NEW AND IMPROVED WHISTLEBLOWER PROTECTIONS FOR EMPLOYEES

New York University School of Law
Center for Labor and Employment Law
64th Annual Conference on Labor
The Impact of the Global Economic Crisis on the Workplace

June 9, 2011
New York City

Jonathan Ben-Asher
Ritz Clark & Ben-Asher LLP
40 Exchange Place - 20th floor
New York, N.Y. 10005
(212) 321-7075
jben-asher@RCBALaw.com
www.RCBALaw.com

Contents

I. **Whistleblowing in 2011**

Until recently, employee whistleblowers in the financial services sector in New York have faced some difficult obstacles. The New York Labor Law doesn't protect them, and the New York courts have refused to create a private right of action for retaliatory discharge in violation of public policy. The Sarbanes-Oxley Act has been construed narrowly by the U.S. Department of Labor and the courts, leaving many employees uncovered or burdened with proof requirements that favor defendants. For many employees who bring to light financial improprieties or fraud, the remedies have either been lacking or limited.

The financial crisis and meltdown convinced enough members of Congress that protecting whistleblowers -- and even encouraging them -- is important. In 2010, Congress created an entirely new and employee-friendly scheme of whistleblower protections, as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Dodd-Frank covers employees who make both internal and external complaints (depending on the context) and gives employees who disclose securities violations to the SEC a chance to receive substantial bounty awards. Congress also amended the Sarbanes-Oxley Act to make it easier for plaintiffs to bring and litigate their cases, and amended the False Claim (Qui Tam) Act in a plaintiff-friendly way as well.

Earlier in the financial crisis, Congress had created whistleblower protections for employees who complain about improprieties in the use of federal bail-out funds under the American Recovery and Reinvestment Act of 2009. These provisions are strong, but have not been widely tested, and since much of the bailout funds have been repaid, may become less significant for employees.

Financial whistleblowers now have significant additional protections and better remedies. This paper analyzes:

1) Developments in the law under the Sarbanes-Oxley Act;

2) The whistleblower provisions of Dodd-Frank, including crucial changes to the Sarbanes-Oxley Act; new protections for whistleblowers of entities which provide consumer financial services; the bounty incentive program for whistleblowers providing information to the SEC; the new anti-retaliation protections for whistleblowers providing information to the SEC; new amendments to the False Claims Act; and

3) The whistleblower provisions of the federal bail-out legislation, Sec, 1553 of the American Recovery and Reinvestment Act of 2009.

II. The Sarbanes-Oxley Act, Sec. 806

In 2002, Congress reacted to the multiplying corporate accounting scandals by enacting protections for employees of publicly traded companies who complain about or disclose certain frauds by their employers. Sec. 806 of the Sarbanes-Oxley gave employees who were retaliated against for making such complaints the ability to seek reinstatement and damages at the U.S. Department of Labor and, in many cases, in federal court.

However, as detailed below, the initial expectations that SOX cases would be a useful remedy for whistleblowers proved highly over optimistic. Decisions from the Department of Labor and the federal courts dramatically narrowed the classes of employees protected by SOX and the protections they could invoke. As a result, employees have rarely prevailed in SOX cases.

In Dodd-Frank, Congress took steps to strengthen SOX Sec. 806. In addition, entirely new whistleblower protections created by Dodd-Frank are broader and stronger than those of SOX, and may in the end eclipse Sec. 806 as a remedy for employees.

A. SOX protections

SOX's whistleblower provision is in Section 806 of the Act, titled "Protection for Employees of Publicly Traded Companies who Provide Evidence of Fraud," and codified in 18 U.S.C. Sec. 1514A, "Civil Action to protect against retaliation in fraud cases." It prohibits a publicly traded company from engaging in a wide range of retaliatory actions: discharging, demoting, suspending, threatening, harassing or "in any other manner" discriminating against an employee in the terms and conditions of employment, because of the protected whistleblowing activities listed in the section. Whether an employer's action is an adverse employment action is analyzed in accordance with the Supreme Court's decision in *Burlington Northern & Santa Fe Railway Co. v. White*, 548 U.S. 53 (2006). *Allen v. Administrative Review Board*, 514 F.3d 468, 476 n. 2 (5th Cir. 2008).

The statute prohibits retaliation by a broad range of actors. These include not only the employer, but any officer, contractor, subcontractor, employee or agent. 18 U.S.C. Sec. 1514A(a).

B. Covered employers and employees

Sec. 806 covers the employees of all publicly traded companies. "Publicly traded companies" are defined as companies with a class of securities registered under section 12 of the Securities Exchange Act of 1934 (15 U.S.C. Sec. 78*l*), or which are required to file reports under section 15(d) of the Act (15 U.S.C. Sec. 78o(d)). 18 U.S.C. Sec. 1514A(a).

1. Subsidiaries of publicly traded companies

Sec. 806 as originally enacted did not specifically cover non-publicly traded subsidiaries of publicly traded companies. As a result, the courts and DOL issued conflicting decisions on whether those subsidiaries are governed by the statute. These decisions fall into three groups: decisions holding that Congress intended to cover subsidiaries; that Congress intended to exclude them; and that subsidiaries are covered when the parent and subsidiary are sufficiently intertwined.

The conflicting decisions are no longer relevant, because with the passage of Dodd-Frank, subsidiaries are now covered employers if their financial information is included in the parent's consolidated financial statement. See Sec. III A, below.

2. Agents and contractors

Some decisions have found liability for related entities which are the "contractor, subcontractor or agent" of a publicly held parent. See *Kalkunte v. DVI Financial Services Inc*. ARB Cases 5-139 and 5-140 (2/27/09) (Non-publicly traded company hired by bankrupt publicly traded employer to handle financial issues and provide CEO was contractor, subcontractor or agent and so could be liable under Sec. 806).

However, the statute's bar against retaliation by employers' agents does not give whistleblowing protection to an employee of a non-public company merely because the non-public employer has business relations with a publicly traded company. *Brady v. Calyon Securities (USA) et al.*, 406 F. Supp.2d 307 (S.D.N.Y. 2005). The court noted that, in contrast, companies "that have acted as agents of publicly traded companies *with respect to their employment relationships*" could be liable under Sec. 806. In *Brady*, the defendant investment bank merely acted as the agent or underwriter in its investment banking relationship with the employer. The court noted that Sec. 806 "simply lists the various potential actors who are prohibited from engaging in discrimination on behalf of a covered employer," and that an employer's "agent or subcontractor" is one of those actors.

See *also Minkina v. Affiliated Physicians Group*, 2005 SOX 19 (February 22, 2005, appeal dismissed, ARB July 29, 2005) (same reasoning as *Brady*); *Goodman v. Decisive Analytics Corp.*, 2006 SOX 11 (January 10, 2006) (Contractor or agent "when discriminating against the employee must have been acting on *behalf* of the publicly traded company").

3. Foreign employers of foreign employees

In *Carnero v. Boston Scientific Corporation*, 433 F.3d 1 (3d Cir. 2006), cert. denied, 548 U.S. 907 (2006), the Third Circuit ruled that a foreign employee of a foreign corporation is not covered by Sec. 806 concerning the foreign employer's misconduct abroad.

The court relied on the general presumption against extra-territorial application of U.S. law; the existence of other provisions of SOX which explicitly provide for extra-territorial application; the absence of references in the legislative history to foreign application and what it characterized as Congress' "focus on problems within the United States;" the dangers of granting authority to DOL and U.S. courts to "delve into the employment relationship between foreign employers and their foreign employees;" Congress' failure to provide a means to enforce Sec. 806 against foreign employers; the absence of a venue provision governing foreign employers; prior ALJ decisions declining to enforce Sec. 806 extraterritorially; and the overall lack of Congressional intent to reach foreign employers.

However, a 2008 decision from the Southern District of New York took a far more liberal view of extraterritoriality. *O'Mahony v. Accenture Ltd*, 537 F. Supp.2d 506 (S.D.N.Y. 2008). There, the plaintiff worked in France for a French subsidiary of a Bermuda company. She had previously worked in the U.S. for an American subsidiary. The court rejected defendants' argument that dismissal was required under *Carnero*.

The court distinguished *Carnero*, focusing on several factors: 1. O'Mahony had previously worked in the U.S. for the American subsidiary before her expatriate assignment in France; 2. As a result, hearing the case would not interfere with the relationship between an foreign employer and its foreign employees; 3. O'Mahony had alleged that fraud was committed in the U.S. (Accenture's decision not to withhold French Social Security taxes from her pay); 4. O'Mahony was suing not just the foreign parent, but also the U.S. subsidiary, based on the American company's actions in the U.S.

