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Trending: Broad Whistleblower Protection

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AUTHORED ARTICLE | 6.21.2013

Law360

Mary Henkel, of counsel in the Vorys Cincinnati office, authored a column entitled “Trending: Broad Whistleblower Protection”, which appeared in the June 21, 2013 edition of *Employment Law360*. The full text of the column is included below.

Trending: Broad Whistleblower Protection

How should financial services companies and publicly traded companies treat employees who claim that the company violated federal law or regulations? Very carefully.

With the decision in *Murray v. UBS* on May 21, 2013, whistleblowers are winning 5 to 0 on broadly defining securities whistleblowers protected by the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act. Under the cases and U.S. Securities and Exchange Commission rules, companies may face liability — or expensive litigation — if an employee could link adverse treatment to a report of a violation. This can happen although the employee did not actually report to the authorities in some cases and even if the employee is wrong.

Compliance officers and risk and human resources managers should seek legal advice early on and closely monitor handling of the would-be whistleblower. Indeed, precautions need to be taken well before there is a potential whistleblower to ensure that the issue is spotted before adverse employment actions are taken without sufficient attention to the potential liability.

In 2010, Dodd-Frank added new whistleblower incentives and protections to those already in place under the 2002 Sarbanes-Oxley legislation. Although SOX and the consumer finance-related portions of Dodd-Frank generally call for administrative proceedings through the U.S. Department of Labor before court action, there are notable exceptions.

Dodd-Frank gives whistleblowers the right to file suit directly in federal court for alleged retaliation, if a disclosure is required or protected by SOX, by laws and rules within SEC jurisdiction or by the law protecting the reporting of a federal crime to a federal officer. Employee agreements to arbitrate disputes with their employers are not enforceable as to these issues. The law provides the remedies of reinstatement, double backpay and attorneys' fees for whistleblowers in these categories who are discharged or otherwise suffer retaliation.

Dodd-Frank Securities Whistleblowers

In general, Dodd-Frank defines a securities whistleblower as one who provides, or collaborates with others to provide, information about a securities violation to the SEC. But an employee who reports an alleged violation to anyone, or to other authorities, may be protected too.

Five district court decisions have held that the anti-retaliation provisions of the act create an exception that expands its protection to people who have not gone to the SEC with the report of violation in some circumstances. An SEC rule also interprets the law to protect whistleblowers who report to persons other than the SEC.

The Law Does Not Require a Report to the SEC

The recent *Murray v. UBS* decision from the U.S. District Court for the Southern District of New York allowed a stock analyst to proceed on a retaliation claim. The analyst alleged that UBS fired him for reporting to his supervisors on alleged attempts to slant his analysis.

It was the fifth ruling on vigorous efforts to dismiss a claim by a whistleblower who did not alert the SEC by arguing for a strict reading of the statutory definition of a whistleblower. *Murray* also endorsed the SEC's own reading of the statute in its regulations.

Murray sums up decisions, from the early case in the same district that generated two opinions, *Egan I* and *Egan II*, to subsequent decisions in other jurisdictions that agreed. *Egan I* explains when whistleblower protections can apply because employees raise supposed violations, even without a report to the SEC. They can apply to a report pursuant to an existing duty to disclose under SEC law or rule, to a report of a federal crime to a federal law enforcement officer or to a report that another SEC law or rule specifically protects.

In other words, if a disclosure, made to anyone, is "required or protected" by a law or regulation within the SEC's jurisdiction or discloses a federal crime to a federal officer, whistleblower protections apply.

In other cases — such as reports of violation of civil law or regulations in general — securities whistleblowers can proceed on a retaliation claim only if they plead a report made to the SEC. In *Egan II*, the court ultimately dismissed *Egan's* case, even though the fired employee alleged that violations of securities regulations and other laws occurred.

The court found that he failed to plead violations within the narrower category of SEC laws or rules requiring or specifically protecting disclosure, failed to plead that others acting jointly with him actually made a report to the SEC and admitted that he had not done so himself.

