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Why Congress Should Pass Whistleblower Protection Law

By **Jason Zuckerman and Matthew Stock** (October 8, 2021, 4:49 PM EDT)

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In an act of remarkable prescience, Rep. Al Green, D-Texas, who chairs the U.S. House of Representatives' Financial Services Committee Subcommittee on Oversight and Investigations, introduced the Whistleblower Protection Reform Act of 2021, or H.R. 5485,[1] on the same day that Facebook Inc. whistleblower Frances Haugen testified at a U.S. Senate hearing, while the trial of Elizabeth Holmes continued to reveal how Theranos Inc. leadership tried to silence and intimidate whistleblowers.[2]

Courageous whistleblowers such as Erika Cheung and Tyler Shultz — the whistleblowers who spoke up about wrongdoing that they claim to have detected at Theranos — and Haugen come forward at tremendous risk to their careers and reputations and protect the public from fraud, threats to public health and safety, and other wrongdoing.

Some whistleblowers even jeopardize their own safety. Truth-tellers deserve genuine whistleblower protection, which entails, at a minimum, protection for internal disclosures, a burden of proof that gives corporate whistleblowers a chance to prevail, an unqualified right to try a retaliation claim before a jury, and the opportunity to recover compensatory damages.

The whistleblower protection provision of the Dodd-Frank Act is extraordinarily weak and lacks these basic tenets of modern whistleblower protection laws. Indeed, due to a drafting error, it does not even protect internal disclosures.[3]

Haugen's whistleblowing has spurred bipartisan indignation about Facebook's business practices and may cause Congress to regulate social media companies. If Congress is serious about protecting Haugen and other truth-tellers, it should promptly enact the WPRA.

Strengthening the Whistleblower Protection Provision of the Dodd-Frank Act

The WPRA would clarify that internal disclosures are protected under the whistleblower protection provision of the Dodd-Frank Act. In the wake of the U.S. Supreme Court's 2018 decision in Digital Realty v. Somers, Dodd-Frank Act whistleblower protection[4] is limited to whistleblowers who have reported a potential violation of the federal securities laws to the U.S. Securities and Exchange Commission. Internal whistleblowing is not protected, unless the whistleblower has also disclosed the violation to the SEC prior to suffering retaliation.

Post-Digital Realty, companies regulated by the SEC have been concerned that whistleblowers will report fraud directly to the SEC rather than reporting internally, thereby impeding the ability of corporate compliance programs to detect and remedy fraud.

As the WPRA would encourage internal whistleblowing, the business community should support

the WPRA. Indeed, as Sen. Chuck Grassley, R-Iowa, pointed out in an amicus curiae brief filed in Digital Realty, "the business community ... successfully lobbied the SEC to adopt rules favoring internal reporting."[5] Absent credible whistleblower protection, companies should not expect whistleblowers to report wrongdoing internally.

Note that a bill introduced by Green in the 116th Congress — the Whistleblower Protection Reform Act of 2019, H.R. 2515 — strengthening the Dodd-Frank Act's whistleblower protection provision, passed by an overwhelming bipartisan majority of 410-12 in July 2019.[6]

Clarifying the Burden of Proof

Subsequent to the enactment of the Dodd-Frank Act, the Supreme Court's decision in University of Texas Southwest Medical Center v. Nassar[7] elevated the burden of proof in Dodd-Frank Act whistleblower retaliation cases to "but-for" causation. In contrast to the Dodd-Frank Act, most of the federal whistleblower protection laws enacted since 1989 employ a "contributing factor" causation standard.

The WPRA would employ "contributing factor" causation in Dodd-Frank Act retaliation cases, i.e., a whistleblower would prevail "upon a showing that protected conduct was a contributing factor in the unfavorable personnel action alleged in the complaint."

Prohibiting Post-Employment Retaliation

The WPRA would clarify that the Dodd-Frank Act prohibits post-employment retaliation against a whistleblower.[8] As many SEC whistleblowers cooperate with SEC investigations and enforcement actions years after they are no longer employed by the company whose misconduct they reported, it is critical to provide robust protection against retaliation post-employment.

Failing to prohibit post-employment retaliation could give an SEC whistleblower's former employer free rein to retaliate against and intimidate the whistleblower to try to dissuade them from further cooperating with an SEC investigation or testifying at a trial in a prosecution stemming from their disclosure.

Authorizing Compensatory Damages

Unlike nearly all whistleblower protection laws, the Dodd-Frank Act does not authorize compensatory damages, i.e., damages for emotional distress and reputational harm.[9] If a whistleblower experiences harassment or a hostile work environment due to their whistleblowing but does not suffer economic damages, the whistleblower would not recover monetary damages in a Dodd-Frank Act retaliation action.

The WPRA fixes this significant deficiency by authorizing prevailing whistleblowers to recover compensatory damages, in addition to economic damages and attorney fees.

