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Business Litigation Update

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Dodd-Frank Whistleblower Protections Apply Only to Employees Who Report Alleged Securities Violations to the SEC

Key Notes:

- Current and former employees who do not report alleged violations to the SEC can no longer sue for retaliation under Dodd-Frank.
- While companies should face fewer retaliation suits, employees may have a greater incentive to report alleged violations to the SEC. Companies should ensure that their internal compliance policies are up to date and effective.
- Internal whistleblowers may still have the lesser protections of Sarbanes-Oxley against retaliation for reporting violations.

On February 21 the U.S. Supreme Court resolved a circuit split by unanimously holding that the anti-retaliation provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act, popularly known as Dodd-Frank, do not apply to alleged whistleblowers who report only internally and not to the SEC. *See Digital Realty Trust v. Sommers,* 583 U.S. ___ (2018). This ruling was widely expected, even though the SEC and numerous lower courts have treated the protection as applying to internal whistleblowers, and it has important consequences for employers subject to federal securities laws.

Enacted in 2010, Dodd-Frank gives employees who report securities violations protections against retaliation more expansive than those afforded by the Sarbanes-Oxley Act of 2002. Under Sarbanes-Oxley, whistleblowers must file a claim within 180 days with the Secretary of Labor and are limited to recovery of back pay, interest, and attorney fees and costs. A whistleblower under Sarbanes-Oxley includes an employee who reports a violation to company management. Under Dodd-Frank, however, employees can sue for retaliation in federal court within six years and may recover *double* back pay, interest, and attorney fees and costs. They may also receive rewards or bounties based on any recoveries their reporting helps the government obtain.

At issue in *Digital Realty* was the Dodd-Frank statutory definition of a whistleblower as an employee 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." Despite this seemingly clear language, the SEC and some lower courts had read Dodd-Frank, like Sarbanes-Oxley, to cover employees who only report alleged violations internally to company management.

The plaintiff in *Digital Realty* had reported to executive management what he alleged was a violation of Sarbanes-Oxley by his supervisor, a senior vice president. He was fired and subsequently sued for retaliation. The Ninth Circuit held that he was protected by Dodd-Frank even though he had not reported the alleged violation to the SEC. Reversing, the Supreme Court found that the Dodd-Frank definition is clear and therefore must be followed unless doing so produces an "absurd result," which was not the case here and in fact was argued by neither the plaintiff nor the SEC, which filed a brief and argued in the plaintiff's favor. Finding the statute clear, Justice Ginsburg wrote for the court, "Dodd-Frank's anti-retaliation provision does not extend to an individual … who has not reported a violation of the securities laws to the SEC."

Companies should be aware that the Supreme Court's ruling may create a stronger incentive for employees to report alleged violations to the SEC rather than internally, and should adjust their internal compliance procedures accordingly, as necessary. Some advocates for the Ninth Circuit's broader construction of a Dodd-Frank whistleblower in fact argue that the broader application benefited companies by encouraging employees first to report internally rather than to the SEC, allowing companies to address issues internally as well.

On the other side of the ledger, however, many believe that extending Dodd-Frank anti-retaliation protection to internal whistleblowers allows disgruntled and terminated employees to file spurious retaliation suits. Most Dodd-Frank plaintiffs in fact never report alleged violations to the SEC. Business groups generally support the narrower, plain statutory reading of Dodd-Frank for this reason, and companies should benefit by facing fewer retaliation suits following the Supreme Court's adoption of that reading.

Companies should also be aware that employees who only internally report violations may still be covered by the more limited but still important protections of Sarbanes-Oxley, which allow employees to pursue administrative remedies and recover back pay, interest, and attorney fees and other litigation costs.

FOR MORE INFORMATION

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