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THINK SARBANES-OXLEY WHISTLEBLOWER PROTECTION DOESN'T APPLY TO YOUR COMPANY? THINK AGAIN.

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Employers who are privately held may have believed that they did not have to worry about the whistleblower protections of the Sarbanes-Oxley Act because the SOX applies to publicly held companies. But last week's Supreme Court decision in ***Lawson v. FMR***, holding that the whistleblower protections of the SOX apply to private contractors that perform work for publicly held companies, means that a lot of employers will have to get up to speed.

The Sarbanes-Oxley Act was enacted in 2002 to safeguard investors in public companies after **the collapse of Enron**.

Lawson v. FMR

Jackie Hosang Lawson and Jonathan M. Zang worked for private companies that advised or managed the Fidelity family of mutual funds. The mutual funds themselves are publicly held but have no employees. Lawson contended that she was constructively discharged after she raised concerns that expenses were being overstated. Zang alleged that he was terminated after he "rais[ed] concerns about inaccuracies in a draft" registration that was filed with the Securities and Exchange Commission.

After filing administrative complaints with the U.S. Department of Labor, Lawson and Zang sued, alleging SOX retaliation, in the U.S. District Court in Massachusetts, and their employers moved to dismiss the lawsuits for failure to state claims for which relief could be granted. The court denied the motions, but the employers appealed, and won reversal from the U.S. Court of Appeals for the First Circuit, which hears appeals from federal courts in Maine, Massachusetts, New Hampshire, Rhode Island, and the Territory of Puerto Rico. The Supreme Court reversed the First Circuit decision, which means that Lawson's and Zang's SOX claims will be allowed to proceed.

The Supreme Court Decision

The Supreme Court was called upon to interpret the language contained in Section

1514A of Sarbanes-Oxley defining who is protected by the anti-retaliation provisions:

> No [public] company . . . , or any officer, employee, contractor, subcontractor, or agent of such company, may discharge, demote, suspend, threaten, harass, or in any other manner discriminate against an employee in the terms and conditions of employment because of [whistleblowing or other protected activity].

A majority of the Court, in an opinion written by Justice Ruth Bader Ginsburg and joined by Chief Justice John Roberts and Justices Stephen Breyer and Elena Kagan (and joined in principal part by Justices Antonin Scalia and Clarence Thomas, who had a separate concurring opinion), held that this language clearly encompasses employees of private companies who perform consulting work for public employers – including outside accountants, attorneys, and others.

In construing the whistleblower protections broadly to cover employees of private contractors that perform work for public companies, the majority relied on the text of the statute, the nature of the "mischief" at Enron to which Congress was responding, and the language of earlier legislation that Congress referenced when enacting Sarbanes-Oxley. (Scalia and Thomas would have found in favor of Lawson and Zang based on the plain language of Section 1514A alone.)

According to Ginsburg's opinion, Congress included the whistleblower protections in Sarbanes-Oxley in order to head off another Enron debacle, which was facilitated by Enron's outside contractors as well as Enron's own officers. Ginsburg placed substantial weight on the legislative history of the SOX, which indicated Congress's recognition that outside professionals play a critical "gatekeeping" role in detecting and reporting fraud involving the public companies with which they contract. Ginsburg said that Congress recognized that employees of Enron contractors were primarily deterred from reporting irregularities by the fear that they would suffer retaliation if they did so.

Ginsburg's opinion also compared Section 1514A with the whistleblower protection provisions contained in the Wendell H. Ford Aviation Investment and Reform Act for the 21st Century (known as "AIR 21"), enacted two years before Sarbanes-Oxley to prohibit retaliation against those who provide information to their employers or the federal government about air carrier safety violations. AIR 21, which contains parallel statutory text and whistleblower protection schemes, has been read to protect, in addition to air carrier employees, the employees of contractors and subcontractors of the carriers.

