Do Not Attempt To Interfere With Potential Whistleblowing, SEC Warns

written by vickyp | November 19, 2014

Earlier in 2014, Sean McKessy, Chief of the Office of the Whistleblower of the United States Securities and Exchange Commission (the "SEC" or "Commission"), warned lawyers against using private contracts such as employment agreements to discourage potential whistleblowers from reporting alleged corporate misconduct to the SEC and other regulators. In particular, McKessy's comments cautioned against drafting and enforcing confidentiality agreements, separation agreements and employment agreements that condition eligibility for certain benefits or payments on not reporting company activities to regulators.

Those Canadian companies which are under the jurisdiction of U.S. securities law, and thus subject to the SEC's regulatory oversight, must be careful when drafting and enforcing confidentiality agreements and other similar restrictive covenants in their agreements.

Whistleblower Protection Under the Dodd-Frank Act

The *Dodd-Frank Wall Street Financial Reform and Consumer Protection Act* ("Dodd-Frank Act"), which was enacted in July 2010 in the wake of the financial crisis, made important changes to the law on whistleblower protection. The Act created financial incentives for whistleblowers who report securities law violations to the SEC. More importantly, the legislation enhanced anti-retaliation protection for whistleblowers.

The Dodd-Frank Act expressly prohibits employers from punishing an employee for engaging in protected whistleblowing activity. The Office of the Whistleblower of the SEC has adopted further whistleblower-protection rules, which prohibit "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."

McKessy's comments clarified the SEC's broad interpretation of whistleblower protection rules under the Dodd-Frank Act. McKessy warned it would be improper and unlawful to draft contracts that discourage employees from reporting potential

securities law violations to the SEC.

McKessy has also noted that not only would organizations be liable for violation of the new anti-retaliation rules, lawyers who draft the offending provisions may possibly be personally liable and be barred from practising before the SEC as well.

The SEC has taken an expansive view of who is a whistleblower and the Dodd-Frank Act's anti-retaliation provisions more generally. The SEC publicly stated that whistleblowers are entitled to protection under the Dodd-Frank Act rules regardless of whether or not they report wrongdoings directly to their employer or separately to the SEC.

The Office of the Whistleblower and other relevant regulators are likely to increasingly scrutinize how organizations deal with confidentiality agreements and similar restrictive covenants. The stated purpose is likely to be that those provisions do not violate the broad whistleblower protection rules or weaken the incentive structure for reporting violation created by the Dodd-Frank Act or equivalent regimes.

Recommendations

Given the SEC's expansive approach to whistleblower protection, Canadian companies under the regulatory oversight of the SEC should review their codes of conduct and existing agreements. Contracts with current and former employees that contain confidentiality and non-disparagement provisions could be an issue, and organizations should ensure that those agreements are not so broadly worded as to be interpreted as impeding an aspiring whistleblower's ability or incentive to report wrongdoing. Companies may wish to confer with counsel about the propriety of express exclusions for regulatory reporting in restrictive covenants and employment agreements.

It is uncertain whether broad confidentiality clauses (prohibiting disclosure to third parties in general) and non-disparagement clauses (prohibiting the making of disparaging remarks about the company to third-parties in general) would run afoul of the anti-retaliation rules. Therefore, organizations must be particularly cautious about drafting or attempting to enforce broad confidentiality clauses and non-disparagement clauses that do not contain an express exclusion for regulatory reporting. The goal is to ensure that these agreements or clauses will not be construed as attempts to impede the ability to report proper concerns to regulators without the threat of retaliation.

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