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U.S. Supreme Court Narrows Scope of Whistleblower Anti-Retaliation Protections

On February 21, 2018, in *Digital Realty Trust Inc. v. Somers*, the Supreme Court resolved a circuit split on the question of whether the anti-retaliation protections for whistleblowers under the Dodd-Frank Act extend to individuals who report allegations of misconduct internally or only to those who report such allegations directly to the Securities and Exchange Commission (the “SEC” or the “Commission”).¹ The Court held that individuals who have reported alleged misconduct internally, but not to the SEC, are not covered by the anti-retaliation provisions of the Dodd-Frank Act, 15 U.S.C. § 78u-6(h).

The Supreme Court’s decision could have a significant impact on potential whistleblowers and employers. Current data reflects that whistleblowers overwhelmingly report their concerns internally before reporting them to the SEC. The Court’s narrowing of the definition of “whistleblower” to those who report their concerns directly to the SEC may potentially discourage employees from utilizing internal reporting mechanisms and encourage immediate reporting to the SEC. Given the availability of other remedies, including under the Sarbanes-Oxley Act, however, as well as various other federal and state statutes, it remains to be seen whether the requirement of reporting to the SEC will significantly affect behavior.

In addition, while two Courts of Appeals (the Second and Ninth Circuits) had afforded deference to the SEC’s broader interpretation of the statute, the Supreme Court declined to do so, concluding that the statute was unambiguous, based on both the statutory text and the “purpose and design” of Dodd-Frank. The Court’s opinion may signal a shift away from agency deference.

Background on the Statutory Framework

The *Digital Realty* case implicates two statutes and their interplay: the Sarbanes-Oxley Act and the Dodd-Frank Act.

Congress enacted Sarbanes-Oxley in 2002 as a response to the Enron collapse. Sarbanes-Oxley sought to “safeguard investors in public companies and restore trust in the financial markets.”² As part of that goal, Sarbanes-Oxley provided certain protections to employees who report alleged securities violations to the SEC, any member of Congress, or to a “person with supervisory authority over the employee (or such other person working for the employer who has the authority to investigate, discover, or terminate

¹ *Digital Realty Tr., Inc. v. Somers*, 583 U.S. ____ (2018).

² *Lawson v. FMR LLC*, 134 S. Ct. 1158, 1161 (2014).

misconduct).³ The Sarbanes-Oxley anti-retaliation provision therefore protects individuals who report internally.

To take advantage of the anti-retaliation protections afforded by Sarbanes-Oxley, an employee must first file a complaint with the Department of Labor within 180 days of the alleged violation or of when the employee became aware of the alleged violation.⁴ If the Secretary of Labor has not issued a final decision within 180 days of the complaint, the employee may file an action in federal district court for de novo review.⁵ Conversely, if the agency denies the employee's claim, the employee may file a petition for review to a Court of Appeals, which will review the denial under the deferential "substantial evidence" standard.⁶ If the employee's claim is successful, the employee is entitled to reinstatement, back pay, and non-economic, special damages.⁷

Eight years after passing the Sarbanes-Oxley Act, in 2010, Congress enacted the Dodd-Frank Act. Like Sarbanes-Oxley, the Dodd-Frank Act also sought to encourage reporting of securities violations and to protect whistleblower employees from retaliation. The whistleblower protections in Dodd-Frank differ from those in Sarbanes-Oxley in several key respects. Dodd-Frank provides a private right of action for whistleblowers to bring suit in federal court, and it establishes a six- to ten-year statute of limitations for such claims.⁸ And although Dodd-Frank provides for reinstatement and double back pay, it does not expressly provide for special damages.⁹

Less clear in Dodd-Frank, however, was who qualified as a whistleblower entitled to relief under its anti-retaliation provision. "Whistleblower" is defined in the statute 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."¹⁰ The parties in *Digital Trust* agreed that this narrow definition applies to certain provisions of Dodd-Frank, such as the provision providing for a monetary award for whistleblowers who provide "original information to the

³ 18 U.S.C. § 1514A(a).

⁴ See 18 U.S.C. § 1514A(b)(2).

⁵ See 18 U.S.C. § 1514A(b)(1).

⁶ 29 C.F.R. § 1980.112. Under the "substantial evidence" standard of review, courts will uphold a formal agency adjudicative ruling if the agency's decision is supported by such "relevant evidence as a reasonable mind might accept as adequate to support a conclusion." *Consol. Edison Co. of New York v. N.L.R.B.*, 305 U.S. 197, 229 (1938).

⁷ See 18 U.S.C. § 1514A(c).

