U.S. Virgin Islands, and 55 foreign countries. The most common complaint categories in fiscal year 2013 were Corporate Disclosures and Financials (17.2%), Offering Fraud (17.1%), and Manipulation (16.2%).

The OWB posts a Notice of Covered Action for each SEC enforcement action in which a final judgment or order results in monetary sanctions exceeding $1 million. Once a Notice of Covered Action is posted, eligible whistleblowers have 90 days to submit a claim for an award. To date, there have been 431 final judgments or orders eligible for awards.

The SEC issued its first award under the whistleblower program on August 21, 2012, paying the maximum 30 percent payout allowed by law to a whistleblower who provided information relating to an ongoing multi-million dollar fraud. A court awarded more than $1 million in sanctions, and the whistleblower was paid about $50,000, or 30 percent of the approximately $150,000 that had been collected by the end of the fiscal year. The whistleblower

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was also eligible for further payouts based on additional collections or any increase in the amount of sanctions.23

Subsequently, several more whistleblowers have received awards. In August and September 2013, the SEC awarded approximately $125,000 to three whistleblowers for information they provided to help the SEC and the U.S. Department of Justice stop a sham hedge fund.24 On October 1, 2013, the SEC announced the largest whistleblower bounty to date, an award of more than $14 million to a whistleblower who provided information leading to an SEC enforcement action that recovered substantial investor funds.25 And on October 30, 2013, the SEC announced an award of more than $150,000 to a whistleblower whose information assisted in halting a scheme that was defrauding investors.26

While these recent bounties will likely encourage more whistleblowers to come forward with information, a New York state lawyer’s association recently issued an opinion concluding that attorneys cannot ethically obtain such awards by providing confidential information about their clients.27 The New York County Lawyers’ Association analyzed the duties of attorneys under the New York Rules of Professional Conduct, concluding that participation in the whistleblower bounty program would create a conflict of interest between attorneys and their clients.28

B. Dodd-Frank Act Whistleblower Protections

Section 922 of the Dodd-Frank Act amended the Securities Exchange Act of 1934 (Exchange Act) to add a new Section 21F, containing anti-retaliation protections for whistleblowers who report possible securities law violations.29 The statute prohibits retaliation against whistleblowers who provide information to the SEC; initiate, testify in, or assist any investigation or judicial or administrative action of the SEC related to such information; or make disclosures required or protected under SOX, the Exchange Act, 18 U.S.C. section 1513(e), and any other law, rule, or regulation subject to the SEC’s jurisdiction.30

An employee claiming retaliation under the Dodd-Frank Act may bring an action directly in federal district court (as opposed to the procedure under SOX, where a complainant is first

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25 Id.
26 Id.
28 Id.
required to file an administrative complaint with the Department of Labor, OSHA), and can take advantage of a longer statute of limitations and broader remedies than those available under SOX.\(^{31}\) Alternatively, the SEC can also enforce Dodd-Frank’s anti-retaliation protections on a whistleblower’s behalf.\(^{32}\)

The remedies available under Section 21F are more generous than those available to whistleblowers under SOX. Upon a finding of retaliation, Section 21F provides for the whistleblower’s reinstatement, \textit{double} \(\text{backpay}\) (as opposed to just \(\text{backpay}\), as under SOX), attorneys’ fees and other costs.\(^{33}\) There is no explicit provision for the recovery of non-pecuniary damages, such as emotional distress or loss of reputation damages.\(^{34}\) The Act does not provide for a trial by jury or for recovery of punitive damages.\(^{35}\)

1. **Retroactivity**

In \textit{Jones v. Southpeak Interactive Corp.}, a district court addressed the question of whether Dodd-Frank’s anti-retaliation provision, which became effective on July 22, 2010, could be applied retroactively to an alleged retaliatory discharge that occurred in August 2009.\(^{36}\) The court held that the statute did not apply retroactively. First, the court examined the text and history of the law and found that there was no clear congressional intent respecting retroactivity. The court then considered whether retroactive application would affect substantive rights, liabilities, or duties on the basis of conduct prior to the statute’s enactment. Because the Dodd Frank Act authorizes double-back pay, it increased the liability imposed under Sarbanes-Oxley, and thus retroactive application was not appropriate.

