

SEC Charges More Public Companies for Confidentiality Agreements That Might Deter Whistleblowers

3 min read

Mar 22, 2017

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In the past two years, the SEC has [charged six public companies](#) with violating SEC Rule 21F-17, which prohibits confidentiality agreements that could impede employees from making whistleblower claims directly to the SEC. Since the [Employment Law Observer reported on the SEC's first case](#) attacking a confidentiality agreement, the SEC has charged five more companies with Rule 21F-17 violations. In each case, the employer had confidentiality or severance agreements that either: (a) purported to limit the types of information that an employee may convey to the SEC or other authorities; or (b) required departing employees to waive their rights to any individual monetary recovery in connection with reporting information to the government. The employers settled the cases by, among other things, amending the agreements and paying a significant civil penalty.

Rule 21F-17 has been effective since August 12, 2011. The rule was issued by the SEC in connection with the The Dodd-Frank Wall Street Reform and Consumer Protection Act. The Dodd-Frank Act amended The Securities Exchange Act of 1934 to add Section 21F, "Whistleblower Incentives and Protection," to encourage whistleblowers to report possible violations of the federal securities laws directly to the SEC. The SEC implemented its new authority under Section 21F by issuing Rule 21F-17, which provides, in relevant part, that "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."

On October 16, 2016, the SEC's Office of Compliance Inspections and Examination released a risk alert that employers should consider in reviewing whether their confidentiality and severance agreements comply with Rule 21F-17. Even though the alert is directed to SEC regulated investment advisers and broker-dealers, the guidance applies to any employer with confidentiality agreements.

According to the risk alert, the SEC will review provisions of confidentiality or other agreements required by employers that contain language that, either by itself or under the circumstances in which the agreements are

used, impedes employees and former employees from communicating with the SEC regarding possible securities law violations. The risk alert gives examples of problematic provisions, including:

1. requiring employees to forfeit all benefits if they violate any of the terms of the agreements;
2. requiring employees to represent that they have not assisted in any investigation involving the employer;
3. prohibiting against disclosures of confidential information without any exception for voluntary communications with the SEC concerning possible securities laws violations;
4. requiring employees to notify and/or obtain consent from the employer before disclosing confidential information without any exception for voluntary communications with the SEC concerning possible securities laws violations; and
5. purporting to permit disclosures of confidential information only as required by law without any exception for voluntary communications with the SEC concerning possible securities laws violations.

The SEC's enforcement actions show that it will aggressively protect whistleblowers' rights and its access to their information. In fact, in five out of the six cases, there was no evidence that anyone was prevented from communicating directly with the SEC about potential securities laws violations or that any agreements were enforced to prevent communication with the SEC.

Confidentiality provisions are critical to most employers' business and are typically recommended by counsel and human resource professionals. It is necessary to review the language in those provisions, however, to ensure that the agreements comply with the existing and ever-changing state and federal laws. Overbroad provisions or language which may be read to prevent an employee from lawfully reporting or communicating with a government agency regarding allegedly illegal conduct is could be unenforceable, which could lead to an entire agreement rendered void.

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Topics

Whistleblower, Confidential Information, SEC, Confidentiality Agreement, Securities & Exchange Commission

