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Expert Analysis

Whistleblower Developments In Courts and Agencies

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Whistleblower activity is on the rise under both Section 922 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, 15 USC §78u-6 (Dodd-Frank), and Section 806 of the Sarbanes-Oxley Act, 18 USC §1514A (SOX), which protect individuals who report conduct they reasonably believe constitutes a violation of federal law relating to financial, securities or shareholder fraud. On Nov. 16, 2015, the Securities and Exchange Commission's (SEC) Office of the Whistleblower (OWB) released its Annual Report on the Dodd-Frank Whistleblower Program, in which OWB reports 3,923 tips from whistleblowers in 2015—an increase of 8 percent over 2014 and an increase of 30 over 2012, the first year of the program.

The report also highlights that OWB paid more than $37 million to eight whistleblowers in 2015. See U.S. Sec. & Exch. Comm'n, 2015 Annual Report to Congress on the Dodd-Frank Whistleblower Program (2015), https://www.sec.gov/whistleblower/reportspubs/ annual-reports/owb-annual-report-2015.pdf. Likewise, according to recent figures released by the Occupational Safety and Health Administration (OSHA) which enforces the whistleblower provisions of SOX, there was a 7 percent increase in the number of SOX whistleblower cases filed in fiscal year 2015 as compared to fiscal year 2014. See U.S. Dept. of Labor, Whistleblower Investigation Data: FY2005-FY2015 (2015), http://www.whistleblowers.gov/wb_data_FY05-15.pdf.

As whistleblower activity has increased, there have been a number of significant whistleblower cases and developments in the last year. This month's column reviews some of these important developments.

SOX Procedures

OSHA published a Final Rule governing whistleblower retaliation complaints filed under SOX on March 5, 2015, more than three years after the notice and comment period of the Interim Rule. The Final Rule implements the procedures and timelines for handling whistleblower complaints under SOX, which was necessitated by 2010 amendments to SOX by Dodd-Frank.

At the complaint stage, whistleblowers now have 180 days (extended from the prior 90 days) from the date of the alleged retaliation to file a whistleblower complaint under SOX. The Final Rule relaxes the requirements for filing a complaint, including allowing oral complaints, complaints made in foreign languages and filing of the complaint by any person on the complainant's behalf. In addition, the complainant must show only that his or her protected activity was a contributing factor to the adverse action in order to trigger an OSHA investigation.

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If the complaint establishes such a prima facie case, respondent bears the burden of showing, by clear and convincing evidence, that it would have taken the adverse action regardless of the protected activity. If the employer cannot make this showing, then OSHA's investigation will continue. The Final Rule reflects OSHA's rejection of commenters' criticisms made during the notice and comment period that these standards set a low bar for complainants and a high bar for defending employers, increasing the likelihood of an investigation.

Under the Final Rule, within 60 days of the filing of the complaint, OSHA's Assistant Secretary will issue a written finding of whether there is reasonable cause to believe the complaint has merit. If there is reasonable cause, OSHA will issue a preliminary order providing all relief necessary to make the complainant whole, including reinstatement, back pay with interest, compensation for any special damages, litigation costs and attorney fees. Instead of actual reinstatement, OSHA may order "economic reinstatement" during the pendency of the dispute, which allows a complainant to collect pay and benefits even without formal reinstatement.

The Final Rule does not address commenters' concern raised during the notice and comment period that the rule does not provide circumstances under which preliminary reinstatement would be inappropriate, such as when the employee is a security risk. Additionally, in cases where the employer ultimately prevails, the employer cannot recover wages paid to the complainant during the reinstatement period, even if the reinstatement was purely economic.

Following the issuance of the preliminary order, the parties have 30 days to file objections and request a hearing before an administrative law judge (ALJ). Under the Final Rule, the filing of objections will stay any remedy in the preliminary order, except for reinstatement. Upon the issuance of the ALJ's decision, the parties then have 14 days to petition OSHA's Administrative Review Board (ARB) to review the ALJ's decision. The final order of the ARB must be issued within 120 days of the hearing and may be appealed within 60 days to the U.S. Court of Appeals. If the final order of the ARB is not issued within 180 days of the initial filing of the complaint, and there is no showing of bad faith delay, the complainant may bring an action in the federal district court and either party may request a jury trial.

Internal Reporting

While Dodd-Frank defines "whistleblower" to mean "any individual who provides…information…to the Commission," 15 USC §78u-6(a)(6), the U.S. Courts of Appeals are split over whether a whistleblower has standing to bring a claim under Dodd-Frank if the whistleblower has complained only internally, and has not complained to the SEC.

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On July 17, 2013, the U.S. Court of Appeals for the Fifth Circuit in *Asadi v. G.E. Energy (USA)*, 720 F3d 620 (5th Cir. 2013), held Dodd-Frank requires that a whistleblower report an alleged violation to the SEC to be covered by Dodd-Frank. Subsequently, on Aug. 4, 2015, the SEC issued an interpretive rule stating that under Dodd-Frank an individual's status as a whistleblower is determined by SEC Rule 21F-2(b)(1), which provides that to be covered a whistleblower need not have complained to the SEC.

On Sept. 10, 2015, the U.S. Court of Appeals for the Second Circuit, rejecting *Asadi* and giving deference to the SEC's interpretive guidance, held in *Berman v. Neo@Ogilvy*, 801 F3d 145 (2d Cir. 2015), that employees who complain internally only, rather than complaining to the SEC, are whistleblowers under Dodd-Frank. Thus, the Second Circuit held a finance director who reported suspected irregularities internally—including delayed payments to clients and improperly recognized revenues—but was terminated before he raised these concerns with the SEC, was found to be a whistleblower under Dodd-Frank entitled to its anti-retaliation protections.