Clarifying That Oral Disclosures Are Protected

In what appears to have been a solution in search of a problem, the SEC amended Exchange Act Rule 21F-2(a) in September 2020 to limit protected whistleblowing under the Dodd-Frank Act anti-retaliation provision to written disclosures. Oral whistleblowing, such as statements made to SEC staff during an interview, are not protected.

This interpretation is contrary to the plain meaning of the Dodd-Frank Act. Indeed, the second form of protected conduct set forth in the whistleblower protection provision of the Dodd-Frank Act — "initiating, testifying in, or assisting in any investigation or judicial or administrative action of the Commission" — contemplates protection for oral disclosures.

The writing requirement is also a significant departure from a well-developed body of precedent

construing similar whistleblower protection laws, including the Supreme Court's 2011 decision in Kasten v. Saint-Gobain Performance Plastics Corp.[10] holding that oral disclosures are protected under the anti-retaliation provision of the Fair Labor Standards Act.

Moreover, excluding oral disclosures from the ambit of Dodd-Frank Act whistleblower protection is inconsistent with the remedial purpose of the statute and the SEC's interest in encouraging whistleblowers to come forward.

If a whistleblower cooperates with an SEC investigation by providing important information during an interview with SEC staff without also documenting that information in a written submission, the SEC would apparently look the other way if the whistleblower suffers retaliation due to their cooperation with an SEC investigation.

Although the SEC's interpretation is limited to its enforcement of the Dodd-Frank Act whistleblower protection provision, Congress should clarify that both oral and written reporting to the SEC is protected.

Authorizing Jury Trials

The WPRA clarifies that the Dodd-Frank Act authorizes a trial by jury and that Dodd-Frank Act whistleblower retaliation claims are not subject to mandatory arbitration.

Strengthening the SEC Whistleblower Reward Program

The WPRA would also strengthen several key aspects of the SEC's successful whistleblower program.[11]

Monetary Sanctions Collected by a Bankruptcy Trustee Would Qualify for an Award

The SEC whistleblower program issues awards to whistleblowers based on the total monetary sanctions collected in its successful enforcement actions. Eligible whistleblowers receive between 10% and 30% of the collections as an award. The current SEC whistleblower rules deem monetary sanctions collected by a bankruptcy trustee ineligible for an award.

As such, a whistleblower could report and halt an accounting fraud similar to WorldCom but would not be eligible to receive an award, as WorldCom filed for bankruptcy after its accounting scheme was revealed. Similarly, a whistleblower reporting and halting a Ponzi scheme to the SEC could halt the scheme and help return money to defrauded investors but would not receive an award if the recoveries for investors are obtained in a bankruptcy proceeding.[12]

To address this significant weakness in the SEC whistleblower program, the WPRA would authorize the payment of awards from "any monies recovered by a bankruptcy trustee as a result of the original information provided by a whistleblower."

Requiring Timely Processing of Whistleblower Award Applications

Most SEC whistleblowers are surprised about how many years it takes to receive an award after initially submitting a tip. Oftentimes, if a whistleblower submits a credible tip, the SEC's investigation will take two to four years, or longer, prior to the SEC bringing an enforcement action.

In some cases, the fraud is unequivocal, and the wrongdoer may choose to settle the matter after the investigation rather than contest it through litigation. In other matters, the SEC could litigate a case for years before ultimately concluding an enforcement action.

Once the SEC concludes a successful action with monetary sanctions in excess of $1 million, a whistleblower must submit an application for an award within 90 calendar days of the SEC posting

the action on its Notices of Covered Action page.[13]

It takes about two to three years for the SEC to determine whether a whistleblower is eligible for an award and the award percentage — the percentage of collected monetary sanctions in the covered action. This lengthy process feels like an eternity for SEC whistleblowers.

The WPRA would require the SEC to issue an initial award determination within one year of the deadline to apply for an award. Recognizing the challenges that the SEC faces in making complex determinations concerning applications for whistleblower awards, the WPRA permits extensions of that deadline in certain circumstances.

This requirement is substantially similar to a provision in the Whistleblower Programs Improvement Act, or S. 2529, that was introduced in the 116th Congress.[14]

Funding the SEC Office of the Whistleblower

The WPRA would authorize the SEC Office of the Whistleblower to increase its limited staffing without using taxpayer dollars by permitting it to fund operations from the Investor Protection Fund. The fund is financed entirely through monetary sanctions paid to the SEC by securities law violators and is used to pay whistleblower awards. No money is taken or withheld from harmed investors to pay those awards.