4. Claims by in-house counsel

What happens when the whistleblower is an employer's in-house counsel? The Ninth Circuit has ruled that the possibility of disclosure of attorney-client privileged information does not bar in-house counsel from bringing a SOX charge. The court relied on the fact that the district court can supervise the proceedings to minimize the prejudice to the employer's confidential information. *Van Asdale v. International Game Technology*, 577 F.3d 989 (9th Cir. 2009).

C. Protected whistleblowing activity

An employee is protected from retaliation for engaging in any lawful act taken to provide information, cause information to be provided, or otherwise assist in an investigation, regarding any conduct which the employee "reasonably believes" constitutes a violation of the criminal provisions noted in the statute, any SEC rule or regulation, or any provision of federal law relating to fraud against shareholders. 18 U.S.C. Sec. 1514A(a)(1). The criminal statutes noted are 18 U.S.C. Secs. 1341 (mail fraud), 1343 (wire fraud), 1344 (bank fraud) and 1348 (securities fraud). One court has held that violation of an SEC guideline – as opposed to rule or regulation – cannot be the predicate of a protected complaint under Sec. 806. *Allen v. Stewart Enterprises*, 514 F.3d 468 (5th Cir. 2008).

A recent expansive decision by Judge Sweet in the Southern District holds that an employee is also protected for reporting fraudulent acts by an employer's clients. Sharkey v. J.P. Morgan Chase & Co., 2010 U.S. Dist. LEXIS 139761 (S.D.N.Y. 2010). In that case, the employee complained internally that a long term Private Wealth client of J.P. Morgan was engaged mail fraud, bank fraud and money laundering. The court held that "[b]ecause SOX is a statute designed to promote corporate ethics by protecting whistleblowers from retaliation, it should not be read narrowly," and that Sec. 806 "by its terms does not require that the fraudulent conduct or violation of federal securities law be committed directly by the employer that takes the retaliatory action." (However, the court dismissed the complaint, finding that the plaintiff had not adequately alleged the specific illegal conduct which was the basis of her complaint.)

A significant issue in SOX cases has been whether employees are protected only if they complain about perceived fraud on shareholders, or about any of the frauds noted in Sec. 806. Courts are divided on this issue.

An example of the expansive view is O'*Mahony v. Accenture Ltd*, 537 F. Supp.2d 506 (E.D.N.Y. 2008). The court concluded that Sec. 806 "clearly protects an employee against retaliation based on the whistleblower's reporting of fraud under any of the enumerated statutes regardless of whether the misconduct related to 'shareholder' fraud." See also *Reyna v. Con Agra Foods, Inc*., 506 F. Supp.2d 1363 (M.D. Ga. 2007) (reporting of mail or wire fraud sufficient, even if unrelated to fraud on shareholders; employee had reported a supervisor's scheme to have ineligible relatives covered as dependants on the employer's health insurance); *Smith v. Corning Inc.*, 496 F. Supp. 2d 244 (W.D.N.Y. 2007) (denying employer's motion to dismiss employee's claim based on allegation that company was implementing a financial reporting system that did not comply with GAAP, which would have resulted in incorrect reports to shareholders). However, to the contrary, see *Bishop v. PCS Administration*, 2006 WL 1460032 (N.D. Ill. 2006); *Livingston v. Wyeth*, 520 F.3d 344 (4th Cir., 2008), discussed below.

Employees are protected when they provide information or assistance, either within the company or to an appropriate federal official. Within a company, employees can go to "a person with supervisory authority over the employee," or someone who has authority to "investigate, discover, or terminate misconduct." 18 U.S.C. Sec. 1514A(a)(1)(C). Externally, they can provide information or help to a federal regulatory or law enforcement agency, or a congressperson or congressional committee. 18 U.S.C. Sec. 1514A(a)(1)(B) and (C).

Employees are also protected from retaliation for filing, participating in, or assisting in a proceeding relating to the listed federal provisions, if the employer has "any knowledge" of the employee's activity. The "proceeding" can be one which has been filed, or is "about to be filed." 18 U.S.C. Sec. 1514A(a)(2). The "filed or about to be filed" language also appears in the anti-retaliation prohibition of the False Claims Act, and in that context protects employees who are collecting information about possible fraud "before they have put all the pieces of the puzzle together." [1]

For an employee to show protected activity, whether by providing information or assisting in an investigation, the employee "must point to point to affirmative acts which advance the investigation." *Mahoney v. Keyspan Corp.*, 2007 WL 805813 (E.D.N.Y. March 12, 2007). "Merely expressing concern or support for a whistleblower" is not protected activity. The court in *Mahoney* held that plaintiff's conversations with Keyspan's in-house and outside counsel in support of a whistleblower did not qualify.

However, the court ruled that plaintiff did engage in protected activity by successfully urging the CEO to meet with the whistleblower and the company's lawyers to " 'hear directly… the details of accounting frauds at the company.' " The court relied on plaintiff's assistance in "opening a channel of communication with the CEO," and held that Sec. 806 applies not only to "those who blow the whistle" but also those who "make the whistle audible." A contrary interpretation, the court noted, would "lead to a point that isolates the whistleblower in a way that Congress could not have intended."

While protected activity includes the "lawful acts" noted in Sec. 806, it may not include an employee's refusal to engage in unlawful activity. In a Fifth Circuit case, the employee, an equity analyst at an investment advisory firm and broker-dealer, refused to

---

1 See, e.g., *U.S. ex rel. Yesudian v. Howard University*, 153 F.3d 731, 739-40 (D.C. Cir. 1998).

change her rating of a stock, despite pressure from her superiors at a meeting, and said she would not sign a report that rated the stock more highly. The court upheld a decision of the Administrative Review Board finding that the employee had not engaged in protected activity, because the employer had not expressed its intent to make her change her rating, and the employee had never told a supervisor that the rating would violate securities laws. *Getman v. Administrative Review Board*, 2008 WL 400232 (5th Cir. 2008).

To encourage whistleblowing, employers are required to set up audit committees, which must have procedures for employees to confidentially and anonymously report concerns regarding questionable accounting or auditing matters. Public L. No. 107-204 at Sec. 301, amending 15 U.S.C. 78f. Outside of civil litigation, Sarbanes-Oxley criminalizes retaliation against whistleblowers. These penalties apply even if the object of retaliation is not an employee. 18 U.S.C. 1513(e).

D. What is a "reasonable belief" that fraud has occurred?

A major question in SOX cases is the level of knowledge a plaintiff must have regarding an employer's alleged fraud to qualify for whistleblower protection. Sec. 1514(a)(1) protects employees who provide information, cause information to be provided, or otherwise assist in an investigation regarding conduct which the employee "reasonably believes" constitutes a violation of the listed provisions.

1. "Good faith" standard

The legislative history indicates that Congress intended that the reasonable belief standard be liberally applied. Noting that retaliation cases should be subject to the "reasonable person" test, the Judiciary Committee cited to a whistleblower case under the Clean Water Act in which the Third Circuit spoke of protecting "good faith" and "non-frivolous" employee complaints. S. Rep. No. 107-146, 107th Cong., 2d Sess. 19 (2002). *Passaic Valley Sewerage Commissioners v. United States Department of Labor*, 992 F.2d 474, 478-79 (3rd Cir. 1993).

Some courts in SOX cases have adopted the *Passaic Valley* analysis, noting that "the threshold is intended to include all good faith and reasonable reporting of fraud, and there should be no presumption that reporting is otherwise, absent specific evidence." See, e.g., *Collins v. Beezer Homes USA Inc.*, 334 F.Supp.2d 1365 (N.D. Ga. 2004); *Bishop v. PCS Administration (USA), Inc.*, 2006 WL 1460032 (N.D. Ill. 2006). As these cases noted, Sec. 806 does not require whistleblowers to identify the statutory provisions they believe are being violated. "If Congress had intended to limit the protection of Sarbanes

Oxley…or to have required complainants to specifically identify the code section they believe was being violated, it would have done so." Id.

