

## **Review of Recent Whistleblower Developments: October 2022**

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### **First Circuit Denies Extension of SOX Anti-Retaliation Protection to Federal Statutes within the Enforcement Power of the SEC**

In [\*Baker v. Smith & Wesson, Inc., No. 21-2019, 40 F.4th 43 \(1st Cir. 2022\)\*](#), the First Circuit refused to extend SOX's anti-retaliation protection to a whistleblower's claim involving violation of "statutes within the enforcement power of the SEC." The plaintiff, a former employee of Smith & Wesson (S&W), reported certain illegal conduct by S&W employees that he believed violated a provision of the Foreign Corrupt Practices Act addressing accounting practices and internal controls. Section 1514A of SOX limits whistleblower anti-retaliation protection to claims about certain statutes relating to fraud as well as "any rule or regulation of the Securities and Exchange Commission." The plaintiff asserted the statute's protections extend beyond SEC "rules and regulations" to "statutes within the enforcement power of the SEC." The court disagreed. First, the court found the plain text of Section 1514A "does not include federal statutes, such as the FCPA." Second, the court observed that "any rule or regulation of the [SEC]" cannot extend to federal statutes "because the SEC does not have the authority to enact statutes." Finally, the court identified that elsewhere in Section 1514A Congress specifically cited to particular federal statutes, none of which include the FCPA statute at issue. The court reversed the district court's denial of summary judgment to S&W and remanded with instructions to enter summary judgment in favor of S&W.

### **Second Circuit Requires Showing of "Retaliatory Intent" under SOX Anti-Retaliation Provision**

In [\*Murray v. UBS Securities, LLC, No. 20-4202 \(2d Cir. 2022\)\*](#), the Second Circuit held that Section 1514A of SOX requires that an anti-retaliation claim requires a showing of the employer's retaliatory intent by a preponderance of the evidence. Specifically, such intent is the intent to "discriminate against an employee ... because of" lawful whistleblowing activity. The plaintiff, a former strategist in

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UBS Securities' commercial mortgage-backed securities business, alleged two of his superiors "improperly pressured him to skew his research," and he was thereafter terminated in retaliation for reporting this conduct to his direct supervisor. At trial, the district court did not instruct the jury that the plaintiff must prove retaliatory intent and rejected UBS's objection to this omission. The Second Circuit agreed with UBS that the instruction about retaliatory intent should have been given to the jury. The court found the plain meaning of Section 1514A requires a showing of retaliatory intent based on the statute's terms: to "*discriminate* against an employee ... *because of*" whistleblowing. Per the court, to "discriminate" requires a "conscious decision to act," and "because of" means "by reason of" or "motivated by." The court found this translates to a showing of retaliatory intent. The court further observed that its interpretation of Section 1514A to require such a showing is consistent with its interpretation of the similarly worded Federal Railroad Safety Act, 49 U.S.C. § 20109(a). The Second Circuit vacated the jury's verdict and remanded for a new trial.

## **Second Circuit Requires an SEC Covered Action as Prerequisite to Award for Related Actions**

In [\*Hong v. S.E.C., No. 21-529, 41 F.4th 83 \(2d Cir. 2022\)\*](#), the Second Circuit denied plaintiff's petition for review from the SEC's denial of a whistleblower award. The plaintiff had applied for an award after submitting a Tip, Complaint or Referral (TCR) form to the SEC about his former employer's possible securities law violations. The Federal Housing Finance Agency and Department of Justice, each of which were investigating plaintiff's former employer, learned about the plaintiff's tip and met with the plaintiff. While the FHFA and the DOJ entered into settlements with the former employer, the SEC never brought an enforcement action and never contacted the plaintiff about his tips. In denying the plaintiff's request for a whistleblower award, the SEC found the FHFA and DOJ actions were not covered actions — that is, actions "brought by the [SEC] under the securities laws," as is required under Section 21F of the SEC Whistleblower Program rules. The SEC also rejected the plaintiff's argument that the other agencies' actions constituted related actions because there was no covered action. Because the FHFA's and DOJ's actions were not "covered judicial or administrative action[s]" under Section 21F, and because the SEC did not itself bring a covered action, the other agencies' actions could not constitute "related actions." The Second Circuit agreed and denied the plaintiff's petition for review.

## **SEC Adopts Amendments to Whistleblower Rules Providing Additional Incentives to Whistleblowers for Non-SEC Actions and Limiting the SEC's Ability to Decrease the Size of Awards**

On August 26, 2022, the SEC [adopted](#) two amendments to the whistleblower program rules proposed earlier this year. The first amendment (to Rule 21F-3) allows the SEC to make awards to whistleblowers for related, non-SEC actions that might otherwise be covered by another agency's whistleblower program, even where that other program has the more direct or relevant connection to the related action. In the [Final Rule](#), the SEC commented that the amendment will incentivize whistleblowers "to report potential violations of the federal securities laws when another program has a statutory cap, significantly lower award range, or discretionary award structure." The second amendment (to Rule 21F-6) affirms the SEC's authority to consider the size of a potential award as a grounds for changing the award's amount but limits any such change to an increase in the award. Under the amendment, the SEC cannot decrease an award on these grounds. According to SEC Chair Gary Gensler, these two amendments are meant to "strengthen [the] whistleblower program" and to better "protect investors." At the same time, in the Final Rule, the SEC posited the impact of the amendments "is expected to be small" but acknowledged the changes could increase both

award amounts and the number of tips received. With over \$1.3 billion awarded to 278 individuals since the program's inception in 2012 — nearly half of which was awarded in 2021 alone — even a “small” impact could have major implications for potential whistleblowers and their attorneys going forward.

## **SEC Awards Approximately \$40 Million to Whistleblowers in Q3 2022**

On July 15, 2022, the SEC [awarded](#) more than \$6 million to two whistleblowers who provided critical information and assistance in two separate covered actions. The first award was over \$3 million to a whistleblower who was solicited to invest in a product they believed was being misrepresented. The whistleblower promptly alerted the SEC and continued working with the staff after the SEC opened an investigation. The second award was also over \$3 million to a whistleblower who first reported concerns internally, then later submitted a tip to the SEC. The whistleblower also met with the SEC multiple times to provide additional information throughout the investigation.

On July 19, 2022, the SEC [awarded](#) more than \$17 million to a single whistleblower who prompted the opening of the investigation that led to a successful covered action. The whistleblower also provided the staff with detailed information and documents, which further led to the success of a related action. As a result, the SEC stated that the whistleblower was also entitled to an award based on amounts collected in the related action.

On August 9, 2022, the SEC [awarded](#) more than \$16 million to two whistleblowers who provided information and assistance in a successful SEC enforcement action. The first whistleblower was awarded about \$13 million. They prompted the opening of the investigation and provided information on difficult-to-detect violations as well as identified key witnesses and provided critical information to the staff. A second whistleblower was awarded more than \$3 million for submitting important new information during the course of the investigation.

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National Law Review, Volumess XII, Number 298

Source URL: <https://natlawreview.com/article/review-recent-whistleblower-developments-october-2022>