Preventing Arbitrary Reductions of Whistleblower Awards

A September 2020 amendment to the rules governing the SEC whistleblower program suggests that the SEC can arbitrarily reduce a whistleblower award if it determines that an award would be larger than reasonably necessary to reward the whistleblower and to incentivize other similarly situated whistleblowers to come forward.[15]

The WPRA clarifies that when the SEC determines a whistleblower's award, it will not lower an award based on its dollar amount. Rather, the award determination will be based solely on the stated criteria in the SEC whistleblower rules, e.g., the significance of the tip and the extent of the whistleblower's assistance.[16]

Nullifying the Amended Rule Restricting Awards for Related Actions

This August, SEC Chair Gary Gensler suspended[17] an amendment to the SEC whistleblower rules[18] that precludes the SEC in some instances from making an award in related enforcement actions brought by other law enforcement and regulatory authorities if a second, alternative whistleblower award program might also apply to the action. The WPRA would nullify that rule.

Promoting Success of the SEC Whistleblower Program

Last month, the SEC announced that its whistleblower program has paid approximately $1 billion in awards to whistleblowers for their tips and assistance that have led to the recovery of nearly $5 billion in sanctions and helped the SEC "detect, investigate, and prosecute potential violations of the securities laws."[19]

As former SEC Chairs Jay Clayton and Mary Jo White have publicly stated, retaliation protections are a key component of the whistleblower program. For the SEC to continue to attract whistleblower tips that protect investors and halt major frauds, whistleblowers must be protected against retaliation.

A recent poll shows that 81% of likely voters believe that Congress should prioritize enacting laws to protect corporate employees who report fraud.[20]

To ensure that truth-tellers such as Haugen will come forward, Congress should act without delay

to enact the WPRA.

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[1] https://www.zuckermanlaw.com/wp-content/uploads/Whistleblower-Protection-Reform-Act-of-2021-.pdf.

[2] The trial has also revealed that Holmes' retaliation against and intimidation of whistleblowers was carried out with the assistance of lawyers https://www.law360.com/articles/1422080/david-boies-threatened-theranos-whistleblower-jury-told.

[3] https://www.zuckermanlaw.com/sec-whistleblower-protections-dodd-frank-and-sarbanes-oxley-prohibitions-against-retaliation/.

[4] Digital Realty, Inc. v. Somers, 138 S. Ct. 767 (2018).

[5] Brief for Senator Charles Grassley as Amicus Curiae, 2,Digital Realty Trust, Inc. v. Paul Somers, No. 16-1276 (U.S. Supreme Court, 2018), https://www.scotusblog.com/wp-content/uploads/2017/10/16-1276-bsac-Sen.-Grassley.pdf.

[6] https://www.zuckermanlaw.com/proposed-legislation-would-strengthen-protections-for-corporate-whistleblower/.

[7] 570 U.S. 338 (2013).

[8] As discussed in a well-reasoned recentSixth Circuit decision holding that the False Claims Act's anti-retaliation provision proscribes post-employment retaliation, Haugen's whistleblowing following her resignation from Facebook should be protected under the Dodd-Frank Act's analogous whistleblower protection provision. See United States ex rel. Felten v. William Beaumont Hosp.,993 F.3d 428 (6th Cir. 2021). But there is also case authority reaching a contrary conclusion. The WPRA would clear up this split of authority.

[9] https://www.zuckermanlaw.com/sarbanes-oxley-authorizes-damages-repetitional-harm/.

[10] 131 S. Ct. 1325, 1335 (2011).

[11] https://www.zuckermanlaw.com/sp_faq/sec-whistleblower-program/.

[12] As highlighted in a recent Wall Street Journal article,John McPherson provided"extraordinary and continuing" assistance in helping the SEC halt a $1.4 billion investment scam, but because the target company declared bankruptcy, McPherson did not receive a whistleblower award. Whistleblower Thought He Would Get a Big Payout. Instead He Got Nothing and Went Broke, Wall St. J., June 27, 2021. Investors, however, were able to recoup more than $1 billion through the bankruptcy process.

[13] https://www.sec.gov/whistleblower/claim-award.

[14] https://www.zuckermanlaw.com/wp-content/uploads/2019/09/Whistleblower_Programs_Improvement_Act.pdf.

[15] https://www.zuckermanlaw.com/sec-adopts-amendments-to-whistleblower-rules-that-will-strengthen-some-aspects-of-the-program-but-also-reduce-large-awards-and-limit-protection-against-retaliation/.

[16] See §240.21F-6.

[17] https://www.sec.gov/news/public-statement/gensler-sec-whistleblower-program-2021-08-02#_ftn1.

[18] https://www.sec.gov/rules/final/2020/34-89963.pdf.

[19] https://www.sec.gov/news/press-release/2021-177.

[20] Stephen Kohn, Congress Should Pass Stronger Whistleblower Protections, Law 360 (Oct. 14, 2020), https://www.law360.com/articles/1318228/congress-should-pass-stronger-whistleblower-protections.
