SIMPSON THACHER
REPORT FROM WASHINGTON

To read the oral argument in *Lawson v. FMR LLC,* please click here.

The Supreme Court Holds That Employees Who Work For Contractors of Public Companies are Protected From Retaliation Under SOX for Whistleblowing

March 10, 2014

On March 4, 2014, in *Lawson v. FMR LLC*, the Supreme Court clarified the reach of whistleblower protection under the Sarbanes Oxley Act, concluding in a 6-3 opinion that employees of a public company's *private* contractors and subcontractors are covered by the federal law. The Court reversed and remanded the First Circuit's holding, and based its decision on the statutory text, the events prompting Congress to adopt SOX, and earlier legislation Congress drew upon. Significantly, the decision acknowledged that SOX provides protection beyond that offered by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, offering protection to internal whistleblowers.

BACKGROUND

The case concerned the definition of the SOX anti-retaliation protected class. The relevant statute, 18 U.S.C. § 1514A(a) states "[n]o [public] company . . . or any . . . contractor . . . of such company . . . may [retaliate] against an employee . . . because of [SOX-protected activity]." The issue before the Court was whether the whistleblower protections are limited to employees of public companies or extend as well to employees of privately held contractors and subcontractors of public companies.

The defendants were privately-held companies that, by contract, provide advisory and management services to the Fidelity family of mutual funds. The Fidelity Funds are publicly-held entities organized under the Investment Company Act of 1940. The Fidelity Funds have no employees of their own but rather are overseen by a board of trustees that rely on private companies such as the defendants to provide advisory and management services. Plaintiffs were two putative whistleblowers who were employees of the defendant advisors and managers. After plaintiffs raised concerns about the management of Fidelity Funds, one plaintiff was terminated and the other plaintiff resigned claiming a constructive discharge of their employment. Both plaintiffs filed complaints with the Occupational Safety & Health Administration of the Department of Labor alleging unlawful retaliation under the SOX whistleblower protections. Regulations issued by the OSHA—in its capacity as the agency with delegated authority to enforce such whistleblower protections—defined "employee" to include employees of private contractors and subcontractors of public companies. Before the agency issued a final decision in the administrative review process, plaintiffs filed complaints in Boston federal court.

The Report From Washington is published by the Washington, D.C. office of Simpson Thacher & Bartlett LLP.

At the district court level, the defendants moved to dismiss the complaints, arguing that the SOX whistleblower protections cover only employees of public companies. The district court disagreed, concluding that the provisions cover both employees of public companies as well as employees of private contractors and subcontractors of public companies. To protect against the potentially sweeping scope of his interpretation, the district court imposed a limitation (not found in the express text of the statute) that the employees must be reporting violations relating to fraud against shareholders. The defendants appealed to the First Circuit.

In a 2-to-1 decision, the First Circuit reversed. The majority, while acknowledging that different readings may be given to the word "employee" in the statute, found that "the more natural reading is the one advanced by the defendants." The majority pointed to the fact that the relevant title and sub-title of the statute expressly refers to "protections for employees of publicly traded companies." The majority also worried that plaintiffs' position "creates anomalies and provides very broad coverage." The majority concluded: "If we are wrong and Congress intended the term 'employee' … to have a broader meaning than the one we have arrived at, it can amend the statute."

In dissent, Judge Thompson embraced the interpretation advocated by plaintiffs: "Because my colleagues impose an unwarranted restriction on the intentionally broad language of the Sarbanes-Oxley Act, employ a method of statutory construction diametrically opposed to the analysis this same panel employed just weeks ago, take pains to avoid paying any heed to considered agency views to which circuit precedent compels deference, and as a result bar a significant class of potential securities-fraud whistleblowers from any legal protection, I dissent."

SUMMARY OF THE DECISION

"[a]bsent any textual qualification, we presume the operative language means what it appears to mean: A contractor may not retaliate against its own employee for engaging in protected whistle-blowing activity."

-Justice Ginsburg

Justice Ginsburg wrote the majority opinion, which was joined by Justices Breyer, Kagan and Chief Justice Roberts. The Court looked first to the language of the language means what it appears to mean: A contractor may not retaliate against its own employee for engaging in protected whistle-blowing activity." According to the Court, the same interpretation is appropriate when looking at the term "an employee" in the provision as a whole. Justice Ginsberg rejected the narrower interpretation embraced by the First Circuit and the Dissent, because under the limited definition "[c]ontractors' employees would be disarmed; they would be vulnerable to retaliation by their employers for blowing the whistle on a scheme to defraud the public company's investors, even a scheme engineered entirely by the contractor."

The Court wrote that it was common knowledge that Congress adopted the whistleblower protection as an effort to "ward off another Enron debacle." The Court explained that in 2002, Congress was "focused on the role of Enron's outside contractors in facilitating the fraud." The Court further mentioned that two of the four examples of retaliation included in the Senate Report involved outside professionals that were retaliated against by their own employers. As a result, the Court concluded it was "safe[]" to conclude that Congress enacted the provision in an attempt to "encourage whistleblowing by contractor employees who suspect fraud involving the public companies with whom they work." Further, affording protection to mutual fund investment advisors is "crucial" to SOX's mission, and therefore the Court's holding "avoids insulating the entire mutual fund industry" from receiving this protection.