In \textit{Ott v. Fred Alger Mgmt., Inc.}, another district court considered the application of the Dodd-Frank Act to whistleblowing occurring both before and after the effective date of the statute.\(^{37}\) The plaintiff provided information to the SEC about an allegedly unlawful trading policy both before and after the law became effective. The parties did not dispute that the anti-retaliation provision does not apply retroactively. However, the defendant argued that the plaintiff did not engage in “protected activity” under the Dodd-Frank Act because she did not provide “new” information to the SEC since she had already made the SEC aware of the policy before the statute’s enactment. The defendants cited a comment in which the SEC took the position that applying Section 21F prospectively, “for new information provided to the Commission after the statute’s enactment and not to information previously submitted,” was most consistent with the statutory language and congressional intent.\(^{38}\) The court rejected this

\(^{31}\) 15 U.S.C. §§ 78u-6(h)(1B)(i), (iii).
\(^{32}\) 17 C.F.R. § 240.21F-2(b)(2).
argument, noting that the SEC comment upon which the defendants relied was made in the context of the “bounty” provision of Section 21F, not the anti-retaliation provision, and that SEC regulations state that “the anti-retaliation protections apply whether or not [a whistleblower satisfies] the requirements, procedures and conditions to qualify for an award.” The court also noted that even if the plaintiff’s reporting had occurred entirely before the Dodd-Frank Act’s effective date, she might still have been protected under the anti-retaliation provision because the alleged adverse actions occurred after the statute’s effective date.

2. Courts Split Over Reconciling Whistleblower Definition and Anti-Retaliation Protections

Many of the recent cases interpreting the Dodd-Frank Act have focused on an apparent inconsistency between the statute’s definition of the term “whistleblower” and the scope of the statute’s anti-retaliation whistleblower protections. Section 922 of the Dodd-Frank Act defines a whistleblower as “any individual who provides, or 2 or more individuals acting jointly who provide, information relating to a violation of the securities laws to the Commission, in a manner established, by rule or regulation, by the Commission.”

Based on this statutory language, it would appear that the anti-retaliation provision only covers individuals who provide information “to the Commission.” However, both the SEC and the first federal district courts to address the issue interpreted scope of the Act’s protections far more broadly.

On May 4, 2011, a district court judge in the Southern District of New York issued the first decision interpreting the scope of Dodd-Frank’s whistleblower anti-retaliation provisions. In Egan v. TradingScreen, Inc., Judge Leonard Sand interpreted the anti-retaliation provisions of Section 21F of the Dodd-Frank Act as covering not only whistleblowers who provide information to the SEC, but also individuals whose disclosures are “required or protected” under the Sarbanes-Oxley Act (“SOX”), the Securities Exchange Act, 18 U.S.C. § 1513(e), or any other law, rule, or regulation subject to the SEC’s jurisdiction.

Egan claimed that his employment was terminated after he informed the company’s President that its CEO was diverting the company’s corporate assets to another company that the CEO solely owned. Egan asserted that his termination under these circumstances constituted unlawful retaliation under Section 21F. The defendants moved to dismiss Egan’s retaliation claim on the ground that he was not a “whistleblower” covered by Dodd-Frank, because Egan made his reports to TradingScreen, not to the SEC.