⁸ See 15 U.S.C. § 78u-6(h)(1).

⁹ See 15 U.S.C. § 78u-6(h)(1).

¹⁰ See 15 U.S.C. § 78u-6(a)(6).

Commission that led to the successful enforcement” of an action resulting in monetary sanctions over \$1 million.¹¹

The parties disputed, however, whether the narrow definition applies to Dodd-Frank’s anti-retaliation provisions, which directly reference the broader activity (such as internal reporting) protected under Sarbanes-Oxley. Specifically, Dodd-Frank’s anti-retaliation provision states:

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—

- in providing information to the Commission in accordance with this section;
- 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
- in making disclosures that are required or protected under the Sarbanes-Oxley Act of 2002¹² . . . and any other law, rule, or regulation subject to the jurisdiction of the Commission.¹³

The third subsection of the Dodd-Frank anti-retaliation provision (“Subsection (iii)”) protects whistleblowers who make disclosures that are protected under the Sarbanes-Oxley anti-retaliation provision. Since the Sarbanes-Oxley anti-retaliation provision protects whistleblowers who report potential wrongdoing internally, Dodd-Frank’s incorporation of disclosures protected by Sarbanes-Oxley raised questions about whether the Dodd-Frank Act also protects internal reporting.

The SEC’s Statutory Interpretation

In 2011, the SEC weighed in on the scope of Dodd-Frank’s anti-retaliation provisions.¹⁴ Under the SEC’s implementing rule (“Rule 21F”), for “purposes of the anti-retaliation protections,” a person is a whistleblower if the person provides information in a manner described in the anti-retaliation provision of Dodd-Frank that references Sarbanes-Oxley.¹⁵ And in 2015, the SEC issued an interpretation of Rule 21F, clarifying that “[u]nder [the SEC’s] interpretation, an individual who reports internally and suffers

¹¹ See 15 U.S.C. 78u-6(a)(1), (b)(1).

¹² 15 U.S.C. 7201 et seq.

¹³ 15 U.S.C. § 78u-6(h)(1)(A).

¹⁴ See Exchange Act Rule 21F-2, 17 C.F.R. § 240.21F-2.

¹⁵ Rule 21F-2(b)(1).

employment retaliation will be no less protected than an individual who comes immediately to the Commission.”¹⁶

One of the issues implicated by *Digital Realty* was whether the SEC’s interpretation should be given *Chevron* deference by the Court. Under *Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, “administrative implementation of a particular statutory provision qualifies for *Chevron* deference when it appears that Congress delegated authority to the agency generally to make rules carrying the force of law, and that the agency interpretation claiming deference was promulgated in the exercise of that authority.”¹⁷

Determining whether an agency interpretation is entitled to *Chevron* deference involves a two-step process. First, the Court considers “whether Congress has directly spoken to the precise question at issue.”¹⁸ “If so, then the inquiry is over, and [the Court] must give effect to the ‘unambiguously expressed intent of Congress.’”¹⁹ But “if the statute is silent or ambiguous with respect to the specific issue,” the Court must proceed to the second step and determine whether the agency’s interpretation is “based on a permissible construction of the statute.”²⁰ If the agency’s interpretation of the statute “‘is a reasonable one, th[e] court may not substitute its own construction of the statutory provision,’ even if the Court believes the provision would best be read differently.”²¹

Conflicting Decisions Had Created a Circuit Split

Since Dodd-Frank’s enactment, three Courts of Appeal have addressed the question of whether Dodd-Frank’s anti-retaliation protections extend only to employees who report misconduct to the SEC or also to employees who report misconduct internally. The Fifth Circuit was the first Court of Appeals to address the issue. The court held that a whistleblower who only reported misconduct to an internal supervisor was not protected by Dodd-Frank’s anti-retaliation provision.²² In so holding, the Fifth Circuit held that the definition of “whistleblower” plainly and unambiguously precluded relief for the whistleblower who only reported internally, and that there was no conflict between the definition and the anti-retaliation

¹⁶ Interpretation of the SEC’s Whistleblower Rules Under Section 21F of the Sec. Exch. Act of 1934, SEC Release No. 34-75592, 2015 WL 4624264 (Aug. 4, 2015).

¹⁷ *United States v. Mead Corp.*, 533 U.S. 218, 226–27, 121 S. Ct. 2164, 150 L.Ed.2d 292 (2001).

¹⁸ *Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837, 842 (1984).

¹⁹ *Id.*

²⁰ *Id.* at 843.