Trial courts in Tennessee, Connecticut and Colorado, as well as Murray, have generally adopted the interpretation in Egan I. Securities whistleblower complaints are likely to survive a motion to dismiss, without any report to the SEC.

The Decisions Trend toward Broader Coverage

The Nollner case in Tennessee, like Egan, ultimately dismissed the plaintiff's retaliation case, while agreeing that some categories of disclosures invoke securities whistleblower protections, even without any report to the SEC.

Nollner relied heavily on Egan I but ruled a little differently. It criticized Egan's statement that the law "does not protect" those who report violations of SEC laws or regulations that do not impose a duty to disclose, saying that the law "also protects whistleblowers who make 'protected' disclosures, not just 'required' disclosures." Nollner also appears to overlook the reference to reports of a federal crime to a federal officer, noting only that reports must relate to matters within the SEC's jurisdiction.

The test for a sustainable suit continued to evolve. Nollner said:

Harmonizing all of these provisions, as the court must, a plaintiff seeking protection under § 78u-6(h)(1)(A) (iii) must at least show the following:

He or she was retaliated against for reporting a violation of the securities laws

- The plaintiff reported that information to the SEC or to another entity (perhaps even internally) as appropriate
- The disclosure was made pursuant to a law, rule, or regulation subject to the SEC's jurisdiction
- The disclosure was "required or protected" by that law, rule, or regulation within the SEC's jurisdiction

Note the word "perhaps" above.

By the time that the Colorado district court examined the boundaries of securities whistleblower protection in Genberg v. Porter, looking to Egan I, Nollner and Kramer v. Trans-Lux Corp, it restated Nollner's test this way:

In order to prevail on a [Dodd-Frank Act] retaliation claim, a plaintiff must show:

- He reported an alleged violation to the SEC or another entity, or internally to management
- He was retaliated against for reporting the alleged violation
- The disclosure of the alleged violation was made pursuant to a rule, law, or regulation subject to the SEC's jurisdiction
- The disclosure was required or protected by that rule, law, or regulation within the SEC's jurisdiction.

The word "perhaps" has disappeared. Genberg's claim could proceed simply because he told company management about alleged securities violations.

The Law Does Not Require a Report to the SEC in a Specific Form

In Kramer, like Genberg, the court allowed the employee's claim to proceed. The terminated employee in Kramer first complained to the company's CFO and the audit committee of the board, then sent a letter to the SEC. He did not file a report on the form prescribed by the SEC.

The defense argued that this put him outside the statutory definition of a whistleblower as one who provides information about a violation "in a manner established, by rule or regulation, by the [SEC]." 15 U.S.C. § 78u-6(a)(6). The Kramer court looked to Egan I and Nollner in holding that the retaliation provisions broaden the whistleblower definition. Examining SEC rules issued after those cases as well, it concluded that Kramer's letter was enough to invoke the retaliation provisions.

The Law Protects Reports Based on a Reasonable Belief about a Violation

Kramer also upheld the SEC rule found at 17 C.F.R. § 240.21F-2(b)(1), which says you are a whistleblower if you "possess a reasonable belief that the information you are providing relates to a possible securities law violation."

This aspect of the SEC rule and the Kramer decision are reflected in the Genberg court's statement of the elements of a claim. While the earlier Nollner formulation referred to "reporting a violation," after issuance of the SEC rule and the decision in Kramer, the most recent decision refers twice to an "alleged violation." Another New York decision held that a "plausible" good-faith, subjective belief suffices to state a claim.

Under the federal district court rulings thus far, an employee can state a claim for retaliation under the Dodd-Frank securities whistleblower law without identifying an actual violation, without using a specific SEC form and indeed, without reporting to the SEC at all in some cases.

Consumer Financial Protection Whistleblowers

The Consumer Finance Protection Act (CFPA) portion of Dodd-Frank has not generated notable court decisions to date, but issues raised about consumer finance practices also should be treated with caution. The threshold requirement that the whistleblower need only have a reasonable belief is built into the statute itself. One can submit a complaint to the Department of Labor's Occupational Health and Safety Administration by email or call a toll-free line.