Justice Sonia Sotomayor, in a dissenting opinion joined by Justices Samuel Alito and Anthony Kennedy, criticized the majority for giving the law a "stunning reach." In Sotomayor's opinion, Section 1514A was "deeply ambiguous," and the purpose of the Act was to "safeguard investors in *public* companies" (emphasis added).

Sotomayor said that the majority's interpretation could extend Sarbanes-Oxley whistleblower protection even to the nannies, gardeners, and other household employees of public company officers and employees. Moreover, she said, whistleblower protection could apply to *any* employee of a private business that contracted with public companies, regardless of the employee's position or job responsibilities, who reported fraud that had little or no connection to the interests of public company shareholders.

The dissent's approach touched on a significant question that remains after the *Lawson* decision: does the SOX whistleblower protection apply to contractor employees only to the extent that the whistleblowing relates to the

contractor's work *as a contractor for the public company*? Or, alternatively, does it apply to *any* whistleblowing related to the contractor company? The government took the position during oral argument that the former interpretation applied, but the text of the statute contains no such limitation. The majority ultimately declined to answer this question, emphasizing that the *Lawson* plaintiffs sought a "mainstream application" of the law (that is, they asserted claims related only to alleged retaliation for reporting activities that directly implicated the interests of the shareholders of the mutual funds).

Practical Steps That Contractors Can Take in Light of *Lawson*

Sarbanes-Oxley should now be on the radar of all private employers that do business with publicly held companies. Even though some ambiguity remains regarding the law's potential scope, companies can take affirmative steps to minimize potential exposure to whistleblower claims.

Determine which of your employees are likely to have SOX whistleblower protection. To assess whether your employees are potentially entitled to Sarbanes-Oxley protection, you should closely review your contracts and business relationships to determine what services or products are regularly supplied to publicly held companies. Employees responsible for servicing those accounts are in the best position to detect and report fraud in connection with public companies and most likely to be covered. Of course, you should err on the side of "overinclusion" and proceed as if the whistleblower protections apply, at least until the coverage issues are sorted out by the courts.

Encourage whistleblowing. If you have not already done so, you should implement measures to create a work environment that encourages employees to report suspected fraud, including fraud at public companies that the employees serve, without fear of retribution. This can be done by putting anti-retaliation policies in place, conducting appropriate training, and following through appropriately on fraud reports.

Revise your no-retaliation policy. Be sure to implement anti-retaliation policies that are broad enough to include protection for the various types of fraud reports protected by Sarbanes-Oxley. Such policies should clearly define the types of fraud that should be reported, including shareholder fraud at public companies for which you provide services, provide instructions on how to report suspected fraud, and prohibit retaliation against employees who make such reports.

Take reports of fraud seriously. Treat any fraud reports as serious matters, and conduct thorough, well-documented investigations. The precise nature of employee reports should be carefully documented, in case a question ever arises regarding whether the reported wrongdoing falls within the protected activities covered by Sarbanes-Oxley. Follow up appropriately with those who made the reports to affirm that the company took action, and encourage employees to come forward with any further indications of improper conduct, including perceived retaliation.

Provide SOX training. In addition, train your management staff on Sarbanes-Oxley's whistleblower provisions, and incorporate the anti-retaliation policy and complaint procedures into orientation and training for all of your employees. This is particularly important for employees who will be providing services to public companies and for the managers who supervise those employees.

Review employee terminations before it's too late. Finally, you'll never go wrong by reviewing adverse employment actions involving problematic, "complainer," or "troublemaker" employees, and carefully documenting

the basis for disciplinary actions and terminations. The expansion of Sarbanes-Oxley's whistleblower protection provisions provides yet another good reason for these time-honored practices, which can help you show that you took reasonable steps to protect employees from unlawful retaliation and had legitimate, non-retaliatory reasons for any employment actions taken.

If you would like to discuss the *Lawson* decision or how it applies to your company, please contact any member of our **Litigation Practice Group**, or the Constangy attorney of your choice.

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