²¹ *Somers v. Digital Realty Tr. Inc.*, 119 F. Supp. 3d 1088, 1096 (N.D. Cal. 2015), *aff’d*, 850 F.3d 1045 (9th Cir. 2017), *rev’d and remanded*, *Digital Realty*, 583 U.S. ____ (2018).

²² *See Asadi v. G.E. Energy (USA), L.L.C.*, 720 F.3d 620 (5th Cir. 2013).

provision.²³ Significantly, the Fifth Circuit indicated that the two sections of the statute could be reconciled because the anti-retaliation provision would cover an employee who reported a violation to both a supervisor and the SEC. Because the Fifth Circuit held the statute to be unambiguous, it did not defer to the SEC's interpretation.

The Second Circuit held differently when it addressed the issue two years later. A divided panel of the court held the statutory language to be ambiguous and deferred to the SEC's interpretation. The Second Circuit noted that the Fifth Circuit's interpretation would leave the subdivision of the anti-retaliation provision that refers to Sarbanes-Oxley "with an extremely limited scope."²⁴ For example, the number of whistleblowers who report both to the SEC and an internal supervisor would "likely . . . be few in number."²⁵ And "more significant" for the Second Circuit panel was that attorneys and auditors are required to report wrongdoing to their employer before reporting to the Commission.²⁶

In *Digital Realty*, a divided Ninth Circuit panel went even further than the Second Circuit. The court noted that statutory definitions are "just one indication of meaning,"²⁷ and that "[r]eading the use of the word 'whistleblower' in the anti-retaliation provision to incorporate the earlier, narrow definition would make little practical sense and undercut congressional intent."²⁸ The court held that, under the principles of statutory interpretation, Dodd-Frank's anti-retaliatory provisions include whistleblowers who report only internally. The Ninth Circuit also observed that, were there any ambiguity in the statute, the SEC's interpretation should be afforded deference.

The Supreme Court's Opinion

In the February 21, 2018 opinion authored by Justice Ginsburg and joined by Chief Justice Roberts, and Justices Kennedy, Breyer, Sotomayor and Kagan, the Supreme Court reversed the Ninth Circuit's decision and held that the Dodd-Frank anti-retaliation provisions only protect individuals who report potential securities law violations to the SEC.

Justice Ginsburg's opinion states that, when a statute includes an explicit definition, courts are required to follow that definition, even if it departs from the term's ordinary meaning.²⁹ In this case, the Court

²³ *Id.* at 627.

²⁴ *Berman v. Neo@Ogilvy LLC*, 801 F.3d 145, 151 (2d Cir. 2015) *abrogated by Digital Realty*, 583 U.S. ____ (2018).

²⁵ *Id.*

²⁶ *Id.* at 151-52.

²⁷ *Somers v. Digital Realty Tr. Inc.*, 850 F.3d 1045, 1049 (9th Cir. 2017) (quoting Antonin Scalia & Bryan A. Garner, *Reading Law: The Interpretation of Legal Texts* 228 (2012)), *rev'd and remanded*, *Digital Realty*, 583 U.S. ____ (2018).

²⁸ *Id.*

²⁹ *Digital Realty*, 583 U.S. at ____ (slip op., at 9).

found that the statutory definition of the term “whistleblower” only includes individuals who report to the SEC, and the statute provides that the definition “shall apply” throughout the relevant section.³⁰ Thus, the Court concluded that the definition describes *who* is eligible for whistleblower protections, whereas the subsections of the anti-retaliation provisions describe what conduct is protected—when performed by a whistleblower. Individuals who do not qualify as whistleblowers are therefore not protected.

The Court also noted that a different section of the Dodd-Frank Act, which created the Consumer Financial Protection Bureau (“CFPB”), includes a whistleblower protection provision that does not require individuals to report to the CFPB or any other entity.³¹ In the Court’s view, since Congress imposed a government-reporting requirement on the Dodd-Frank whistleblower provision but did not impose the same requirement with respect to another anti-retaliation provision in the same statute, courts cannot dispense with the reporting requirement.