The court noted that Dodd-Frank’s definition of “whistleblower,” found at 15 U.S.C. section 78u-6(a)(6), defines the term to mean individuals who provide information to the SEC. The court acknowledged that if Congress wanted to extend whistleblower protections to

39 Id. at *5 (quoting 17 C.F.R. § 240.21F-2(b)(1)(iii)).
individuals beyond those who report to the SEC, it could have explicitly done so. But the court then looked the statute’s anti-retaliation provision, found at 15 U.S.C. section 78u-6(h)(1)(A), and noted that, in addition to protecting lawful acts done by the whistleblower to provide information or testimony to the SEC, sub-section 78u-6(h)(1)(A)(iii) protects whistleblower disclosures that are required or protected under: (1) the Sarbanes-Oxley Act; (2) the Securities Exchange Act; (3) 18 U.S.C. § 1513(e); and (4) any other law, rule, or regulation subject to the jurisdiction of the Commission.

The court determined that this created a contradiction in the statute, as “a literal reading of the definition of the term ‘whistleblower’ in 15 U.S.C. § 78 u-6(a)(6), requiring reporting to the SEC, would effectively invalidate § 78u-6(h)(1)(A)(iii)’s protection of whistleblower disclosures that do not require reporting to the SEC.” The court then determined that “[t]he contradictory provisions of the Dodd-Frank Act are best harmonized by reading 15 U.S.C. § 78u6(h)(1)(A)(iii)’s protection of certain whistleblower disclosures not requiring reporting to the SEC as a narrow exception to 15 U.S.C. § 78u-6(a)(6)’s definition of a whistleblower as one who reports to the SEC.”

Thus, under the court’s reading of the statute, a plaintiff asserting a section 21F retaliation claim must either:

- allege that his information was reported to the SEC, or that his disclosures fell under the four categories of disclosures delineated by 15 U.S.C. § 78u-6(h)(1)(A)(iii) that do not require such reporting: those under the Sarbanes-Oxley Act, the Securities Exchange Act, 18 U.S.C. § 1513(e), or other laws and regulations subject to the jurisdiction of the SEC.

The court dismissed Egan’s claim without prejudice, permitting Egan to amend his complaint to include factual allegations in accordance with the standards it articulated.42

The SEC, in its final regulations adopted on May 25, 2011, took the same position as the district court in Egan that a whistleblower need not make a disclosure to the SEC to be protected under section 21F. Rather, under the agency’s interpretation, an individual is a protected whistleblower if he or she provides covered information in a manner described in 15 U.S.C. section 78u-6(h)(1)(A), i.e., the individual either provides the information to the SEC or in a disclosure otherwise required or protected under SOX, the Exchange Act, 18 U.S.C. 1513(e), or any other law, rule, or regulation subject to the SEC’s jurisdiction.43

The implications of this interpretation adopted by the SEC and the district court in Egan are significant: if any SOX-protected disclosures fall within the scope of Dodd-Frank’s whistleblower provisions whether or not the employee reports to the SEC (despite the statutory definition of “whistleblower” as someone who reports “to the Commission”), employees in any

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42 Egan amended his complaint, and the defendants subsequently moved to dismiss the amended complaint. On September 12, 2011, the court granted the defendants’ motion to dismiss, finding that Egan had not pleaded facts in accordance with the standards it articulated.

43 17 C.F.R. § 240.21F-2(b).
SOX matter will arguably be able to bring their whistleblower retaliation claims under Dodd-Frank instead of SOX. Dodd-Frank has an expansive six to ten-year statute of limitations (as opposed to SOX’s 180-day statute of limitations), a direct right of action in federal district court, as opposed to having to exhaust remedies before OSHA, and double back-pay damages. Thus, based on this interpretation of the Act, plaintiffs may opt to pursue SOX claims under the more employee-favorable provisions of Dodd-Frank, including claims that might otherwise be time-barred under SOX, instead of under OSHA’s administrative scheme. Such a shift in strategy could greatly diminish OSHA’s role in investigating and adjudicating SOX cases going forward, and could lead to the 180-day SOX statute of limitations becoming obsolete. The comments to the SEC’s regulations did not address these implications with respect to the existing SOX statutory scheme. Nor did the court’s opinion in Egan address the issue, probably because TradingScreen was not a SOX-covered entity.

