

## [Securities Regulation Daily Wrap Up, TOP STORY—N.D. Cal.: Ambiguity in whistleblower provisions keeps anti-retaliation claim alive, \(May 18, 2015\)](#)

Securities Regulation Daily Wrap Up

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By Amanda Maine, J.D.

A federal court denied a company's motion to dismiss a former employee's anti-retaliation claim. The court held that under *Chevron*, the whistleblower protection provisions of the Dodd-Frank Act and a subsequent SEC rule were ambiguous. The court also found that the SEC rule was a reasonable interpretation of the Act's whistleblower protection provisions and was therefore entitled to deference (*Somers v. Digital Realty Trust, Inc.*, May 15, 2015, Chen, E.).

**Background.** Paul Somers worked as a vice president of portfolio management at Digital Realty Trust. According to his complaint, Somers made complaints to senior management about actions by his supervisor that eliminated internal controls over certain corporate actions in violation of the Sarbanes-Oxley Act (SOX). Shortly afterwards, Digital Realty fired Somers. Somers sued Digital Realty for, among other things, retaliatory termination in violation of the Dodd-Frank Act and SEC Rule 21F-2(b)(1). Digital Realty moved to dismiss because Somers did not report any of the alleged internal controls violations to the SEC and therefore did not qualify as a whistleblower under Dodd-Frank.

**Whistleblower protection under Dodd-Frank.** Under Dodd-Frank Act Section 21F(a)(6), for an individual to qualify as a whistleblower, he or she must provide information relating to a violation of the securities laws to the Commission. However, in June 2011, the SEC issued final rules interpreting Dodd-Frank's whistleblower provision. In particular, Rule 21F-2(b)(1) deemed a person to be a whistleblower if they made disclosures that are required or protected under SOX, which would include employee disclosures made internally to supervisory personnel without regard to whether the individual also reported the information to the SEC. Several courts have noted this disconnect between the statutory provision and the subsequent SEC rule.

***Chevron* deference: ambiguity.** Under the test established in *Chevron, U.S.A. v. Natural Res. Def. Council, Inc.* (U.S. 1984), to determine if an agency's interpretation of a statute is entitled to deference, a court must first evaluate if the applicable provisions are ambiguous. Digital Realty argued that Section 21F(a)(6)'s definition is plain and unambiguous. The court disagreed, stating that Section 21F's express requirement of reporting misconduct to the SEC does not take into consideration arguably conflicting statutory language and other indications of legislative intent.

The court then pointed to a number of factors that support a finding of ambiguity. Digital Realty's definition of "whistleblower" would essentially render Section 21F(h)(1)(a)(iii) ("subsection (iii)") superfluous because subsection (iii) clearly contemplates protection for individuals who do not make reports to the SEC. Digital Realty's interpretation would also render the words "to the Commission" in subsections (i) and (ii) superfluous because these words would be unnecessary if persons who provide information to the Commission are the only ones who can ever be deemed whistleblowers.

The court also advised that the legislative history of Dodd-Frank supports a finding of ambiguity because subsection (iii) did not appear in any version of the bill before it was passed and there was no discussion of the subsection in the legislative record. "[G]iven the belated addition of subsection (iii), it is at least reasonable to assume that Congress intended for the scope of the DFA whistleblower-provisions to be broader than in earlier versions of the bill, which versions unambiguously required an external report to the Commission in order to be protected from employer retaliation," according to the court.

The court also rejected the argument put forth by Digital Realty and the Fifth Circuit that SOX anti-retaliatory provisions are “moot” because an aggrieved individual would prefer to bring claims under Dodd-Frank, given that it provides for more damages, has a longer statute of limitations, and does not require administration exhaustion. Individuals might indeed have reasons to prefer to pursue relief under SOX, the court observed, including OSHA investigation at the administrative level and additional damages for noneconomic harms.

Finally, the court observed that policy reasons support a finding of ambiguity. Digital Realty’s and the Fifth Circuit’s solution to the conflict would be reading subsection (iii) narrowly to require a report to the SEC, which would be contrary to Dodd-Frank’s purpose of encouraging the reporting of securities violations and would be ineffective as a preventative measure because employers would be unaware when such a report was made, according to the court.

**Chevron deference: reasonableness.** The court also found that Rule 21F-2(b)(1) was a reasonable interpretation of the Dodd-Frank Act under *Chevron*. The interpretation eliminated the tension between the narrow statutory definition and the broader coverage of subsection (iii). It also comported with Dodd-Frank’s framework to incentivize broader reporting of illegal conduct and the SEC’s policy that encourages internal reporting of possible violations. In addition, it enhances the SEC’s ability to bring enforcement actions against employers that retaliate for reporting. Taken together, the court determined that the SEC’s interpretation was reasonable and thus entitled to deference.

**Other matters.** The court also rejected Digital Realty’s argument that Somers did not adequately allege that his internal reports were protected under Sarbanes-Oxley. Digital Realty had not made this argument on its initial motion to dismiss, and as such, this argument was waived. Finally, the court denied Somers’s motion to disqualify Digital Realty’s counsel, Seyfarth Shaw, due to having potentially adverse interests. Somers was unable to demonstrate a “substantial relationship” under California law between the brief time he used Seyfarth Shaw in an unrelated matter and Seyfarth Shaw’s current representation of Digital Realty.

The case is [No. C-14-5180](#).

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Companies: Digital Realty Trust Inc.

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