What Three Pending Issues Could Blow Open the Doors of the Whistleblower Provisions of Sarbanes-Oxley / Dodd-Frank

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A Decade of Growth in Whistleblower Law

- Congress enacts new whistleblower-protection statutes – e.g., Consumer Finance (2010), Food Safety (2011), Motor Vehicle (2012)

- Dodd-Frank Act (2010)
  - New “bounty” programs at SEC and CFTC
  - New whistleblower protections for employees reporting to SEC and CFTC
  - Amendments to SOX (longer SOL; no predispute arbitrations; coverage of subsidiaries; jury trial guaranteed)

- SEC steps into employment relationship via enforcement actions
  - Penalizing employers for retaliation (2014 - 2016)
  - Prohibiting agreements that “impede” employees (2015 - 2017)
Expansion in SOX Whistleblower Protections


- 2014 – Supreme Court expands SOX to cover contractor employees in *Lawson v. FMR LLC*.

SOX 2018 Three Hot Issues

• Attorney-Client Privilege: Can SOX plaintiff use attorney/client privileged information to prove retaliation case?

• Internal Reporting: Does Dodd-Frank protect employee against retaliation for reporting internally, and not to the SEC, if disclosures are “required or protected” by SOX?

• Extraterritorial Application of SOX: Does SOX’s Section 806 protect employees working in other countries?
• *Jordan v. Spring Nextel* (ARB 2009) – SOX complainants allowed to use privileged information to prove retaliation.

• *Van Asdale v. IGT* (9th Cir. 2009) – Trial courts can use protective orders to minimize disclosure.

• SEC Part 205, 17 C.F.R. § 205.3(d)(2) - In-house attorneys allowed to “report out” to the SEC to prevent substantial harm to investors or fraud on SEC, and § 205.1 states that Part 205 preempts state ethics rules that conflict.
• In-house counsel sues Bio-Rad Labs under SOX 806, Dodd-Frank Act and California wrongful discharge law alleging retaliatory termination.

• Bio-Rad moves to dismiss on grounds that plaintiff cannot prove case without use of privileged information in violation of California rules of professional responsibility.

• Federal Court in (N.D. Cal. Dec. 2016) denies motion to dismiss:
  – ABA Model Rules of Professional Conduct 1.6 allows such disclosures where necessary to prove claim (adopted in most states).
  – Federal common law also allows such disclosures/FRE 502.
  – State ethics rules conflicting with Part 205 or SOX are preempted.

• On February 7, 2017, after three hours of deliberation, a federal court jury awards over $11M in damages, including compensatory and punitive damages ($5M) (the latter under California common law) to a G.C. Whistleblower. Appeal pending before U.S. Court of Appeals for the Ninth Circuit, but not on privilege issue.
Privilege – Implications of Bio-Rad

• SEC Part 205 preempts attorney/client privilege provisions
• State ethics laws “frustrate” the purpose of SOX (“reporting up”) and SEC Part 205 (“reporting out”)
• Dodd-Frank’s jury trial “carve out” significant
• The company waived the privilege by using client confidential and privileged information in prior proceedings (OSHA)
• Will Wadler rue his failure to report his concerns to the SEC?
• Bio Rad’s late filing of quasi-dispositive motions
• Keep the whistleblower under the corporate tent
• Attorneys fees alone can be huge ($3.5M)
• Lawyers are not great witnesses (Davis Polk partner)
• Dodd-Frank Section 922 protects “whistleblowers” against retaliation and defines “whistleblower” as someone who reports to SEC, in accordance with SEC’s whistleblower reward program.

• Section 922 separately defines “protected conduct” to include disclosures “required or protected” under SOX, which protects internal reporting of violations of fraud statutes and securities laws.

• So does Dodd-Frank protect internal reporting?

• Important issue because Dodd-Frank provides longer SOL (up to 6 years vs. SOX’s 180 days); direct access to federal court without OSHA exhaustion; and double back-pay damages (vs. SOX single damages).


• Oral argument on Somers held by SCOTUS on November 28, 2017, with a decision expected in June 2018.
  • Questions at oral argument imply the SCOTUS will require SEC reporting
  • Concern about rule making process behind Section 922
  • Little concern for “absurd result”
  • Literal interpretation of the statute

In *Villanueva v. Core Labs* (ARB 2011), the ARB found no such clear expression of intent in SOX 806, and held statute does not apply extraterritorially.
• In *Blanchard v. Exelis Sys. Corp.* (ARB 2017), the ARB held that SOX 806 applies extraterritorially where the public company’s misconduct overseas affects the U.S. “in some significant way.”

  – Supreme Court in *RGR Nabisco Inc v. European Community* (2016) had clarified standard to require “clear indications of extraterritoriality.”

  – Whistleblower in Blanchard, a security supervisor working for a contractor at Bagram AFB in Afghanistan, had reported other supervisors committing fraud in billing and covering up a security breach.

  – ARB found clear indications of extraterritoriality because SOX 806 incorporated certain statutes that applied extraterritorially – e.g., prohibitions on wire fraud and securities fraud and, thus, held that SOX 806 applied.
Extraterritorial Application – AB InBev

• Dodd-Frank anti-retaliation provisions do not protect non-U.S. employees working for non-U.S. companies overseas even if companies are listed on U.S. exchanges. *Liu Meng-Lin v. Siemens AG* (2d Cir. 2014).

• But SEC penalized a non-U.S. company with ADRs listed on a U.S. exchange for imposing restrictive confidentiality agreement on a non-U.S. whistleblowing employee working at a plant in India. *In re AB InBev* (SEC Order 2016).

  – Separation agreement impeded employee from communicating with SEC.

  – While not in a retaliation case, SEC order has significant impact on employment relationship between non-U.S. company and non-U.S. employee working outside U.S.
C.F.R. § 164.502. Under this exception, it is legal for an employee or business associate of an entity covered by HIPAA to disclose PHI if the individual believes that the covered entity has:

- Engaged in unlawful conduct;
- Engaged in conduct that violates professional or clinical standards; or
- Provided care, services, or conditions that potentially endanger patients, workers, or the public.

But this exception does not completely supersede the overarching rule of privacy. The disclosing individual must have a good-faith belief that one of the violations above has occurred, and the disclosure of PHI must be made to:

- A health oversight agency or public health authority legally authorized to investigate the alleged violations;
- A healthcare accreditation organization, for the purpose of reporting violations of professional or clinical obligations; or
- An attorney retained by the worker or business associate for the purpose of determining her legal options with respect to the observed misconduct.
• Employers must make calculated decisions to protect the attorney/client privilege
• “Internal reporting” only is in doubt
• SOX still a stateside remedy for now
• Don’t forget HIPPA retaliation provisions
Questions
Thank You!