A good faith, non-frivolous standard is consistent with the Department of Labor's regulations. Under them, a complainant may be sanctioned only for filing a "frivolous" or "bad faith" charge. 29 CFR 1979.105(b). DOL has interpreted the reasonable belief standard to protect employees who are completely mistaken in their evaluation of the employer's alleged fraud. As one ALJ wrote in a decision under Sec. 806, "[a] belief that an activity was illegal may be reasonable even when subsequent investigation proves a complainant was entirely wrong. The accuracy of falsity of the allegations is immaterial…." *Halloum v. Intel Corporation*, 2003 SOX 0007, March 4, 2004.

A "good faith" standard is also entirely sensible. Given the complexities of the violations that employees may complain about (e.g. mail fraud, bank fraud, wire fraud, securities fraud), an employee should not be required to have a professional's sophisticated understanding of the intricacies of federal securities and criminal law to be protected from retaliation.

2. Relation to frauds listed in Sec. 806

At the same time, an employee's communications to the employer "must definitively and specifically relate to [one] of the listed categories of fraud or securities violations [in] 18 U.S.C. § 1514A(a)(1)." *Vodopia v. Koninklijke Philips Electronics, N.V.*, 2010 U.S. App. LEXIS 22081 (2nd Cir. 2010); *Van Asdale v. International Game Tech.*, 577 F.3d 989, 996-97 (9th Cir. 2009); *Day v. Staples, Inc.*, 555 F.3d 42, 56 (1st Cir. 2009); *Welch v. Chao*, 536 F.3d 269, 275 (4th Cir. 2008); *Allen v. Administrative Review Board.*, 514 F.3d 468, 476 (5th Cir. 2008).

An instructive decision on this issue is *Fraser v. Fiduciary Trust Company International*, 417 F.Supp.2d 310 (S.D.N.Y. 2006). While the court noted that Congress did not intend to require the plaintiff to identify a specific code section he believes was violated, it held that "general inquiries" are not sufficient. Rather, "the reported information must have a certain degree of specificity [and] must state particular concerns which, at the very least, reasonably identify a respondent's conduct that the complainant believes is illegal." Protected activity must "implicate the substantive law protected in Sarbanes-Oxley 'definitely and specifically.'" (Plaintiff engaged in protected activity by drafting an email questioning the company's failure to provide the same advice to all its clients concerning the advisability of selling WorldCom bonds to avoid losses, and by advising the defendant's President that he had been told not to circulate the e-mail.) See also *Bozeman v. Per-Se Technologies*, 456 F.Supp.2d 1282, 1359 (N.D. Ga. 2006).

3. Plaintiffs with special expertise

When a plaintiff has special expertise in the issues surrounding the fraud, he may be held to a higher standard. In *Allen v. Administrative Review Board*, 514 F.3d 468 (5th Cir. 2008), the Fifth Circuit held that the objective reasonableness of a complainant's belief must be evaluated from the perspective of the complainant, and that the reasonableness of the belief of a licensed CPA must be evaluated from the perspective of an accounting expert. As a result, the court determined that the plaintiff should have understood that the records he cited as the basis for the alleged fraud did not have to be submitted to the SEC, and that the company had not violated an SEC rule or regulation.

4. Speculation insufficient:

Courts have also rejected whistleblower claims based on a whistleblower's speculation that an employer's non-fraudulent activity might, in the end, lead to financial losses and ultimate fraud on shareholders. These decisions have required that the employee's belief that the company is engaged in misconduct be both subjectively and objectively reasonable. See, e.g.,

Day v. Staples, Inc. 555 F.3d 42 (1st Cir. 2009) The court held that an employee's complaint about shareholder fraud must allege basic elements of securities fraud (Misrepresentation / omission, scienter, loss, and a causal connection between the misrepresentation and the loss). The loss to the company must be material. Thus, alleged data manipulation not related to company's financial condition and not reported to shareholders does not qualify as a predicate fraud for an action under Sec. 806. Similarly, also not qualifying are complaints about inefficiency, and even violations of GAAP.

Platone v. U.S. Department of Labor, 548 F.3d 322 (4th Cir. 2008) (Alerting superiors to billing discrepancy that affects short term profits does not constitute a claim of securities fraud.)

Livingston v. Wyeth Inc., 520 F.3d 344 (4th Cir.2008) (Finding no reasonable belief for plaintiff's complaints that pharmaceutical company would be unable to meet compliance and training deadlines of a consent decree regarding adulterated drugs and therefore would be fined $15,000 a day by the FDA; plaintiff's belief was speculative, as he did not have a reasonable belief about an existing violation);

Bishop v. PCS Administration (USA), Inc., 2006 WL 1460032, 2006 U.S. Dist. LEXIS 37230 (N.D. Ill. 2006) ("a reasonable belief that implementing certain procedures will be insufficient to prevent violations is not, by itself, a reasonable belief that a violation has occurred or been attempted." Plaintiff's belief must be both subjectively and objectively reasonable, and in determining reasonableness, the employee's experience, background and access to information are relevant.)

DOL has also dismissed claims based on an employee's speculation that an employer's non-fraudulent conduct might create financial losses. See, e.g., *Smith v. Hewlett Packard*, 2005 SOX 00088 (January 19, 2006) (no protected activity where employee complained about "systematic race discrimination" caused by allegedly discriminatory evaluation processes, and noting that the result might be different if plaintiff had complained about the employer's failure to disclose to shareholders the filing of a discrimination class action); *Minkina v. Affiliated Physician's Group*, 2005 SOX 19 (February 22, 2005) (employee did not engage in protected activity by reporting to OSHA what she believed to be dangerous air quality in the workplace, since the possibility that those conditions would lead to financial losses was mere speculation).

The Ninth Circuit (but of course) takes a more liberal approach. *Van Asdale v. International Game Technology,* 577 F.3d 909 (9th Cir. 2009). While the court stated the law similarly as the First Circuit did in *Day v. Staples,* above, the court emphasized that the employee can be wrong in his belief that fraud occurred, and need not have reached a conclusion that fraud occurred.

A 2007 decision of the Administrative Review Board, affirmed by the Fourth Circuit, shows how the reasonable belief standard is difficult for employees to meet. *Welch v. Cardinal Bankshares Corporation,* ARB Case 05-064 (ARB, May 31, 2007, *aff'd Welch v. Chao*, 536 F. 3d 269 (4th Cir. 2008), *cert. denied,* 129 S. Ct. 1985 (2009). After an extended hearing, the ALJ below had ruled that Cardinal Bankshares violated Sec. 806 by terminating its CFO in retaliation for various complaints he had made about financial improprieties. The CFO, Welch, had a) complained about insider trading by Bank officers; b) refused to sign off on a quarterly financial statement overstating the company's income; c) refused to attest to the validity of financial statements because the company's auditor did not provide him with necessary information; and d) complained that Cardinal's internal controls improperly permitted employees outside the finance department to make journal entries without his knowledge.

The ALJ rejected Cardinal's argument that Welch had only been fired because he refused to meet, without counsel, with the company's auditors about the issues he had raised. The ALJ first considered the close temporal relationship between Welch's protected activity and his termination; he noted that Welch was fired only six weeks after his first complaint, and shortly after his later complaints. The ALJ noted that, in any event, Cardinal's management team engaged in a campaign to discredit and terminate him that began well before Welch refused to participate in the meeting without his lawyer, immediately after he refused to sign off on the disputed quarterly report. Finally, the ALJ ruled that Cardinal would not have terminated Welch but for his protected activity, rejecting the argument that the presence of Welch's counsel at the meeting was either unwarranted or prohibited by the company's rules.

As for remedies, the ALJ ordered that Welch be reinstated, and required further submissions on the calculation of an award of back pay, attorney's fees and costs The ALJ did not address the issue of emotional distress damages, which, as noted below, are arguably within the category of "special damages."

On appeal, the ARB reversed the ALJ's decision. It ruled that, as a matter of law, Welch could not have had a reasonable belief that Cardinal Bankshares was engaging in fraud. It held that Welch had to prove both that he actually believed there was fraud, and that a person with his expertise and knowledge would also have had that belief. As the CFO, Welch should have known that no fraud occurred. The ARB also held that an employee's belief that an employer is violating accounting standards, such as those in GAAP, is insufficient grounds for a SOX claim, because Congress sought to protect only employee complaints about violations of the statutory and regulatory provisions listed Sec. 806. Finally, Welch's complaints about Cardinal's lack of internal controls were also not protected activity, since "[a]lthough having a deficient internal control may make an institution more vulnerable to fraud, in itself it is not fraudulent."