The CFPA whistleblower law offers reinstatement, backpay, compensatory damages and attorneys' fees and expenses for employees who are discharged or otherwise suffer retaliation for whistleblowing.

List of Protected Whistleblower Reports

Employees are protected for reporting violations of a long list of laws governing consumer lending or of any other rule, order, standard or prohibition prescribed by the Consumer Financial Protection Bureau. They are also protected for aiding CFPB enforcement efforts or refusing to participate in violations. The listed laws are the following:

Under Title 12 of the U.S. Code, "Banks and Banking"

- Federal Deposit Insurance Act — as to disclosures from nonfederally insured depositories
- Real Estate Settlement Procedures Act of 1974
- Home Mortgage Disclosure Act of 1975
- Alternative Mortgage Transaction Parity Act of 1982
- Truth in Savings Act
- Home Owners Protection Act of 1998
- Omnibus Appropriations Act of 2009 Section 626 — pertaining to state enforcement of Truth in Lending Act
- Secure and Fair Enforcement for Mortgage Licensing Act of 2008

Under Title 15 of the U.S. Code, "Commerce and Trade"

- Truth in Lending Act
- Home Ownership and Equity Protection Act (HOEPA)
- Fair Credit Billing Act
- Consumer Leasing Act
- Fair Credit Reporting Act
- Equal Credit Opportunity Act
- Fair Debt Collection Practices Act
- Electronic Fund Transfer Act, except for Section 920
- Interstate Land Sales Full Disclosure Act
- Gramm-Leach-Bliley Act Sections 502 through 509, except for Section 505 [(15 U.S.C. 6802–6809, except for 15 U.S.C. 6805] as it applies to 15 U.S.C. 6801(b)]

CFPA Whistleblower Procedure

If reporting alleged unlawful activity under the CFPA is not covered by the securities whistleblower law (that is, is not required or protected by SEC laws or regulations, SOX or the federal crime-reporting statute), a complaint is first filed with the Department of Labor. If the Labor Department does not act on it in 210 days, however, the whistleblower can file suit in federal court.

Complaints can also be appealed to the appropriate U.S. Court of Appeals, after Labor Department investigation, administrative law judge and administrative review board rulings.

What to do when an employee accuses the company of violating federal law or regulations:

- Call in a rapid-response team, including knowledgeable counsel, as soon as the possibility of a whistleblower claim arises.

- The law in this area is emerging. Get an up-to-the-minute update.
- Investigate and document the investigation.
- Take corrective or remedial measures as warranted by any noncompliance you discover.

What to do before any allegations are made:

- Maintain strong reporting channels and attention to internal compliance.
- Ensure that policies and manager training are updated to prohibit retaliation for complaints (internal or external) of legal violations.
- Make sure that managers can identify possible whistleblower retaliation claims.
- Check and revise, as needed, policies, handbooks and employee agreements (including severance agreements). Eliminate any appearance of discouraging employees from reporting violations to the SEC, the CFPB or other federal law enforcement authorities.

A Note on Pending CFPB and SOX Whistleblower Issues

Development of the law under Dodd-Frank is still in its early stages — with challenges swirling around the reach of SOX § 806, 43 and the administration's recess appointments, including the appointment of Richard Cordray as director of the CFPB.

Cases defining the coverage of SOX will affect the reach of the enhanced protections in Dodd-Frank. *Lawson v. FMR*, pending in the United States Supreme Court, concerns whether disclosures of securities law violations by the employees of private companies that serve as contractors to public companies are protected by SOX.

The court's view on who are "covered employees" and other developing issues will define not only what SOX protects but also who can proceed under the Dodd-Frank securities whistleblower provisions.

Even if the challenge to Cordray's appointment succeeds, actions of the Labor Department on complaints under the CFPA may not be affected. Based on the statutory language alone, OSHA will accept CFPA whistleblower retaliation complaints.