A number of other district courts have followed Egan and the SEC and interpreted Dodd-Frank’s anti-retaliation provision to protect internal reporting.\(^\text{44}\) Several courts have concluded that the statute is ambiguous and have given Chevron deference to the SEC’s interpretation.\(^\text{45}\) However, the Fifth Circuit and at least one district court have taken a narrower view. In Asadi v. G.E. Energy (USA), L.L.C., the Fifth Circuit explained that, when “faced with questions of statutory construction, [courts] must first determine whether the statutory text is plain and unambiguous, and if it is . . . must apply the statute according to its terms.”\(^\text{46}\) In addition, “a court should give effect, if possible, to every word and every provision Congress used.” Applying these principles to the Dodd-Frank Act, the Asadi court “start[ed] and end[ed] [its] analysis with the text of the relevant statute—15 U.S.C. § 78u-6.” First, the Fifth Circuit found that the statute’s definition of a whistleblower “expressly and unambiguously requires that an individual provide information to the SEC to qualify as a ‘whistleblower’ for purposes of § 78u-6.” Next, the Fifth Circuit held that the “perceived conflict” between this definition and the anti-retaliation provision recognized by various district courts and the SEC “rests on a misreading of the operative provisions of § 78u-6.” The Fifth Circuit explained that under the “plain language and structure” of the statute, there is only one category of Dodd-Frank whistleblowers: “individuals who provide information relating to a securities law violation to the SEC.” The categories of activity protected by the anti-retaliation provision of section 78u-6(h)(1)(A) do not conflict with the whistleblowing provision; they define the scope of the protection available to whistleblowers. The plaintiff’s interpretation, the court said, would impermissibly read the words “to the Commission” out of the definition of “whistleblower” for purposes of the anti-retaliation provision, violating the principle that every word is to be given effect.


\(^{46}\) Asadi v. G.E. Energy (USA), L.L.C., 720 F.3d 620, 622 (5th Cir. 2013) (quotation marks and alteration omitted).
The Fifth Circuit also noted that to construe the Dodd-Frank Act’s anti-retaliation provision to extend beyond the statutory definition of “whistleblowers” would render SOX’s whistleblower provision moot for practical purposes. The court explained that individuals would be unlikely to file SOX anti-retaliation claims, with their administrative exhaustion requirement, much shorter statute of limitations, and more limited damages, instead of simply filing Dodd-Frank Act claims, if the Dodd-Frank Act’s anti-retaliation provision overlapped with SOX in covering reports to company management. Finally, the Fifth Circuit held that it did not owe deference to the SEC’s broader interpretation of the anti-retaliation provision as covering internal reports to company management because the statute was clear and unambiguous.

Post-Asadi district court decisions have split over the proper interpretation of these provisions. At least two district courts in other circuits have expressly disagreed with the Fifth Circuit, finding the statute to be ambiguous and granting deference to the SEC’s interpretation. By contrast, a district court in the Northern District of California followed the Asadi court’s reasoning, holding that the statute is not ambiguous and does not protect individuals who do not meet the statute’s definition of a whistleblower.

3. Extraterritoriality

At least two district courts have taken the position that the Dodd-Frank Act’s anti-retaliation provision does not cover employees working outside the United States. The lower court in the Asadi case dismissed the plaintiff’s claim on the ground that the provision does not apply extraterritorially, an issue not reached by the Fifth Circuit in its decision.

The plaintiff in the case alleged that he was a U.S.-based employee who was working in Jordan pursuant to a temporary relocation when he became aware of a possible violation of the Foreign Corrupt Practices Act (“FCPA”) by G.E. Energy (USA), LLC in Iraq. The plaintiff alleged that, after reporting his concern to the company, he received a negative performance review, was pressured to step down, and was ultimately terminated from his position. In analyzing whether the Dodd-Frank Act’s anti-retaliation provision could apply extraterritorially, the court cited the “longstanding principle” that congressional legislation does not apply outside the United States “unless a contrary intent appears.” The court explained that the Dodd-Frank Act’s anti-retaliation provision is silent on the question, creating a presumption that it does not apply extraterritorially. The court further noted that other sections of the act explicitly address their extraterritorial scope in limited contexts, which strengthened the conclusion that the anti-retaliation provision does not apply extraterritorially.

