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CA District Court: Insurance Policy Covering Securities Claims May Extend to SOX Whistleblower Claims

Proskauer Whistleblower Defense on **August 30, 2023**

A recent California district court addressed the question of whether, for insurance coverage purposes, a SOX whistleblower claim is a "securities claim," and answered that question in the affirmative. *Skye Bioscience v. PartnerRe Ireland Insurance DAC*, No. 23-cv-01218.

Section 1514A of SOX provides a cause of action for employees who face alleged retaliation because of certain lawful whistleblowing activity. 18 U.S.C. § 1514A(a). Section 1514A differs from other provisions in SOX in that the elements of a SOX whistleblower retaliation claim focus on the employment relationship. Section 1514A provides for traditional employment remedies such as reinstatement and backpay, and it is administered by the Occupational Safety and Health Administration (OSHA) instead of the Securities and Exchange Commission (SEC).

These aspects of Section 1514A have led insurers to conclude that insurance coverage for securities claims does not extend to SOX whistleblower claims. For example, some insurers have assumed that liability arising from an employee termination should be covered by a company's Employment Practices Liability (EPL) insurance instead of a Directors, Officers, and Company Liability (D&O) insurance which ordinarily covers losses from securities claims. *See, e.g.*, *In re Verizon Ins. Coverage Appeals*, 222 A.3d 566, 574 (Del. 2019) (narrowly interpreting similar policy language to only cover claims which are specifically relating to securities); *Kollman v. Nat'l Union Fire Ins. Co.*, 2007 WL 2344825, at *3 (D. Or. Aug. 13, 2007), *aff'd*, 542 F. App'x 649 (9th Cir. 2013) (breach of contract claim involving securities transactions was not covered under policy for securities claims).

The *Skye Bioscience* decision may cause insurers to reconsider this assumption.

Background

Skye Bioscience, Inc. was sued by a former employee who alleged that the company terminated her after she reported alleged securities law violations, in violation of the SOX whistleblower protections. Skye then sought coverage from its insurer PartnerRe Ireland Insurance DAC under a D&O policy that covered "Securities Claim[s]," which was defined to include violations of the Securities Act of 1933, the Securities Exchange Act of 1934, related rules or regulations and "similar securities laws or regulations . . . arising out of . . . the ownership, purchase, sale or distribution of or offer to purchase, sell, or distribute any securities of the Company."

Adopting the arguments advanced by insurers and courts described above, PartnerRe denied coverage on the basis that a wrongful termination claim, even if under SOX, did not fall within the meaning of "Securities Claim" under the applicable policy. Skye countered that the former employee's whistleblower retaliation claim arose from SOX, which Congress expressly defined as a "securities law."

Ruling

Applying New York law, the court denied PartnerRe's motion to dismiss, holding that Skye plausibly alleged that the whistleblower lawsuit was covered by the policy. The court agreed with Skye that SOX is a "securities law," and, in any event, that Section 1514A of SOX is "similar" to the Securities and Exchange Act of 1934 given the clear similarities between the language in Section 1514A of SOX and Section 78u-(6)(h) of the Exchange Act.

The court rejected PartnerRe's argument that interpreting the D&O policy to extend to SOX whistleblower retaliation claims would effectively convert the D&O coverage into EPL insurance, explaining that "a claim under § 1514A is a specific kind of employee action that is uniquely tied to securities laws and regulations."

Implications

This decision suggests that, at least in the insurance coverage context, SOX's whistleblower provision can be viewed as a securities law (and thus come within insurance coverage for such claims). As this is a departure from earlier decisions, this case may be an outlier.

Notably, the analysis in this case differs from that increasingly adopted in cases analyzing whether a SOX whistleblower claim is domestic or extraterritorial in nature. The trend there is for courts to conclude that a SOX whistleblower claim focuses on "*regulating employment relationships*." *See, e.g.*, *Garvey v. Admin. Rev. Bd., United States Dep't of Lab.*, 56 F.4th 110, 127-28 (D.C. Cir. 2022) (emphasis in original). And on that basis, courts then focus domestic versus extraterritorial inquiry on the site of employment, rather than on the location of alleged underlying securities law violations (or their effects).

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