Following the Second Circuit's decision in *Berman*, however, the district court in *Verble v. Morgan Stanley Smith Barney*, No 3:15-CV-74-TAV-CCS (ED Tenn. Dec. 8, 2015), joined the Fifth Circuit and held Dodd-Frank whistleblowers are required to report suspected violations to the SEC in order to have standing to bring a Dodd-Frank retaliation claim.

On Nov. 10, 2015, the defendants in the Berman matter advised the Second Circuit they will not be pursuing a petition for writ of certiorari with the U.S. Supreme Court and, thus, a circuit split remains. Whether internal reports qualify for Dodd-Frank protection is important because, among other things, Dodd-Frank provides greater recoveries (including two times back pay) and longer time frames (six years) for bringing a retaliation claim than those available under SOX.

Director Liability

In a matter of first impression, the district court in *Wadler v. Bio-Rad Laboratories*, No 15-cv-02356-JCS (ND Cal Oct. 23, 2015), held directors who engage in retaliatory actions against a whistleblower are subject to individual liability under both SOX and Dodd-Frank. In *Wadler*, Bio-Rad's former general counsel sued his employer and individual members of its board of directors, alleging he had been terminated in retaliation for investigating and reporting to senior management possible violations of the Foreign Corrupt Practices Act. The plaintiff contended the decision to terminate him had been made by the full board and certain board members had known he had reported the alleged misconduct to his supervisors. The defendants sought to dismiss, arguing neither SOX nor Dodd-Frank permits directors to be held personally liable for retaliation.

With respect to SOX, the Northern District of California rejected the defendants' argument that Congress had intended to exclude directors from individual liability. Rather, the court held the issue of personal liability turned on whether the prohibition of retaliation by an "agent" of a public company included directors. Ultimately, however, the court concluded the SOX claims against the individual defendants other than the CEO were untimely.

With respect to Dodd-Frank, which simply precludes retaliation by an "employer," the court found the term "employer" was ambiguous and saw nothing in Dodd-Frank's legislative history that suggested Congress intended to eliminate individual liability. The court stated Dodd-Frank clearly was designed to increase whistleblower protection and therefore opined that a step as significant as removing individual liability would have been noted in the statute's legislative history. Accordingly, the court ruled the directors may be held individually liable under Dodd-Frank for retaliating against whistleblowers.

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Notably, the court also joined the Second Circuit's decision in *Berman*, and deferred to the SEC's position that Dodd-Frank whistleblower protection extends to individuals who report suspected violations internally, as well as those who report to the SEC.

Pleading Standard

On Dec. 15, 2015 the District of Connecticut in *Wiggins v. ING U.S.*, No 3:14-cv-01089 (D Conn. Dec. 15, 2015), refused to dismiss a SOX whistleblower claim, ruling: (1) the heightened Rule 9(b) pleading standard for fraud claims does not apply to SOX whistleblower retaliation claims; and (2) to plead a "reasonable belief" of a securities law violation, a SOX whistleblower plaintiff needs to show his or her claim approximately satisfied the elements of a claim under the securities laws that allegedly were violated (i.e., that the whistleblower claim is sufficiently "tethered" to a claim for a securities law violation).

In *Wiggins*, the plaintiff alleged her employer terminated her after she raised concerns about irregularities in the processing of terminated retirement plans, which she purportedly believed violated federal securities laws, including alleged "frequent inaccuracies in market value assessments on retirement plans…and deliberately failing to provide identified 'problem' files for quarterly auditing procedures." The plaintiff subsequently filed suit under SOX and Dodd-Frank, claiming she was retaliated against for her internal complaints.

The company moved to dismiss, arguing the plaintiff was required to meet the heightened pleading requirement under Rule 9(b) of the Federal Rules of Civil Procedure with respect to her allegations of fraud on which her whistleblower claim was based. The court rejected the argument, reasoning that because SOX protects employees who only "reasonably believe" fraud is occurring, Rule 9(b) does not apply.

The court also rejected the company's argument that the plaintiff failed to allege her belief of wrongdoing was objectively reasonable. Based on the ARB's decision in *Sylvester v. Parexel International*, ARB No. 07-123 (Dept. of Labor ARB May 25, 2011), and the Second Circuit's decision in *Nielsen v. AECOM Technology Corp.*, 762 F3d 214 (2d Cir. 2014), the court concluded a SOX whistleblower must allege she believed her employer's actions at least approximately satisfied the elements of a claim under the securities laws allegedly violated. Ultimately, the court concluded that although the plaintiff's Amended Complaint could have been drafted with more specificity, it "sufficiently tethers" the behavior the plaintiff believed was illegal to the federal statutes or SEC rules she believed her employer's conduct violated.

Confidentiality Agreements

On April 1, 2015, the SEC announced its first enforcement action against a company for using allegedly improper restrictive language in confidentiality agreements. The SEC charged a global technology and engineering firm with violating Dodd-Frank's whistleblower protections by requiring witnesses in certain internal investigations to sign confidentiality statements which included warnings that they could face discipline or even termination if they discussed the matters with outside parties (absent the prior approval of the company's legal department).

Since these internal investigations included allegations of possible securities violations, the SEC found the terms of the company's confidentiality statements violated SEC Rule 21F-17, which prohibits companies from taking any action to impede whistleblowers from reporting possible securities violations to the SEC. To settle the charges, the company agreed to pay a $130,000 penalty and amend its confidentiality statement to clarify that its employees are free to report possible securities violations to the SEC and other federal agencies.

The OWB's Annual Report on the Dodd-Frank Whistleblower Program, issued in November 2015, notes that the SEC will continue to focus on agreements that have language that reasonably could have the effect of impeding whistleblowers from reporting securities violations to the SEC.

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