The Supreme Court also found that the “purpose” of Dodd-Frank “corroborate[d]” the Court’s interpretation.³² Specifically, the purpose of the Dodd-Frank anti-retaliation provision is “to motivate people who know of securities law violations to *tell the SEC*.”³³ Relying on the statute’s legislative history, the Court noted that, by requiring individuals to report to the SEC in order to obtain protection under the Dodd-Frank anti-retaliation provision, Congress intended to enhance SEC enforcement and help the SEC recover money for victims of financial fraud.³⁴ This contrasts with the broader goal of the Sarbanes-Oxley Act, which sought to disrupt the “corporate code of silence” and encourage even internal reporting.³⁵

Finally, because the Court found that the statutory definition was unambiguous, deference to the SEC’s position that internal reporting is protected was not warranted under *Chevron*.³⁶

Justice Thomas wrote a concurrence, which Justices Alito and Gorsuch joined, clarifying that he joined the opinion “only to the extent it relies on the text of the Dodd-Frank Wall Street Reform and Consumer Protection Act.”³⁷ The concurrence states that the question is whether the term “whistleblower” in the Dodd-Frank anti-retaliation provision includes persons who did not report to the SEC. This question, the

³⁰ *Id.*

³¹ *Id.* at 10.

³² *Id.* at 11.

³³ *Id.* (quoting S. Rep. No. 111-176, p. 38 (2010) (emphasis added)).

³⁴ *Digital Realty*, 583 U.S. at ___ (slip op., at 11).

³⁵ *Id.* at 11-12 (quoting *Lawson*, 571 U.S. 429, at ___ (2014) (slip op., at 4)).

³⁶ *Id.* at 18-19.

³⁷ *Digital Realty*, 583 U.S. at ___ (Thomas, J., concurring in part and concurring in the judgment) (slip op., at 1).

concurrence argued, is resolved by the statutory language alone.³⁸ He disagreed with the Court's opinion to the extent that it relied on legislative history and declined to join the portions of the Court's opinion that did so.

Justice Sotomayor wrote a concurrence, which Justice Breyer joined, to note her disagreement with Justice Thomas's concurrence.³⁹ She wrote that, even when the meaning of the statute can be clearly ascertained from its text, consulting legislative history can still be useful.⁴⁰

Conclusion

The Supreme Court's decision to restrict whistleblower protections only to employees who report information directly to the SEC may encourage employees to bypass internal reporting mechanisms. Indeed, the Solicitor General, acting as *amicus curiae*, argued that Digital Realty's reading of the statute would "eviscerate the incentive for internal reporting."⁴¹ Data reflects that currently, most employees who report alleged misconduct to the SEC had previously made an internal report. According to the SEC's 2017 Annual Report to Congress: Whistleblower Program, approximately 83% of those who received monetary awards under Dodd-Frank raised their concerns internally before reporting to the Commission.⁴² Eliminating Dodd-Frank's anti-retaliation protection for employees who are terminated prior to reporting to the SEC may well result in less internal reporting. Although employees who only report internally may still seek relief under the anti-retaliation provisions of Sarbanes-Oxley, they must meet the shorter statute of limitations and exhaust administrative remedies before seeking relief in a federal court.

This narrow interpretation also may have the undesirable effect of weakening the role of corporate compliance programs. Most companies encourage internal reporting as an early warning system to protect against fraud and other securities violations. The SEC regulations also provide incentives for internal reporting by employees.⁴³ The Supreme Court's decision, however, may discourage employees from utilizing internal reporting systems.

Finally, the *Digital Realty* decision may signal a shift away from *Chevron* and agency deference. While the Court engaged in statutory interpretation, including a review of legislative history, it declined to afford deference to the SEC's interpretation, holding that no such deference was warranted. *Digital Realty*

³⁸ *Id.*

³⁹ *Digital Realty*, 583 U.S. ____ (Sotomayor, J., concurring) (slip op., at 1).

⁴⁰ *Id.* at 3.

⁴¹ Transcript of Oral Argument at 53:2–6, *Digital Realty Tr. Inc. v. Somers.*, 137 S. Ct. 2300 (2017) (No. 16-1276).

⁴² U.S. Securities and Exchange Commission, 2017 Annual Report to Congress: Whistleblower Program 17 (2017).

⁴³ *See, e.g.*, Rule 21F-6, 17 C.F.R. § 240.21F-6(a)(4).

therefore appears to follow the trajectory of *King v. Burwell*,⁴⁴ reaffirming the principle that it is the province of the courts to interpret statutes. In *Burwell*, the Supreme Court recognized that the statutory text was ambiguous but that the “statutory scheme” and the “broader structure” of the statute rendered the statute unambiguous.⁴⁵ Although the *Digital Realty* Court held that the statute’s “explicit definition” of “whistleblower” was unambiguous, clear, and conclusive, the Court also noted that the statute’s “purpose and design” corroborated the Court’s view of the statutory language. The Supreme Court’s decision may encourage other courts to engage in statutory interpretation unguided by agency interpretation.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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⁴⁴ 135 S. Ct. 2480 (2015).

⁴⁵ *Id.* at 2492-93.