2nd Circ. Could Resurrect Zombie SEC Whistleblowers
By Ed Beeson

New York (September 26, 2014, 7:25 PM ET) -- The U.S. Securities and Exchange Commission will go before the Second Circuit on Monday seeking to convince three judges it was right to limit access to its whistleblower program. If it fails, the agency could be forced to pay bounties to a host of tipsters who came to it before the Dodd-Frank Act was passed.

The New York federal appeals court is set to hear arguments from Larry Stryker, a whistleblower whose award claim was denied by the SEC because he tipped the agency before the July 21, 2010, enactment of the Dodd-Frank Act.

If the circuit panel were to find for him, it would open the floodgates to claims from other whistleblowers whose pre-Dodd-Frank tips led to big enforcement actions but personally gained them nothing, said Steven Pearlman, partner at Proskauer Rose LLP and co-head of its whistleblowing and retaliation group.

“The question is, where do you draw the line?” he said. At the very least, he said, such a decision would threaten to drain the account the SEC set up to pay out whistleblower awards.

According to an SEC document filed with the court, Stryker for years fed information to the agency that eventually led to a June 2010 enforcement action against Advanced Technologies Group Ltd. and two of its executives and netted a $24 million settlement.

Soon afterward, Stryker filed a claim for a whistleblower award, but the SEC denied him on the grounds his tips did not meet the definition of “original information” because they were provided before Dodd-Frank was enacted.

The law, among other things, required the SEC to set up a whistleblower program and pay those who provide it original information leading to an enforcement action where sanctions total more than $1 million. But Stryker, who would stand to collect between 10 and 30 percent of the penalties in his case, contends the SEC went beyond its congressional mandate when it put a start date on when successful tips would be eligible for awards, which wasn't explicitly called for by the Dodd-Frank Act.

“The plain text, structure, and legislative history of the act are all unambiguously clear” about when a whistleblower is and is not eligible for an award, attorneys for Stryker wrote in a brief before the Second Circuit. “The date that a whistleblower initially submits ‘original’ information to the SEC is not part of the statutory definition of original information, and it has no bearing whatsoever on whether he is eligible to receive an award.”

The commission fired back, saying the statutory language shows Congress had intended for the program to be limited to present-day tipsters and not those who pre-dated Dodd-Frank. Additionally, the agency added, where there is ambiguity, deference should be given to the SEC, per the U.S. Supreme Court in Chevron USA v. Natural Resources Defense Council Inc.

An SEC spokeswoman declined to comment on the case, and an attorney for Stryker did not return a message seeking comment.

Attorneys say while it is understandable Stryker would press hard for an award — particularly as another individual was recently awarded a bounty worth at least $30 million — he faces an uphill climb convincing the court to move against the SEC.

“Unfortunately, the odds are long for the whistleblower in this case because courts typically give deference to the SEC on these type of matters, especially where the applicable statute doesn’t expressly authorize the retroactive application of the law,” said Jordan Thomas, chair of Labaton Sucharow LLP’s whistleblower representation practice.

Even if there is a real question about whether the statute provided room for a start date for the rewards program, an overriding issue for the courts may be that there is no limiting principle within Stryker’s appeal, attorneys say.

Nonetheless, Pearlman expects the appellate court will give Stryker’s argument its full attention. “This is an issue of first impression," he said. "The Second Circuit is going to roll up its sleeves."

A big argument will be over whether the SEC is entitled to what’s known as Chevron deference.

Stryker contends that the agency is not. He argues that while the SEC has said it is entitled to Chevron deference to interpret one aspect of its whistleblower rules — the definition of whistleblower status — this is not the provision under which the agency denied his claim in the first place, which was the definition of original information.

“The creative argument put forth by the commission’s appellate counsel is not entitled to any Chevron deference whatsoever, and cannot now form the basis for denying Mr. Stryker’s claim,” attorneys for Stryker wrote.

Instead, Stryker's attorneys argue that lawmakers’ actions in drafting the whistleblower statute, including modeling it after the “best practices” of the Internal Revenue Service’s own whistleblower program, show Congress’ intent not to time-bar certain whistleblower claims.

“Significantly, Congress did not include the timing-disqualification contained in the IRS law in the Dodd-Frank Act’s whistleblower law,” Stryker’s attorneys wrote. “This deliberate omission is clear evidence that Congress did not intend to disqualify Dodd-Frank Act whistleblowers on the basis of when they provided information to the SEC and also did not consider such a disqualification a ‘best practice.’”

Pearlman, however, said he was struck by the extensiveness of the SEC’s response to Stryker’s claims. “They might be wanting to send the message that they take any challenge to their program very seriously," he said.

Stryker is represented by Stephen M. Kohn, Michael D. Kohn and David K. Colapinto of Kohn Kohn & Colapinto LLP and Karim Kamal of the Law Office of Karim H. Kamal.

The SEC is represented by Anne K. Small, Michael A. Conley, John W. Avery, William K. Shirey and Stephen G. Yoder.

The case is Stryker v. Securities and Exchange Commission, case number 13-4404, in the U.S. Court of Appeals for the Second Circuit.