The Fourth Circuit affirmed. *Welch v. Chao*, 536 F. 3d 269. The Court held that Sec. 806 contains an independent materiality requirement, apart from the materiality required by the predicate fraud statutes listed in Sec. 806. It further held that while a plaintiff does not have to be correct in his belief that the employer actually violated the law, he must still have made a complaint about conduct the he reasonably believed "definitely and specifically" related to a violation of one of the listed provisions. However, an employee does not have to identify specific statutory provisions in his complaint to the employer.

The Court did find that the ARB was wrong in holding that communications about misclassifications in a company's financial statements can never be the basis of a SOX complaint. But it concluded that Welch had "utterly fail[ed] to explain how Cardinal's conduct could reasonably be regarded as violating" any of the provisions listed in Sec. 806, and that Welch had supported his argument before the ARB with only inapposite and irrelevant authority or conclusory, general statements.

E. Enforcement

Employees have a choice of remedies under SOX. While an employee has to first file a charge with the Department of Labor, if 180 days elapse before DOL has completed all the steps required by statute (investigation, hearing, and appeal), the employee can remove the charge to federal court in an action de novo.

Employees must file a charge with the Department of Labor within 180 days from when the violation occurred. 18 U.S.C. Sec. 1514A(b)(2)(D). (As discussed in Section IIIA below, the original statute of limitations under SOX was 90 days, but Dodd-Frank lengthened it). The 180 days runs from the date the employee receives "'final, definitive, and unequivocal notice' of an adverse employment decision," and the time limit will be "equitably tolled" only in extraordinary circumstances. *Halpern v. XL Capital, Ltd.*, ARB Case No. 04-120, 2005 DOL Ad. Rev. Bd. LEXIS 98 (August 31, 2005). Each discriminatory act starts a new clock for the filing of a charge (or at least the amendment of a prior charge.) *McClendon v. Hewlett-Packard Company*, 2005 WL 2847224 (D. Idaho 2005); *Willis v. Vie Financial Group,* 2004 WL 1774575 (E.D. Pa. 2004)

DOL is required to investigate the charge. If DOL does not issue a final decision (including a decision on an administrative appeal) within 180 days, the employee can bring an action "for de novo review" in federal court. An employee cannot sue in federal court if his own "bad faith" caused DOL's delay. 18 U.S.C. Sec. 1514A(b)(1)(B).

1. Administrative proceedings at the Department of Labor

DOL's proceedings are governed by the procedures set out in the federal law, enacted in 2000, covering whistleblowing in the airline industry – Sec. 519 of the Wendell H. Ford Aviation Investment and Reform Act for the 21st Century, 49 U.S.C. Sec. 42121(b). 18 U.S.C. Sec. 1514A(b)(2)(A). The Department of Labor's regulations on SOX enforcement are at 29 CFR Part 1980.

a. The employee's prima facie case

At DOL, the complainant must make a prima facie showing that "protected activity" under Sec. 806 was a "contributing factor" to the unfavorable personnel action alleged in the complaint. DOL's regulations require that the charge, as supplemented by DOL's interviews with the charging party, allege "the existence of facts and evidence to make a prima facie showing" (i) that the employee engaged in protected activity or conduct, (ii) that the named person knew or suspected, actually or constructively, that the employee engaged in the protected activity, (iii) that the employee suffered an unfavorable personnel action, and (iv) that there are circumstances sufficient to raise an inference that protected activity was a contributing factor in the unfavorable action. 29 CFR Sec. 1980.104(b). The regulations state that the employee can normally prove the employer's knowledge and causation by showing, for example, that the adverse action took place shortly after the protected activity. 29 CFR 1980.104(b)(2).

Without this prima facie showing, the charge will be dismissed, without an investigation. 29 CFR 1980.104(b)(2), 29 CFR 1980.104(d). Even if the employee makes the prima facie showing, the charge will also be dismissed if the employer demonstrates by "clear and convincing evidence" that it would have taken the same unfavorable action absent the employee's protected activity. 29 CFR 1980.104(c). The employer has twenty days from receiving notice of the complaint to file a written statement, affidavits and documents in support of its position, and to request a meeting with DOL. 29 CFR 1980.104(c).

b. Department of Labor investigations

If the employee makes the required *prima facie* showing and it is not rebutted by the employer, DOL must conduct an investigation, and complete it within 60 days after the complaint is filed. The investigation is to determine if there is "reasonable cause" to believe that a violation occurred. DOL is supposed to investigate in a manner which protects the confidentiality of witnesses who provide information on a confidential basis. [2]

DOL should also determine whether the information gathered initially warrants preliminary reinstatement while the charge is pending. If so, DOL gives the employer notice of the substance of the relevant evidence, including redacted or summarized witness statements, and the employer has ten business days to respond in writing and meet with investigators to oppose preliminary relief. [3]

After conducting the investigation, DOL issues written findings as to whether there is reasonable cause to believe the employer discriminated against the employee in violation of the Act. [4] If DOL does find in the employee's favor, it is supposed to order preliminary relief, which can include reinstatement, back pay, compensation for "special

---

[2] 29 CFR 1980.104(d), 1980.105(a).

[3] 29 CFR Sec. 1980.104(e).

[4] 29 CFR Sec. 1980.105(a).

damages,"[5] and costs and expenses, including attorney's and expert witness fees.[6] DOL's findings and preliminary order are effective within thirty days unless either party files timely objections and requests a hearing.[7] The filing of objections stays all aspects of the order, *excep*t for an order of reinstatement.[8]

If DOL has ordered reinstatement, it is effective immediately.[9] DOL will deem reinstatement "inappropriate" if the employer establishes that the complainant is a security risk, even if the information on which that contention is based was obtained after the employee's discharge. 29 CFR 1980.105(a)(1).

However, an employee's ability to obtain reinstatement has been impeded by the Second Circuit's decision in *Bechtel v. Competitive Technologies*, *Inc*. 448 F.3d 469 (2d Cir. 2006). In *Bechtel*, the court reversed the district court's preliminary injunction requiring the employer to reinstate the employee. The Court of Appeals held that a district court lacks jurisdiction to enforce a reinstatement order of the Department of Labor.

DOL's regulations provide that there is no ALJ review of a decision by OSHA to conduct an investigation. If an ALJ determines that the complaint was erroneously dismissed, the ALJ will hear the case on the merits, rather than remanding to OSHA for the completion of an investigation.[10]

c. Department of Labor hearings

DOL's administrative hearings are conducted in accordance with the rules of practice and procedure of DOL's Office of Administrative Law Judges.[11] Hearings are

---

[5] "Special damages" are discussed in Sec. 3 below.

[6] 29 CFR 1980.105(a)(1).

[7] 29 CFR 1980.105(c), 1980.106(a).

[8] 29 CFR 1980.106(b)(1).

[9] 29 CFR 1980.105(c).

[10] 29 CFR 1980.109(a).

[11] 29 CFR 1980.107(a), referring to procedures codified at 29 CFR Part 18, Subpart A. *See* 29 CFR 18.1 through 29 CFR 18.59.

de novo and on the record,[12] and formal rules of evidence do not apply.[13] The OALJ's rules incorporate the provisions of the Administrative Procedure Act (5 U.S.C. Sec. 554), which provide for, among other things, the issuance of subpoenas and taking of depositions, cross-examination, and other procedural protections.[14] DOL must conduct the hearing "expeditiously,"[15] and issue a final order within 120 days after the hearing concludes.[16]

DOL seeks to minimize the likelihood that employees will take advantage of the Act's provision allowing them to sue an employer in federal court if DOL has not issued a final decision within 180 days of the complaint. For example, the summary of the regulations speaks of the need for hearings to be conducted as expeditiously as possible "particularly in light of the unique" 180 day rule, and an ALJ may order those limits extended unless the complaining party agrees to delay filing a federal court action for some period of time after the 180 days.[17] Thus, ALJs are given "broad discretion" to limit discovery in order to expedite the hearing.[18]

DOL may choose to prosecute cases involving significant legal issues, large numbers of employees, egregious violations or where the interests of justice require.[19] The SEC may also participate as an amicus at any time, in the SEC's discretion. Even if the SEC does not participate in the proceeding, the SEC may require that the parties provide it with copies of all pleadings.[20]

---

[12] 29 CFR 1980.107(b).

[13] 29 CFR 1980.107(d).

