Ninth Circuit Holds That Dodd-Frank Whistleblower Provisions Apply to Employees Who Internally Raise Concerns

On March 8, 2017, the United States Court of Appeals for the Ninth Circuit ruled, in a 2-1 decision, to affirm a district court's denial of defendant-employer's motion to dismiss a whistleblower claim brought under the Dodd-Frank Act's ("Dodd-Frank") anti-retaliation provision. Wading into an issue that has already created a circuit split, the Ninth Circuit panel held that the term "whistleblower" extends protection to employees making internal disclosures of alleged unlawful activity, and does not limit protection under Dodd-Frank to employees reporting potential violations to the Securities and Exchange Commission ("SEC").[1] The Ninth Circuit, adopting the broader approach of the Second Circuit rather than the Fifth Circuit's narrower interpretation,[2] reasoned the congressional intent underlying the relevant Dodd-Frank provisions dictated there should be legal protection "for those who make internal disclosures as well as to those who make disclosures to the SEC."[3]

I. Background

Paul Somers, the Plaintiff-Appellee, was employed by Defendant-Appellant, Digital Realty Trust, Inc. ("Digital Realty") from 2010 to 2014. During that time, Somers made numerous reports to senior management alleging federal securities laws violations by Digital Realty. Shortly after he raised these concerns internally, and before he was able to make any report to the SEC, Digital Realty terminated Somers' employment. Following his firing, Somers sued Digital Realty, alleging violations of various state and federal laws, including Section 21F of the Securities Exchange Act of 1934 ("Exchange Act"), which contains anti-retaliation provisions added by Dodd-Frank.

At the district court level, Digital Realty sought to dismiss the retaliation claim on the ground that Somers was not a "whistleblower" entitled to Dodd-Frank's protections because he merely reported possible violations internally and not to the SEC. The district court denied Digital Realty's motion to dismiss after conducting an analysis of the statutory text, Dodd-Frank's legislative history, and the practical implications of reconciling the narrow definition of "whistleblower" with the expansive protections created by the anti-retaliation provision.[4] Somers argued that the court should defer to the SEC's interpretation of the provision conferring anti-retaliation protection under Dodd-Frank to a broader subset of individuals than merely those who report through official channels to the SEC.[5] The district court, while acknowledging the difficulty in finding a "clear and simple way to read the statutory provisions of Section 21F in perfect harmony with one another," sided with Somers, finding that individuals who report internally are protected from retaliation under Dodd Frank.[6]

II. Ninth Circuit's Reasoning

The Ninth Circuit panel began its discussion by chronicling the contours of a robust twenty-first century financial regulatory framework it described as created specifically to curb securities abuses. To frame the case against this regulatory backdrop, the court focused on provisions of the Sarbanes-Oxley Act ("SOX") including

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[1] *Somers* v. *Dig. Realty Tr. Inc.*, No. 15-17352, 4-5 (9th Cir. Mar. 8, 2017) ("Somers").

[2] *See Berman* v. *Neo@Ogilvy LLC*, 801 F.3d 145, 151 (2d Cir. 2015) ("*Berman*"); *Asadi* v. *G.E. Energy (USA), L.L.C.*, 720 F.3d 620 (5th Cir. 2013) ("*Asadi*").

[3] *Id*.

[4] *Somers* v. *Dig. Realty Tr. Inc.*, 119 F. Supp. 3d 1088, 1100-05 (N.D. Cal. 2015).

[5] *Id.* at 1104.

[6] *Id.* at 1104-06.

internal reporting requirements for lawyers, requirements for anonymous reporting avenues within corporate compliance regimes, and most importantly, whistleblower protections for employees. The court acknowledged SOX's express protections of those who lawfully provide information to federal agencies, Congress, or "a person with supervisory authority over the employee."[7] With respect to Dodd-Frank, the court reasoned that, like SOX, the legislation was passed in the wake of a financial scandal with the primary aims of improving accountability and transparency in the financial system, and protecting consumers from abusive financial practices.[8]

As the court observed, Dodd-Frank created incentives and protections for whistleblowers by adding Section 21F to the Exchange Act. Unlike SOX, however, 21F defines a whistleblower as "any individual who provides . . . information relating to a violation of the securities laws to the Commission, in a manner established, by rule or regulation, by the Commission."[9] On its face, this definition describes a whistleblower only as a person who reports information directly to the SEC. The issue in *Somers* arises out of a later subsection of Section 21F – specifically subdivision (iii) – wherein whistleblower protection extends to individuals who make any "required or protected" disclosure under SOX and all other relevant laws. Subdivision (iii) was added after the bill went through Committee, so there is no legislative history on it.

