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The Supreme Court Extends the Sarbanes Oxley Act Whistle-Blower Protections

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On Tuesday, the U.S. Supreme Court ruled that the whistle-blower protections of Section 806 of the Sarbanes Oxley Act apply to employees of privately held companies that are contractors or subcontractors of a public company.

In *Lawson v. FMR LLC, U.S., No. 12-3, 3/4/14*, the Supreme Court reversed and remanded a February 3, 2012, decision from the U.S. Court of Appeals for the First Circuit. The First Circuit held that the plaintiffs, previous employees of a private company that provides advice and management services by contract to the Fidelity family of mutual funds, could not maintain claims of unlawful retaliation under the Sarbanes Oxley Act against their corporate employers. The First Circuit reasoned that "employees," as defined by the Sarbanes Oxley Act, did not include employees of private companies.

In reversing the First Circuit, the Supreme Court first looked at the language of the Sarbanes Oxley Act. The Act provides that "no [public] company . . . or any. . . contractor . . . may discharge . . . or discriminate against an employee" for engaging in a protected whistle-blower activity. The Court noted the definition of "employee" did not include the words "of a public company" after it. In instances where Congress has meant "an employee of a public company" in other statutes, it has said so.

Legislative history also supported the Court's holding. In passing the Sarbanes Oxley Act, Congress explicitly stated that outside professionals bear significant responsibility for reporting fraud by the public companies with whom they contract, and that fear of retaliation was the primary deterrent to such reporting. If the Court did not protect employees of private contractors, then there would be no protection of private contractor employees to ameliorate this fear and encourage reporting of financial wrongdoing.

Furthermore, if the Court read the definition of "employee" to include only those individuals who work for a public company, it would effectively insulate the entire mutual fund industry

from the whistle-blower provisions of the Sarbanes Oxley Act. The Court noted that "virtually all mutual funds are structured so that they have no employees of their own; they are managed, instead, by independent investment advisors."

Three justices dissented to this holding and warned that the ruling was overbroad and could lead to absurd results, potentially extending protection to the personal employees of company officers and employees, e.g., their housekeepers or gardeners. The majority was unpersuaded by these arguments and found them more theoretical than practical.

Bottom Line

Private contractors who provide services to public companies must be aware that their employees will be afforded protection under the Sarbanes Oxley Act whistle-blower provisions.

Practically, this requires private contractors to carefully review the complaints and concerns raised by employees relating to their public clients. This will be especially true when termination or other adverse action is considered against the employee who has engaged in whistle-blowing activity involving a public client.