The court also rejected the plaintiff’s argument that SOX or the FCPA could extend the application of the Dodd-Frank Act. Regarding SOX, the court held that the provisions upon which the plaintiff relied were either inapplicable or themselves did not apply extraterritorially.

47 See Ellington, 2013 WL 5631046 at *2-3; Rosenblum, 2013 WL 5780775 at *4-5.
49 See 720 F.3d at 621, 630 n.13.
The court found the plaintiff’s reliance on the FCPA misplaced because the FCPA does not “protect” or “require” reporting of violations, and thus the plaintiff’s allegations of FCPA violations could not constitute “disclosures that are required or protected” under the relevant law. Thus, the court held that the Dodd-Frank Act’s anti-retaliation provision did not cover Asadi.

The court in Liu v. Siemens A.G. reached a similar conclusion. In Liu, a Taiwanese citizen alleged that he had been terminated for reporting possible violations of the FCPA in North Korea and China by Siemens China, a subsidiary of Siemens A.G., a German corporation. The court followed the reasoning of the Asadi court in holding that the Dodd-Frank Act’s anti-retaliation provision does not apply extraterritorially.

4. Pre-Dispute Arbitration Agreements/Waivers of Claims

Section 21F does not explicitly ban pre-dispute arbitration agreements or waivers of claims. However, in the comments to the regulations, the SEC has taken the position that such language is unnecessary because section 29(a) of the Exchange Act provides that “any condition, stipulation, or provision binding any person to waive compliance with any provision of this title or any rule or regulation thereunder . . . shall be void.” The comments conclude, “Thus, under Section 29(a), employers may not require employees to waive or limit their anti-retaliation rights under Section 21F.”

In the first federal district court decision to address the issue, however, the court in Ruhe v. Masimo Corp. compelled arbitration of a retaliation claim under Section 21F, holding that the plain wording of the statute contains no provision rendering pre-dispute arbitration agreements unenforceable. The court determined that it could not read such a provision into the statute where it did not exist. It remains to be seen whether other courts will follow the reasoning in Ruhe or whether they will find the comments to the SEC’s regulations persuasive.

C. New Consumer Financial Whistleblower Protections

The Dodd-Frank Act also creates a new whistleblower cause of action for employees performing tasks related to the offering or provision of consumer financial products or services. Section 1057 of the Dodd-Frank Act prohibits retaliation against employees who provide information to their employers or to the government they reasonably believe to be a violation of the Consumer Financial Protection Act of 2010 (which is Title X of the Dodd-Frank Act) or any other provision of law subject to the jurisdiction of the Bureau of Consumer Financial Protection. This provision also protects employees who object to, or refuse to participate in, any activity that the employee reasonably believes to be a violation of any law, rule, or standard of the Bureau, who testify in proceedings relating to same, or who file, institute or cause to be filed any

52 76 Fed. Reg. at 34,304.
53 Id.
proceeding under any Federal consumer financial law. Aggrieved employees are required to file a complaint with the Department of Labor, OSHA within 180 days of an alleged violation, and the procedure for handling such complaints, as well as the burdens of proof, remedies, and ability of a complainant to file an action in federal district court and demand a jury trial, are somewhat similar to the scheme to which employers and employees have become accustomed under SOX.

Employees may not waive their rights and remedies under Section 1057 by any “agreement, policy, form or condition of employment, including any pre-dispute arbitration agreement.” Thus, employers will typically be unable to compel arbitration of claims under Section 1057 based on pre-dispute arbitration agreements.