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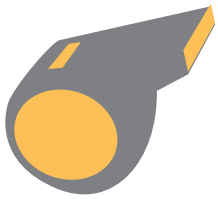
SOX Whistleblower Team Management Alert



First Circuit Rules That SOX Whistleblower Provision Does Not Extend To Employees of Covered Entity's Private Contractors

On February 3, 2012, the First Circuit Court of Appeals ruled in a case of first impression that Section 806 of the Sarbanes-Oxley Act (SOX) does not extend to employees of contractors or subcontractors of a public company. *Lawson v. FMR LLC*, No. 10-cv-2240, 2012 U.S. App. LEXIS 2085 (1st Cir. Feb. 3, 2012).

Background

Plaintiffs Jonathan Zang (Zang) and Jackie Hosang Lawson (Lawson) were employees of Defendants, which are subsidiaries of various Fidelity management companies. Those companies -- all of which are private (*i.e.*, not publicly traded) -- provide advisory and/or management services by contract to Fidelity mutual funds. The Fidelity mutual funds are investment companies registered with the Securities and Exchange Commission (SEC). They have no employees and are not owned or controlled by, or affiliated with, any of the Defendants.

Following his discharge, Zang filed a complaint under Section 806 with OSHA alleging that he was terminated in retaliation for reporting inaccuracies in a draft revised registration statement for certain Fidelity funds. Separately, Lawson filed a complaint with OSHA alleging that she was constructively terminated in retaliation for raising concerns relating to certain cost accounting methodologies. Both Plaintiffs removed their claims to the U.S. District Court for the District of Massachusetts. Zang did so after a full hearing before an Administrative Law Judge (ALJ) at the U.S. Department of Labor (DOL), and following the ALJ's dismissal of his claim. The District of Massachusetts combined the cases and Defendants filed Rule 12(b)(6) motions to dismiss, arguing that Plaintiffs were not covered employees under Section 806. The district court denied the motion.

The Court's Ruling

The First Circuit granted interlocutory review and reversed the district court's ruling, holding that only the employees of public companies are covered by SOX's whistleblower provisions. It stressed that Section 806 provides that no public company "or any officer, employee, contractor, subcontractor, or agent of such company," may retaliate against an employee for engaging in protected activity (18 U.S.C. § 1514A(a)), and that the foregoing language refers to the individuals who are prohibited from retaliating, "not to who is a covered employee."

According to the First Circuit, this interpretation of Section 806's coverage is supported by the following:

- The title of Section 806 ("Protection for Employees of Publicly Traded Companies Who Provide Evidence of Fraud"), and the caption in the first line of subpart (a) of Section 806 ("Whistleblower Protection For Employees Of Publicly Traded Companies");

- Elsewhere in SOX, Congress specifically addressed investment companies and investment advisers, and was explicit as to when it intended coverage and when it did not (*e.g.*, 15 U.S.C. § 7263, exempting investment companies registered under section 8 of the Investment Company Act from certain SOX provisions);
- There are notable distinctions between Section 806 and the language of the Aviation Investment and Reform Act (AIR 21), on which Section 806 was modeled in part. For example, AIR 21 extends protections beyond employees of airlines only to a limited class of contractor and subcontractor employees who perform safety-sensitive functions, but Section 806 lacks analogous language;
- Section 806 varies from the language of other whistleblower protection statutes, such as the Nuclear Whistleblower Protection provision of the Energy Reorganization Act and the whistleblower protection provision of the Pipeline Safety Improvement Act of 2002, which explicitly extend coverage to employees of contractors to entities regulated by those statutes;
- The legislative history (including post-enactment legislative activity) does not support an expansive definition of "employee" under Section 806;
- The Supreme Court has admonished lower federal courts not to give securities laws a scope greater than that allowed by their text; and
- Although the DOL submitted an *amicus* brief favoring Plaintiffs' interpretation of the scope of Section 806 (the SEC submitted an *amicus* brief in support of the Plaintiffs' position as well), the court stressed that neither *Chevron* nor *Skidmore* deference was owed to the DOL's interpretation, particularly given that the Secretary of Labor admitted that the OSHA regulations regarding coverage under Section 806 are not entitled to deference.

Implications For Employers

This decision represents another recent departure from the expansive scope of coverage that the DOL's Administrative Review Board has afforded Section 806. A range of private employers that contract or sub-contract with publicly traded companies now can rely on this decision if and when their employees seek to invoke SOX's whistleblower provisions. However, given the unique relationship between registered mutual funds and their registered investment advisers -- in that the fund itself has no employees and conducts virtually all of its day-to-day operations through the private adviser -- it is possible that this decision could spark the introduction of new legislation or related efforts by governmental agencies (e.g., the SEC) designed to afford whistleblower protection to employees of registered investment advisers. In that regard, it is worth reiterating that the DOL and the SEC submitted *amicus* briefs supporting a broader reading of Section 806 to cover private advisers to public mutual funds.

By: *Steven J. Pearlman*, *Christopher F. Robertson* and *Rachel S. Urquhart*

Steven J. Pearlman is a partner in Seyfarth's Chicago office, *Christopher F. Robertson* is a partner in Seyfarth's Boston office, and *Rachel S. Urquhart* is an associate in Seyfarth's Chicago office. If you would like further information, please contact your Seyfarth attorney, any member of the firm's SOX Whistleblower Team, Steve Pearlman at *spearlman@seyfarth.com*, Chris Robertson at *crobertson@seyfarth.com* or Rachel Urquhart at *rurquhart@seyfarth.com*.