[14] 5 U.S.C. Sec. 554; 5 U.S.C. Sec. 556 (c) and (d).

[15] 49 U.S.C. § 42121(b)(2)(A).

[16] 49 U.S.C. Sec. 42121(b)(3).

[17] 68 FR 102 at 31862 (May 28, 2003).

[18] 29 CFR 1980.107(b).

[19] 69 FR 102 at 31862 (May 28, 2003).

[20] 29 CFR 1980.108(b).

DOL must issue a decision within 120 days after the hearing.[21] DOL may only determine that a violation occurred if the complainant demonstrates that the protected activity was a contributing factor in the challenged personnel action. If the employer shows by clear and convincing evidence that it would have taken the same action in the absence of the protected activity, DOL cannot order any relief. [22]

If the ALJ concludes that the employer violated Sec. 806, the order will provide all relief necessary to make the employee whole, including reinstatement, back pay, "special damages," litigation costs, attorney's fees, and expert witness fees. If the employer shows that the complaint was frivolous or brought in bad faith, the ALJ may award a maximum of $1,000 in attorney's fees to the employer. [23]

d. Appeals from DOL hearing decisions

Either side may seek review of the ALJ's decision by filing a petition at DOL's Administrative Review Board (ARB) within ten business days. If the ARB accepts the case for review, the ALJ's decision becomes "inoperative," although the ALJ's reinstatement order will remain in effect. The ARB is to issue a final decision within 120 days after the hearing concludes. [24]

Assuming DOL issues a final decision within 180 days after the charge was filed, the employee's access to court is limited to appealing that decision to the Court of Appeals for the circuit in which the violation occurred. (The employer has the same right.) [25] The employee may also seek enforcement of the DOL's order in federal district court. [26]

---

[21] 49 U.S.C. Sec. 42121(b)(3). This requirement is in the Ford Aviation Investment and Reform Act, which governs proof and proceedings cases under Sec. 806. See 18 U.S.C. Sec. 11514(b)(2)(A).

[22] 29 CFR 1980.109(a).

[23] 29 CFR 1980.109(b).

[24] 29 CFR 1980.110. The hearing is deemed to conclude ten business days after the ALJ's decision. 29 CFR 1980.110(c).

[25] 49 U.S.C. Sec. 42121(b)(4).

[26] 49 U.S.C. Sec. 42121(b)(6).

e. The reality for employees under SOX

Unfortunately, SOX has not proven to be the strong weapon the employee bar had hoped it would be. Employees have lost the overwhelming proportion of SOX cases, and both DOL and the courts have interpreted Sec. 806 in a restrictive manner. A comprehensive study of all SOX cases at the Department of Labor through Fiscal Year 2008 starkly demonstrates the difficulties employees face. Prof. Richard Moberly, "Unfulfilled Expectations: An Empirical Analysis of Why Sarbanes-Oxley Whistleblowers Rarely Win," 49 William and Mary Law Review 65 (2007):

Cases completed:	172
Dismissed:	113
Withdrawn:	24
Settled:	39
Merit findings (for employee)	0

The employee "win rate" through 2005 at DOL: about 6 %

Settled: 15 – 18%
Withdrawals: 40% at ALJ level (most are not withdrawn to go to federal court)

The recent amendments to SOX in the Dodd-Frank Act were in part a reaction to the difficulties employees have had in proceeding under SOX. And with Dodd-Frank, many employees no longer need SOX as a protection and litigation weapon, because of Dodd-Frank's broader coverage and remedies.

Resources regarding DOL decisions and appeals:

The Department of Labor publishes decisions of both Administrative Law Judges and the Administrative Review Board at www.oalj.dol.gov.

2. Federal court actions

If DOL does not issue a final decision within 180 days, the employee can bring an action "for de novo review" in federal court. [27] Once the federal action is

[27] 18 U.S.C. Sec. 1514A(b)(1)(B). DOL's regulations require that the federal court plaintiff give fifteen days notice to DOL and all other parties of the plaintiff's intention to sue. 29 CFR

filed, DOL loses jurisdiction over the case. *Stone v. Duke Energy Corp.*, 432 F.3d 320 (4th Cir. 2005) [28]

3. Available relief

A prevailing plaintiff is entitled to "all relief necessary to make the employee whole," which "shall include" reinstatement with seniority, back pay with interest, and compensation for any "special damages sustained as a result of the discrimination," including attorney's fees and costs. 18 U.S.C. Sec. 1514A(c).

Sarbanes-Oxley does not state whether a plaintiff can recover damages for emotional distress as part of the "special damages" authorized by Sec. 1514(A)(c)(2)(C). The legislative history only speaks of employees recovering "compensatory damages to make a victim whole," including attorney's fees and costs.

However, a 2007 case from the Eastern District of New York held that "special damages" include damages for "reputational injury" which diminish a plaintiff's future earning capacity. It is not clear from the opinion whether the court was referring to front pay, or damages to compensate plaintiff for the less tangible harm to his reputation and earning capacity. *Mahoney v. Keyspan Corp.*, 2007 WL 805813 (E.D.N.Y. March 12, 2007). The court in *Mahoney* relied on a similar decision from the Southern District of Florida, holding that "a successful Sarbanes-Oxley plaintiff cannot be made whole without being compensated for damages for reputational injury that diminished plaintiff's future earning capacity." *Hanna v. WCI Communities, Inc.*, 348 F.Supp.2d 1332 (S.D. Fl. 2004). But see *Murray v. TXU Corp.*, 2005 WL 1356444 (N.D. Tex. 2005) (Special

---

1980.114(b). This requirement does not appear in Sarbanes-Oxley or the Ford Aviation Investment Act, and should not be jurisdictional.

As noted above, DOL has been concerned over the possibility that a plaintiff could sue in federal court while or after the ARB reviews an ALJ's decision. Noting that duplicative litigation would waste the resources of the parties, DOL and the courts, DOL has encouraged courts to apply principles of issue preclusion and claim preclusion to some of these situations. 68 FR 102 at 31863 (May 28, 2003). See also *Stone v. Duke Energy Corp.*, 2004 WL 1834597 (W.D.N.C. 2004), *aff'd*, 432 F.3d 320 (4th Cir. 2005) (noting DOL's position and declining to issue writ of mandamus compelling continued administrative proceedings, since DOL had only done an initial investigation and "this case should be resolved in the manner of a typical federal question case.")

[28] In pleading Sarbanes-Oxley whistleblower claims, employees' counsel should consider the requirement of Fed. R. Civ. P. 9(b) that fraud claims be pleaded with particular specificity. One court has found that this rule applies in cases under Sec. 806. *Bishop v. PCS Administration (USA), Inc.*, 2006 WL 1460032 (N.D. Ill. 2006).

damages limited to litigation costs, expert witness fees and reasonable attorney's fees, based on text of Sec. 806, and analogizing to pre-1991 remedies of Title VII).

Some courts have construed the "special damages" permitted by the similarly-worded anti-retaliation provision of the False Claims Act to permit awards for emotional pain and suffering. [29] Whistleblowers are often ostracized and ridiculed for raising potentially explosive issues, and experience the tremendous stresses of isolation and career dislocation. They should be able to recover damages for these intangible harms, as well as their lost pay.

III. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010

The Dodd-Frank Act, enacted in response to the financial crisis and the revelations of unchecked risk taking by American banks, contains the most significant changes to whistleblower protections since Sarbanes-Oxley. In many respects, those protections – both substantive and procedural -- eclipse Sarbanes-Oxley, and in some cases make SOX far less relevant to employers and employees. Dodd-Frank makes crucial changes in six critical areas related to whistleblowing:

1. It amends SOX Sec. 806 to broaden the class of covered employers, guarantee the right to a jury trial, preclude mandatory pre-dispute arbitration agreements, and lengthen the statute of limitations.

2. It creates whistleblower rights and remedies for employees of consumer financial services entities.

3. It establishes a new system of bounty incentive rewards for whistleblowers who disclose to the SEC violations of a broad range of securities laws, when the SEC recovers more than $1 million from the violator.

4. It establishes new anti-retaliation provisions for whistleblowers who disclose information to the SEC about securities law violations, with a private right of action in federal court and no administrative exhaustion requirement.

---

[29] *Brandon v. Anesthesia & Pain Mngmt. Assoc., Ltd., et* al., 277 F.3d 936 (7th Cir. 2002) (*in dicta*); *Hammond v. Northland Counseling Center, Inc.*, 218 F.3d 886 (8th Cir. 2000); *Neal v. Honeywell, Inc.*, 191 F.3d 827 (7th Cir. 1999).

