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ALERT

SEC Fines Company for Gouging Whistleblower Protections in Severance Agreements

August 11, 2016

WHAT: The U.S. Securities and Exchange Commission (SEC) recently ordered an Atlanta-based company to pay a $265,000 civil monetary penalty for including provisions in its severance agreements with departing employees that impeded the former employees' ability to participate in the SEC's whistleblower program.

WHEN: The SEC issued its Order on August 10, 2016.

WHAT DOES IT MEAN FOR THE INDUSTRY: This settled action is a stark reminder that the SEC intends to utilize its Enforcement program to protect the flow of information into its whistleblower program. Yesterday's action by the SEC follows last year's $130,000 fine levied on Houston-based KBR Inc. for requiring employee witnesses interviewed during internal investigations to sign confidentiality agreements prohibiting them from disclosing the particulars and subject matter of the interviews without prior approval from the company's legal department. Public companies should review their employment and severance agreements to ensure that they do not contain provisions improperly restricting employees' ability to report securities law violations and that any confidentiality provisions in such agreements are appropriately limited.

OUR ANALYSIS: As previously discussed, the SEC's Whistleblower program continues to produce actionable tips and sizeable rewards. In order to ensure that the tips flow unimpeded to the SEC, Section 21F of the Dodd-Frank Wall Street Reform and Consumer Protection Act amended the Securities Exchange Act of 1934 to include certain whistleblower protections. Pursuant to this authority, the SEC

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Practice Areas

Civil Fraud, False Claims, *Qui Tam* and Whistleblower Actions

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White Collar Defense & Government Investigations promulgated Rule 21F-17, which prohibits any person from "tak[ing] any action to impede an individual from communicating directly with the SEC staff about a possible securities law violation, including enforcing, or threatening to enforce, a confidentiality agreement . . . with respect to such communications." Rule 21F-17 became effective on August 12, 2011.

Beginning prior to the effective date of Rule 21F-17, New York Stock Exchange-traded BlueLinx Holdings Inc., regularly entered into severance agreements with employees who were leaving the company that restricted their ability to participate in the SEC's whistleblower program. Specifically, the severance agreements prohibited employees from sharing confidential information about the company unless compelled to do so by law or legal process; required employees to provide written notice to the company or to obtain written consent from the company's legal department prior to providing confidential information pursuant to such legal process; and required employees to waive their right to any monetary recovery in connection with any complaint or charge filed with an administrative agency such as the SEC.

The SEC found that these provisions "raised impediments to participation by [BlueLinx] employees in the SEC's whistleblower program" by "forc[ing] those employees to choose between identifying themselves to the company as whistleblowers or potentially losing their severance pay and benefits." The SEC further concluded that "by requiring its departing employees to forgo any monetary recovery in connection with providing information to the Commission, BlueLinx removed the critically important financial incentives that are intended to encourage persons to communicate directly with the Commission staff about possible securities law violations."

The SEC found that these restrictions on the ability of employees to share confidential corporate information regarding possible securities law violations with the SEC or accept financial awards for providing information to the SEC undermined the purpose of Section 21F and violated Rule 21F-17. To settle the SEC's allegations, BlueLinx agreed to pay a civil monetary penalty of $265,000, amend its severance agreements to protect employees' whistleblower rights, and clarify with former employees that the severance agreements do not prohibit them from communicating with the SEC without notice to the company or from accepting a whistleblower award.