Although legislative history is not helpful, the Ninth Circuit found that the language of subdivision (iii) "illuminates congressional intent."[10] The Ninth Circuit found that, by incorporating SOX's disclosure requirements and protections through subdivision (iii), Congress meant for Dodd-Frank to bar retaliation against an employee of a public company who "provide[s] information . . . to a person with supervisory authority over the employee."[11] Citing a similar analysis from the Second Circuit, the Ninth Circuit drew attention to the "absurdities" potentially created by a different interpretation, explaining that, "if subdivision (iii) requires reporting to the [SEC], its express cross-reference to the provisions of Sarbanes-Oxley would afford an auditor almost no Dodd-Frank protection for retaliation because the auditor must await a company response to internal reporting before reporting to the Commission, and any retaliation would almost always precede Commission reporting."[12] Even though Dodd-Frank's definition of "whistleblowers" is limited to those persons who report to the SEC, the Ninth Circuit posited that terms can have different operative consequences in different contexts, and therefore was comfortable accepting that the term "may mean a different thing in a different part, depending on context." The court stated that reading the use of the word "whistleblower" to incorporate the earlier, narrower definition of the Exchange Act would "make little practical sense" and "undercut congressional intent." Citing again to the Second Circuit's similar reasoning in *Berman*, the Ninth Circuit concluded that a strict application of Dodd-Frank's definition "would, in effect, all but read subdivision (iii) out of the statute."[13] Furthermore, the court accorded deference to the SEC rules issued in 2011 that contain the more expansive definition of "whistleblower" and found that those rules reflected Congressional intent to provide broad whistleblower protection. With those bases, the court held that any employee who takes any action described in subdivisions (i), (ii), or (iii) of the anti-retaliation provision – including, by reference to SOX, reporting "to a person with supervisory authority over the employee"– is entitled to protection as a whistleblower. The Ninth Circuit

[7] 18 U.S.C. § 1514A(a).

[8] Pub. L. No. 111-203, 124 Stat. 1376, 1376 (2010).

[9] 15 U.S.C. § 78u-6(a)(6).

[10] *Somers* at 8.

[11] *Id.*

[12] *Id* at 9 *citing* Berman, 801 F.3d at 151.

[13] *Somers* at 10.

concluded that the interpretation accurately reflects congressional intent that Dodd-Frank protect employees "whether they blow the whistle internally" or report directly to the SEC.[14]

III. Potential Implications

Digital Realty may seek an *en banc* rehearing from the Ninth Circuit or, alternatively, seek review in the Supreme Court. Further, other circuits may interpret Dodd-Frank more narrowly, as the Fifth Circuit has, [15] rather than agree with the Second Circuit's and Ninth Circuit's broader interpretation.[16] Regardless, the circuit split has already led the Supreme Court to accept certiorari in a case from the Sixth Circuit with similar facts.[17]

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email Bradley J. Bondi at 202.862.8910 or bbondi@cahill.com; Charles A. Gilman at 212.701.3403 or cgilman@cahill.com; Kimberly Petillo-Décossard at 212.701.3265 or kpetillo-decossard@cahill.com; John Schuster at 212.701.3323 or jschuster@cahill.com; Scott Singer at 212.701.3757 or ssinger@cahill.com.

[14] *Id* at 12.

[15] In *Asadi*, the Fifth Circuit held that Dodd-Frank's anti-retaliation provision requires a whistleblower to make a report to the SEC in order to be covered—merely filing an internal complaint (as Somers did) is insufficient. *Asadi* v. *G.E. Energy (USA), L.L.C.*, 720 F.3d 620 (5th Cir. 2013).

[16] In *Somers*, Circuit Judge Owens dissented from the majority's judgment, stating that he agreed with the Fifth Circuit's narrower interpretation of Dodd-Frank in *Asadi*.

[17] In *Verble* v. *Morgan Stanley Smith Barney LLC et al.*, No. 15-6397 (6th Cir. 2017), the Sixth Circuit affirmed the dismissal of a similar whistle-blower claim, though it did not decide the issue at question in *Somers*, instead holding that the plaintiff's claim was too vague for adjudication.