5. It strengthens the substantive and procedural protections for whistleblowers under the False Claims (Qui Tam) Act.

6. It creates new whistleblower protections under the Commodity Exchange Act.

The SEC will be fleshing out the requirements of Dodd-Frank when it issues its final regulations. In December, 2010, the agency issued almost two hundred pages of proposed regulations, and has received the public's comments. See http://www.sec.gov/rules/proposed/2010/34-63237.pdf; 17 CFR Part 240 and 249, Release No. 34-63237. Although the SEC was supposed to issue final regulations at the end of April, it missed the deadline and those are still pending.

A. Dodd-Frank's changes to SOX Sec. 806

1. Covered employers include certain subsidiaries and statistical rating agencies

Dodd-Frank finally settles the question of whether a publicly traded company's wholly-owned subsidiaries are covered employers under SOX Sec. 806; Dodd-Frank states that they are. Under Dodd-Frank Sec. 929A, "covered employers" now include "any subsidiary or affiliate whose financial information is included in the consolidated financial statements of such company.''

The change is extremely significant, because prior to the amendment, many employees had seen their SOX cases dismissed on the ground that their employer was a subsidiary of a publicly traded company, rather than the parent. To avoid dismissal, employees in many cases had argued that the parent company was sufficiently involved in the termination decision and in the subsidiary's Human Resources functions, so as to require a finding of agency. These fact-intensive arguments are now unnecessary.

Dodd-Frank also expands the class of covered employees to include employees of a "nationally recognized statistical rating organization," as defined in section 3(a) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a). [30] Moody's and Standard & Poor's are such agencies.

[30] 15 U.S.C. 78c(a)(1)(62) defines a nationally recognized statistical rating organization as a credit rating agency that—

(A) has been in business as a credit rating agency for at least the 3 consecutive years immediately preceding the date of its application for registration under section 78o–7 of this title;

2. Jury trial

Dodd-Frank amends SOX to provide that parties in SOX proceedings in federal court have the right to a jury trial. Dodd-Frank Sec. 922(c)(1)(B). Courts had issued conflicting decisions on this question.

3. No mandatory pre-dispute arbitration

Dodd-Frank prohibits employers from enforcing mandatory pre-dispute agreements which require arbitration of a claim under SOX Sec. 806. Dodd-Frank Sec. 922(c)(2). One recent case holds that this provision applies retroactively to conduct occurring before Dodd-Frank became effective. (In general, the statute is effective on July 22, 2010, the day after it was signed by President, although a good number of non-whistleblower provisions take effect over several years.) *Pezza v. Investors Capital Corp.*, 2011 U.S. Dist. LEXIS 20035 (D. Ma. March 1, 2011).

4. Lengthened statute of limitations for filing a charge at DOL

SOX Sec. 806 originally contained an unusually short statute of limitations -- 90 days. The Department of Labor's policy did not allow the parties to toll the limitations period. Dodd-Frank extends the limitations period to 180 days. Sec. 922(c)(1)(A).

B. Whistleblower protections for employees of consumer financial services organizations - Dodd-Frank Title X

Dodd-Frank establishes a new set of whistleblower protections for employees of

---

(B) issues credit ratings certified by qualified institutional buyers, in accordance with section 78o–7 (a)(1)(B)(ix) of this title, with respect to—

(i) financial institutions, brokers, or dealers;
(ii) insurance companies;
(iii) corporate issuers;
(iv) issuers of asset-backed securities (as that term is defined in section 1101(c) of part 229 of title 17, Code of Federal Regulations, as in effect on September 29, 2006);
(v) issuers of government securities, municipal securities, or securities issued by a foreign government; or
(vi) a combination of one or more categories of obligors described in any of clauses (i) through (v); and

(C) is registered under section 78o–7 of this title.

organizations that provide financial services to consumers.   The protections cover both internal and external complaints.

The whistleblower protections are far broader than those of SOX 806, because they are not limited to employees of publicly-traded companies, but extend to all employees of entities involved in the provision of consumer financial services – which the statute defines expansively. Protected whistleblowing activity is defined more broadly than it is under SOX.   The enforcement mechanism is somewhat similar to that under SOX: aggrieved employees must first file a complaint with the Department of Labor, but can then remove the case to federal district court if DOL does not issue a final order within the statutory time limits.

1. What employees are covered

A "covered employee" is "any individual performing tasks related to the offering or provision of a consumer financial product or service."   Sec. 1057(b).

A consumer financial product or service has an expansive definition. It includes extending credit, brokering loans, providing certain real estate settlement services or property appraisals, taking deposits or acting as a custodian for a consumer, providing payments or financial data processing services to a consumer, providing consumers with financial advisory services, debt management services or credit counseling services, and collecting and distributing credit or other financial information concerning consumers which will be used in the decision to offer a consumer a financial product or service. The new Bureau of Consumer Financial Protection has the authority to include additional activities in the definition.   Sec. 1002(5).   www.consumerfinance.gov.

2. What is protected activity: internal and external complaints - Sec. 1057(a)

A covered employer or service provider is prohibited from terminating or otherwise discriminating against a covered employee (or the employee's representative) because the employee or his representative:

(1) provided, caused to be provided, or is about to provide or cause to be provided, information to the employer, the Bureau of Consumer Financial Protection, or any other State, local, or Federal, government authority or law enforcement agency, relating to any act or omission that the employee reasonably believes is a violation of any provision Title X of Dodd-Frank (the Consumer Protection Act of 2010), or any other provision of law that is subject to the jurisdiction of the Bureau, or any rule, order, standard, or prohibition prescribed by the Bureau;

(2) testified or will testify in any proceeding resulting from the administration or enforcement of any provision of Title X, or any other provision of law that is subject to the jurisdiction of the Bureau, or any rule, order, standard, or prohibition prescribed by the Bureau;

(3) filed, instituted, or caused to be filed or instituted any proceeding under any Federal consumer financial law; or

(4) objected to, or refused to participate in, any activity, policy, practice, or assigned task that the employee (or other such person) reasonably believed to be in violation of any law, rule, order, standard, or prohibition, subject to the jurisdiction of, or enforceable by, the Bureau.

These listed protected activities go beyond those in SOX. Some cases under SOX Sec. 806 had ruled that merely refusing to participate in unlawful activity did constitute protected activity. Such an objection does constitute whistleblowing under Dodd-Frank Title X.

3. Enforcement - Sec. 1057(c)

a. The charge and DOL investigation

The employee has to file a charge with the Department of Labor, within 180 days after the alleged violation. The Secretary of Labor notifies the alleged violator of the charge and the substance of the supporting evidence, and must give the employer the opportunity to file a written response. Within 60 days after the charge was filed, DOL must initiate an investigation and determine if there is “probable cause” to believe the employer committed a violation.

If DOL finds probable cause, it must order preliminary relief, which can include reinstatement and back pay.

b. Administrative hearing

Either party may object to DOL’s order within 30 days, and request a hearing. However, the request for a hearing does not stay an order of reinstatement.

DOL must issue a final order within 120 days after the hearing concludes.

c. Available relief – 1057(c)(4)(B)

DOL "shall" award a prevailing employee back pay, undefined "compensatory damages" and attorney's fees and expert witness costs.

If DOL finds the employee brought a frivolous claim, it can award $1,000 to the employer.

The Secretary of Labor has authority to seek judicial enforcement of a DOL order, and the court can award injunctive relief and compensatory damages. The employee on whose behalf DOL issued a final order can also sue in district court to compel the employer to comply with the order. 1057(c)(5).

d. Judicial actions - 1057(c)(4)(D)

The employee can bring an action de novo in federal court, if DOL has not issued a final order within 210 days after the employee filed the complaint, or within 120 days after DOL's preliminary determination. Either party has the right to have a jury trial. The court may award a prevailing employee back pay, compensatory damages, reasonable attorney's fees and costs.

e. Unless the employee has brought a judicial action, either party can seek review of the Secretary's order by the Court of Appeals in the Circuit where the employee lived at the time of the alleged violation, within sixty days of the order. 1057(c)(4)(E).

f. Waiver and arbitration – 1057(d)

Employees cannot waive their rights under 1057, and any pre-dispute agreement to arbitrate such a claim is invalid. The bar on arbitration does not apply to an arbitration clause in a collective bargaining agreement, unless DOL determines by rule that the arbitration clause is "inconsistent with the purposes of this title."