Although FMR presented a slippery slope argument in favor of a less-inclusive

"[I]t would thwart Congress' dominant aim if contractors were taken off the hook for retaliating against their whistle-blowing employees, just to avoid the unlikely prospect that babysitters, nannies, gardeners, and the like will flood OSHA with § 1514A complaints."

-Justice Ginsburg

open as a result of its holding. As the Court explained, the "DOL's regulations have interpreted § 1514A as protecting contractor employees for almost a decade." In all of this time, there was not one example before the Court of an employee of a private contractor asserting a § 1514A claim based on allegations unrelated to shareholder fraud. The majority notes, "[i]f we are wrong, however, Congress can easily fix the problem" by amending the statute to remove personal employees of public company officers and employees. "But it would thwart Congress' dominant aim if contractors were taken off the hook for retaliating against their whistle-blowing employees, just to avoid the unlikely prospect that babysitters, nannies, gardeners, and the like will flood OSHA with § 1514A complaints."

The defendant argued that legislative events subsequent to Sarbanes-Oxley's enactment, such as the 2010 Dodd-Frank Wall Street Reform shows that Congress did not intend to extend § 1514A's protections to contractor employees. The majority responded that this argument "failed at the starting gate." According to the majority, "[t]he 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act does not affect this Court's task of determining whether Congress in 2002 afforded protection to whistleblowing contractor employees." The Court further clarified that Section 1514A's whistleblower protections extend to "any person with supervisory authority over the employee" in contrast to Dodd-Frank's whistleblower provision, which "focuses primarily on reporting to federal authorities."

Justices Scalia and Thomas joined the majority in principal part, but dissented in part due to the Court's reliance on legislative history. Justice Scalia wrote that congressional intent "apart from the enacted text is a fiction to begin with."

Justice Sotomayor, joined by Justices Kennedy and Alito, dissented. The dissenting justices disagreed with the majority's broad interpretation of the statute, and wrote that the statute is "deeply ambiguous" as indicated by "the statute's headings, the statutory context, and the absurd results that follow from the majority's interpretation." The dissent acknowledged that the majority's opinion serves a "laudatory purpose" but according to the dissent, the purpose is not one that tracks the statute as envisioned by Congress.

IMPLICATIONS

The recent decision defined the expansive reach of the anti-retaliation provision of SOX. Significantly, the opinion clarified that outside accountants and lawyers who report fraud and wrongdoing at publicly traded companies are protected by the statute. Ultimately, the opinion results in increased exposure for companies, as it expands the number of employees who may bring suit under the SOX whistleblower provision. As a result, many companies, particularly those that are private, may need to create or amend whistleblower compliance policies to prepare themselves for potential whistleblower claims. The opinion will have continuing application for conduct after the enactment of Dodd-Frank, and the decision does not resolve current debate as to whether employees suing under Dodd-Frank must make an external report to the SEC.

For further information about this decision, please feel free to contact:

New York City:
Nicholas S. Goldin
212-455-3685
ngoldin@stblaw.com

Joshua A. Levine
212-455-7694
jlevine@stblaw.com

Mark J. Stein
212-455-2310
mstein@stblaw.com

Washington, DC:
Peter H. Bresnan
202-636-5569
pbresnan@stblaw.com

Cheryl J. Scarboro
202-636-5529
cscarboro@stblaw.com

Peter C. Thomas
(202) 636-5535
pthomas@stblaw.com

UNITED STATES

New York
425 Lexington Avenue
New York, NY 10017
+1-212-455-2000

Houston
2 Houston Center
909 Fannin Street
Houston, TX 77010
+1-713-821-5650

Los Angeles
1999 Avenue of the Stars
Los Angeles, CA 90067
+1-310-407-7500

Palo Alto
2475 Hanover Street
Palo Alto, CA 94304
+1-650-251-5000

Washington, D.C.
1155 F Street, N.W.
Washington, D.C. 20004
+1-202-636-5500

EUROPE

London
CityPoint
One Ropemaker Street
London EC2Y 9HU
England
+44-(0)20-7275-6500

ASIA

Beijing
3919 China World Tower
1 Jian Guo Men Wai Avenue
Beijing 100004
China
+86-10-5965-2999

Hong Kong
ICBC Tower
3 Garden Road, Central
Hong Kong
+852-2514-7600

Seoul
West Tower, Mirae Asset Center 1
26 Eulji-ro 5-gil, Jung-gu
Seoul 100-210
Korea
+82-2-6030-3800

Tokyo
Ark Hills Sengokuyama Mori Tower
9-10, Roppongi 1-Chome
Minato-Ku, Tokyo 106-0032
Japan
+81-3-5562-6200

SOUTH AMERICA

São Paulo
Av. Presidente Juscelino Kubitschek, 1455
São Paulo, SP 04543-011
Brazil
+55-11-3546-1000