

SEC Cracks Down On Employment Agreements That Stifle Corporate Whistleblowers

On April 1, 2015, the Securities and Exchange Commission ("SEC") gave a boost to corporate whistleblowers, reaching its first settlement with a company accused of stifling whistleblowing activity through the use of restrictive confidentiality agreements. In a statement announcing the settlement, the SEC issued a terse warning to all employers, cautioning them to "similarly review and amend existing and historical agreements that in word or effect stop their employees from reporting potential violations to the SEC."¹ The settlement is a reminder that employer agreements should be drafted carefully so they cannot be read as impeding an employee's right to engage in statutorily protected whistleblower activity, or any protected activity.

The April 1 settlement pertains to Section 21F of the Securities Exchange Act of 1934, enacted in 2010 as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Congress intended Section 21F "to motivate those with inside knowledge to come forward and assist the Government to identify and prosecute persons who have violated the securities laws and recover money for victims of financial fraud."² To fulfill this congressional purpose, the SEC adopted Rule 21F-17, which prohibits companies from taking any action to impede whistleblowers from reporting possible securities violations directly to the SEC. This regulation provides in relevant part as follows:

(a) No person may take any action to impede an individual from communicating directly with the Commission staff about a possible securities law violation, including enforcing, or threatening to enforce, a confidentiality agreement . . . with respect to such communications.

The SEC's April 1st settlement involved engineering and construction firm KBR, Inc., a publically-traded company (NYSE:KBR) and a former subsidiary of Halliburton. As part of its internal investigations, KBR required employees to sign the following agreement to preserve the confidentiality of its witness interviews:

I understand that in order to protect the integrity of this review, I am prohibited from discussing any particulars regarding this interview and the subject matter discussed during the interview, without the prior authorization of the Law Department. I understand that the unauthorized disclosure of information may be grounds for disciplinary action up to and including termination of employment.

The SEC found this form confidentiality statement to violate Rule 21F-17. Specifically, it concluded that the statement's threat of disciplinary action discouraged KBR employees from directly passing along information to the SEC without risking termination. As part of the settlement, KBR amended its confidentiality statement to include the following statement:

Nothing in this Confidentiality Statement prohibits me from reporting possible violations of federal law or regulation to any governmental agency or entity, including but not limited to the Department of Justice, the Securities and Exchange Commission, the Congress, and any agency Inspector General, or making other disclosures that are protected under the whistleblower provisions of federal law or regulation. I do not need

the prior authorization of the Law Department to make any such reports or disclosures and I am not required to notify the company that I have made such reports or disclosures.³

In addition to making this change, KBR also agreed to pay a civil money penalty in the amount of \$130,000 to the SEC for transfer to the general fund of the United States.

Employers should take note that the SEC found no proof that any KBR employee was *actually* discouraged from contacting the SEC. The possibility that a whistleblower *might* be discouraged was sufficient to find a violation of Rule 21F-17. The Director of the SEC's Division of Enforcement, Andrew J. Ceresney, put it bluntly: "By requiring its employees and former employees to sign confidentiality agreements imposing pre-notification requirements before contacting the SEC, KBR *potentially* discouraged employees from reporting securities violations to us."⁴

In the wake of this settlement, employers should carefully scrutinize agreements that threaten employment consequences if an employee discusses possible whistleblower activity, or any protected activity, with governmental entities without the prior approval of the employer's legal department.

1 Press Release, SEC: Companies Cannot Stifle Whistleblowers in Confidentiality Agreements: Agency Announces First Whistleblower Protection Case Involving Restrictive Language (April 1, 2015), available at http://www.sec.gov/news/pressrelease/2015-54.html#_VR61stzF81I.

2 S. Rep. No. 176, 111th Cong., 2d Sess. 110-111 (2010) (Dodd-Frank Senate Report).

3 In the Matter of KBR, Inc., Exchange Act Release No. 74619 (April 1, 2015).

4 Press Release, April 1, 2015 (emphasis added).

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