4. Burdens of proof – 1057(c)(3)

In its preliminary determination, DOL is required to dismiss a charge unless the employee proves, as its prima facie case, that the protected activity was a "contributing factor" in the adverse decision. The investigation is not to be conducted if the employer rebuts the prima facie case by demonstrating that it would have taken the same action in the absence of the protected activity. These same burdens of proof apply to DOL's final determination.

C. Dodd-Frank's whistleblower bounty incentive for disclosures to the SEC - Sec. 922

Sec. 922 of Dodd-Frank establishes powerful financial incentives for whistleblowers to report fraud to the SEC, somewhat similar to those under the federal False Claims (qui tam) Act. It provides that whistleblowers who voluntarily provide original information to the SEC relating to the violation of securities laws, which lead to a recovery greater than $1 million in an administrative or judicial enforcement action, may receive ten to thirty per cent of the recovery. The new provisions are amendments to the Securities Exchange Act of 1934, 15 U.S.C. 78a et seq, and create a new section of the Act, Sec. 21E. The bounty provisions will be enforced by the SEC's new Office of the Whistleblower, headed by Sean McKessy.

1. Who is a whistleblower under Sec. 922

Any individual who voluntarily provides information to the SEC about a violation of securities laws, in the manner provided by the SEC's regulations (which have been proposed but are still pending.)

Whistleblowers may submit anonymous claims if they are represented by counsel, but before payment of an award, the whistleblower must disclose his identity. Sec. 922(d)(2).

2. What information must a whistleblower provide to be eligible for an award

a. The information must be "original information" concerning a violation of the securities laws. "Original information" is information which: i) is derived from the whistleblower's independent knowledge or analysis; ii) is not known to the SEC from another source, and iii) is not exclusively derived from an allegation made in an administrative or judicial proceeding, a government report, hearing audit or investigation, or from the news media, unless the whistleblower was the source of that information.

b. The definition of "original" information as including information derived from the whistleblower's independent *analysis* is significant, because it would permit awards to whistleblowers who provide an analysis of misconduct, rather than evidence of the misconduct itself.

3. Covered administrative or judicial actions on which a bounty award can be based

The whistleblower's information must lead to the successful enforcement of an administrative or judicial action for violation of securities laws, with a sanction of more than $1 million. Sec. 922(a)(a)(1). The action can either be brought by the SEC, Sec. 922(a)(1)(1), or be a "related action," which means an action by one of other domestic or foreign entities listed. Sec. 922(a)(a)(5); Sec. 922(h)(2)(D)(i)(I) - (IV). [31]

4. Determination of the award

A whistleblower can receive between ten and thirty per cent of the amount over $1 million which is recovered in the action. Sec. 922(b)(1). The payment appears to be mandatory ("the Commission, under regulations prescribed by the Commissions and subject to subsection (c), shall pay an award….") Sec. 922(b)(1). However the SEC has the discretion to determine the amount of the award. Sec. 922(c)(1). In determining the amount, the SEC is directed to take into consideration the significance of the information the whistleblower provided, the assistance the whistleblower provided, the SEC's interest in deterrence, and other relevant factors that the SEC establishes by rule or regulation. Sec. 922(c)(1)(b).

5. Individuals not eligible to receive a bounty award are, under Sec. 922(c)(2):

a. Whistleblowers convicted of a criminal violation related to the action.

b. Whistleblowers who obtained the information through an audit of financial statements required under the securities laws, if the submission of the information would violate 15 USC 78j-1.

c. Whistleblowers who do not submit their information in the form the Commission requires.

d. Employees, officers or members of law enforcement, regulatory or self-regulatory organizations who obtained the information while associated with the organization.

e. Individuals who knowingly and willingly make any false representations, or use a false document knowing it contains any false information. Sec. 922(i).

[31] The agencies which can bring a "related action are the "Attorney General, an appropriate regulatory authority; a self-regulatory organization; a State attorney general in connection with any criminal investigation; any appropriate State regulatory authority; the Public Company Accounting Oversight Board; a foreign securities authority; and a foreign law enforcement authority. Dodd-Frank 922(h)(2)(D)(i)(I) – (IV).

D. Dodd-Frank's new anti-retaliation protections for whistleblowers who provide information to SEC about securities law violations - Sec. 922(h)

Dodd-Frank establishes new anti-retaliation provisions for employees who provide information to the SEC about securities law violations. In contrast to SOX Sec. 806, the bar on retaliation applies to all employers, and employees who are retaliated against can sue directly in federal court.

1. Expansion of covered employers beyond SOX 806

Dodd-Frank's whistleblowing provisions cover all employers – not just the publicly traded companies covered by SOX Sec. 806. Dodd-Frank Sec. 922(h)(1).

2. Employees covered:

A "whistleblower" is "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." Sec. 922(a)(6). Note that, in contrast to SOX 806, Dodd-Frank requires an external report to the SEC, and does not appear to protect employees who make internal corporate complaints.

3. Prohibited acts – Broad definition

An employer cannot "discharge, demote, suspend, threaten, harass, directly or indirectly, or in any other manner discriminate against" a whistleblower because of the whistleblower's protected activity.

4. Protected activity

Whistleblowers are protected against retaliation for:

a. Providing information to the SEC;

b. Initiating, testifying in, or assisting in any investigation or judicial or administrative action of the SEC which is based on that information; or

c. Making a disclosure required by the Sarbanes-Oxley Act, the Securities Exchange Act of 1934, 18 USC 1513(e) (which criminalizes harmful actions taken against individuals who provide truthful information to law enforcement authorities about any violation or possible of federal law), or any law, rule or regulation subject to the SEC's jurisdiction.

5. Enforcement: Private right of action in federal court

In contrast to SOX and Dodd-Frank's enforcement scheme for employees of entities providing consumer financial services, whistleblowers under 922(h) can sue directly in federal court, without first initiating an administrative proceeding. Sec. 922(h)(1)(B).

a. Available relief

A prevailing plaintiff "shall" be awarded reinstatement with the same seniority the plaintiff would have had but for the discrimination, double back pay with interest, and reasonable attorney's fees, litigation costs and expert witness fees. Sec. 922(h)(1)(C).

922(h) does not provide for damages for emotional distress or punitive damages.

b. Statute of limitations

The limitations period under 922(h) is far longer than that under SOX or under Dodd-Frank's protections for whistleblowers working in consumer financial services. The employee has six years from the date of the violation, or three years from when the employee knew or reasonably should have known the facts material to the claim, but no later than ten years after the date of the violation. Sec. 922(h)(1)(B)(iii).

c. No pre-emption

Whistleblowers can bring an action under 922(h) without losing or impairing their rights and remedies under any other law, or a collective bargaining agreement. Sec. 922(h)(3)

d. Bad actors can't recover: 922(i)

Whistleblowers may not recover damages for retaliation if they knowingly and willfully make a false or fraudulent representation, or use a document knowing it contains such information.

E. Dodd-Frank's anti-retaliation provisions and bounty incentives for Whistleblowers under the Commodity Exchange Act -- Sec. 748

Dodd-Frank establishes whistleblower protections and a bounty incentive program under the Commodity Exchange Act. These provisions track the protections, procedures, remedies and awards for individuals who provide information to the SEC about securities law violations. Sec. 748. The statute provides financial incentives for reports to the Commodity Futures Trading Commission (CFTC), and bars retaliation against an individual who provides that information or assists the CFTC in an investigation. Plaintiffs may sue directly in federal court, within two years of a retaliatory act.

F. Dodd-Frank's expansion of protections under the False Claims (qui tam) Act: Associated persons protected; limitations period defined.

Dodd-Frank expands the class of individuals who are protected from retaliation under the False Claims (qui tam) Act. The False Claims Act prohibits fraud on the government (31 U.S.C. 3729) and retaliation against individuals who make internal and external complaints about false claims (31 U.S.C. 3730(h)). Under Dodd-Frank Sec. 1979A, employers are now prohibited from retaliating against individuals who are associated with a qui tam whistleblower because of the whistleblower's protected activity.

Dodd-Frank also resolves the question of what statute of limitations governs retaliation claims under the False Claims Act. Courts had held that the limitations period was that of the most closely analogous state statute, with varying results. See, e.g., *United States ex rel McKenna v. Senior Life Management, Inc*. 29 F. Supp. 2d 695 (S.D.N.Y. 2006). Dodd-Frank sets a uniform limitations period of three years from the date of the retaliatory act. One case holds that the change in the limitations period is not retroactive. *Riddle v. Dyncorp. International Inc.*, 733 F.Supp 743 (S.D. TX 2010), mot. for reconsideration denied, 2011 U.S. Dist. LEXIS 3958 (January 14, 2011).

IV. The American Recovery and Reinvestment Act of 2009 (ARRA)

The 2009 federal bail-out legislation, the American Recovery and Reinvestment Act, included sweeping protections for whistleblowers who complain about the misuse of bailout funds. P.L. 111-5, 123 Stat. 115, Sec. 1553. The protections, remedies and enforcement mechanisms provided by Sec. 1553 are unusually strong, although they have yet to be tested in litigation. As part of the ARRA, Congress corrected some of the weaknesses which are present in SOX 806.

However, many recipients of the bailout funds have repaid the government, and it is not clear from the statute whether the whistleblower protections continue to apply once the funds are no longer with the recipient. So, how relevant ARRA will be to whistleblowers is an open question.

A. Covered employers:

Employers covered Sec. 1553 are non-federal employers which receive “covered funds.” 1553(a); 1553(g). Covered funds are defined as any contract or payment for which the federal government provides part of the payment or property, as long as some of the funds are authorized by the ARRA. Sec. 1553(g)(2).

1. Non-federal employers include contractors, subcontractors, grantees or recipients of covered funds, if the entity is an employer; professional membership organizations; certification or other professional bodies; any agent or licensee of the federal government; and, significantly, *“any person acting directly or indirectly in the interest of an employer receiving federal funds.”* Sec. 1553(g)(4).

   If the funds are received by a state or local government, Sec. 1553 covers the government as well as its agents, contractors and subcontractors. Sec. 1553(g)(4)(a)(ii).

2. Federal agencies or departments, or other federal agencies, are not employers under the Act. Sec. 1553(g)(4)(B).

B. Covered employees

An employee is protected by the Act if the employee is “an individual performing services on behalf of an employer.” Sec. 1553(g)(3)(A). The breadth of this phrase would indicate that independent contractors are also protected. Federal employees and members of the armed forces are not included. Sec. 1553(g)(3)(B).

C. Prohibited employer conduct – Sec. 1553(a)

1. Employers are barred from discharging, demoting or otherwise discriminating against an employee as a reprisal for the employee making a disclosure to:

   The Recovery Accountability and Transparency Board
   The Inspector General
   The Controller General
   A member of Congress

   A state or federal regulatory or law enforcement agency
   A person with supervisory authority over the employee
   A person working for the employer who has authority to investigate or terminate misconduct
   A court or a grand jury
   The head of a federal agency or
   Their representatives.

2. The employee is protected for complaining about what he reasonably believes is evidence of:

   "Gross mismanagement" of an agency contract or grant relating to covered funds

   A gross waste of covered funds

   A serious and substantial danger to public health and safety related to the use or implementation of the covered funds

   An abuse of authority related to the use or implementation of the covered funds. An abuse of authority means "an arbitrary and capricious exercise of authority by a contracting official or employee that adversely affects the rights of any person, or that results in personal gain or advantage to the official or employee or to preferred other persons." Sec. 1553(g)(1).

   A violation of a law, rule or regulation related to an agency contract or grant, awarded or issued relating to covered funds.

D. Procedure

1. Administrative investigation:

   The employee must first complain to the Inspector General of the agency awarding the contract or grant. Unless the IG believes the complaint is frivolous, or the subject of another proceeding, the IG must investigate the complaint. The IG then submits a report to the complainant, the employer, the agency and the Board. Sec. 1553(b)(1). The IG must make its determination regarding whether to investigate, and complete its investigation, within 180 days after the complaint is filed. Sec. 1553(b)(2)(A). This time period can be extended with the complainant's consent. Sec. 1553(b)(2)(B)(i).

   Access to files: The complainant must be allowed access to the IG's file in accordance with the federal Privacy Act, 5 U.S.C. 552a, with certain limited exceptions. Sec. 1553(b)(4).

2. Subsequent action by the agency - Sec. 1553(c)(2):

   Within 30 days of receiving the IG's report, the head of the agency receiving covered funds must decide whether the employer engaged in a reprisal, and must either grant or deny the employee relief under Sec. 1553, or order the employer to:

   Take affirmative action to "abate" the violation

   Reinstate the employee, with all retroactive pay and benefits, as well as undefined "compensatory damages"

   and/or

   Pay the employee for all reasonable attorneys fees and costs.

   Unlike SOX Sec. 806, there is no administrative hearing.

3. Judicial enforcement of agency orders – Sec. 1553(c)(4):

   If the employer does not comply with the order, the head of the agency can seek to enforce it in federal court, and obtain injunctive relief, compensatory and exemplary damages, and attorney's fees.

4. Appeals: Any party may appeal a decision of the agency to the Court of Appeals, under the Administrative Procedure Act, within sixty days. Sec. 1553(c)(5).

5. Federal court actions – Sec. 1553(c)(3):

   The employee can bring a de novo action in federal court if the head of the agency denies the employee's request for relief in whole or in part, or doesn't issue an order on the merits within 210 days after the employee filed the complaint (or within 30 days after an agreed-upon extension of time has expired), or has declined to investigate the complaint.

   The administrative remedies will not be deemed exhausted for an employee whose bad faith caused the delay.

   Jurisdiction over the action is in the "appropriate" federal district court.

   Either plaintiff or defendant may request a jury trial.

   The plaintiff may seek "compensatory damages and other relief available under this section," which, as described above, includes back pay, exemplary damages, attorney's fees and costs. See Sec. 1553 (c) (3), which also refers to 1553(c)(2). In contrast, the text of SOX Sec. 806 does not authorize compensatory damages.

E. Burden of proof – Sec. 1553(c)(1):

The employee only has to show that his protected activity was a "contributing factor" in the employer's "reprisal." The employee can demonstrate this through circumstantial evidence, which can include either the employer's knowledge of the employee's protected activity, or a temporal relationship between the protected activity and the reprisal.

The employer can rebut this showing by demonstrating that it would have taken the same action in the absence of the employee's protected activity – but it must prove this by "clear and convincing" evidence.

F. Unusual aspects of Sec. 1553

There is no stated statute of limitations in the ARRA, nor is there a reference to any analogous limitations period. This is with respect to both complaints filed with the Inspector General, and actions filed in federal court. For employees, this is a great improvement over SOX Sec. 806, which now has a 180 day limitations period for filing a charge with the Department of Labor. In the absence of a stated limitations period, the four year catch-all provision of 28 U.S.C. 1658(a) may apply. That provision states that "Except as otherwise provided by law, a civil action arising under an Act of Congress enacted after the date of the enactment of this section may not be commenced later than 4 years after the cause of action accrues."

Sec. 1553 bars the waiver of the rights and remedies it provides, including a waiver in a pre-dispute arbitration agreement, and it states that a pre-dispute arbitration agreement with such a waiver is not enforceable. However, a collective bargaining agreement with such a waiver may be enforced with respect to disputes arising under the CBA. Sec. 1553(d).

Sec. 1553 does not pre-empt or limit any other provision of State law providing protections to whistleblowers. Sec. 1553(f)(2).

Employees are explicitly protected for making disclosures in the ordinary course of their duties. Sec. 1553(a). In contrast, in SOX cases, some courts have precluded employees from invoking whistleblower protection because the employee was investigating fraud as part of the employee's normal responsibilities.

G. Likely litigation questions:

Sec. 1553 is rife with unanswered questions for litigants and the courts. Among them:

1. What are the compensatory damages an employee can recover? Do they include emotional distress damages, damage to reputation, or merely out of pocket expenses?

2. What is the "gross mismanagement" of an agency contract or grant relating to covered funds, which can be a predicate for a complaint protected by Sec. 1553? Does it extend to gross

mismanagement of the employer’s business which receives the covered funds? How incompetent does gross mismanagement have to be?

3. Similarly, what constitutes a “gross waste” of covered funds?

4. How much must the public be endangered before a “serious and substantial danger to public health and safety” occurs, which is related to the use or implementation of covered funds?

5.   Is there any statute of limitations on either administrative filings or judicial actions, and what is it? Does the four year catch-all provision of 28 U.S.C. 1658(a) apply?