

AUGUST 12, 2016

SEC Issues Cease-and-Desist Order Against Severance Agreement Clause Limiting Whistleblowers' Rights to Recover Bounty Awards

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On August 10, 2016, the U.S. Securities and Exchange Commission issued a cease-and-desist Order and imposed remedial sanctions against a publicly traded company for including language in its severance agreements requiring outgoing employees to agree to waive recovery of any monetary award from the SEC after filing a whistleblower complaint with the agency. In *BlueLinx Holdings, Inc.*, the SEC determined this waiver in the company's severance agreements violated SEC Rule 21F-17(a) because it impermissibly would impede a whistleblower's right to communicate directly with the SEC about a possible securities law violation.

The SEC's cease-and-desist Order is the result of a settlement reached between the SEC and the company. In addition to having to amend its severance agreements to comply with the cease-and-desist Order, BlueLinx (a building products distributor based in Atlanta with 1,700 employees) agreed to pay a civil money penalty of \$265,000 to the SEC.

In its Order, the SEC determined the following underscored language in the severance agreements was unlawful:

Employee further acknowledges and agrees that nothing in this Agreement prevents Employee from filing a charge with ... the Equal Employment Opportunity Commission, the National Labor Relations Board, the Occupational Safety and Health Administration, the Securities and Exchange Commission or any other administrative agency if applicable law requires that Employee be permitted to do so; however, Employee understands and agrees that Employee is waiving the right to any monetary recovery in connection with any such complaint or charge that Employee may file with an administrative agency. (Emphasis added.)

According to the SEC, by including this language, the company unlawfully restricted its outgoing employees' ability to participate in the SEC's whistleblower program. According to the SEC, "by requiring its departing employees to forego 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 also objected to language in the severance agreements that required departing employees to notify the company's Legal Department prior to disclosing any financial or business information to any third parties, because the language did not expressly exempt the SEC from the restriction. In short, the SEC determined, "BlueLinx forced those employees to choose between identifying themselves to the company as whistleblowers or potentially losing their severance pay and benefits."

The SEC went on to find:

Restrictions on the ability of employees to share confidential corporate information regarding possible securities law violations with the Commission and to accept financial awards for providing information to the Commission ... undermine the purpose of Section 21F, which is to 'encourage individuals to report to the Commission,' and violate Rule 21F-17(a) by impeding individuals from communicating directly with the Commission staff about possible securities law violations.

Company's New Language

Under the Order, the company agreed to include the following provision in all of its severance agreements – as well as in any other agreements with its employees that include prohibitions on the use or disclosure of confidential information relating to the company:

Protected Rights. Employee understands that nothing contained in this Agreement limits Employee's ability to file a charge or complaint with the Equal Employment Opportunity Commission, the National Labor Relations Board, the Occupational Safety and Health Administration, the Securities and Exchange Commission or any other federal, state or local governmental agency or commission ("Government Agencies"). Employee further understands that this Agreement does not limit Employee's ability to communicate with any Government Agencies or otherwise participate in any investigation or proceeding that may be conducted by any Government Agency, including providing documents or other information, without notice to the Company. This Agreement does not limit Employee's right to receive an award for information provided to any Government Agencies.

Extending *KBR, Inc.*

The SEC's Order in *BlueLinx Holdings Inc.* effectively extends the legal analysis the SEC adopted on April 1, 2015, in its cease-and-desist Order against KBR, Inc.¹ In *KBR, Inc.*, the SEC found language in a confidentiality agreement KBR used in conducting internal investigations and witness interviews to be unlawful. Specifically, the SEC struck down language that prohibited KBR employees from "discussing any particulars regarding this interview and the subject matter discussed during the interview, without the specific advanced authorization of the company's general counsel." The SEC determined that this confidentiality requirement violated SEC Rule 21F-17(a) because it did not make an exception for an employee's right to communicate directly with the SEC about a possible securities law violation.

¹ See Philip M. Berkowitz, Philip N. Storm, Gregory Keating, and Kevin E. Griffith, [SEC's Attack on Confidentiality Agreements](#), Littler Insight (Apr. 6, 2015).

In *BlueLinx Holdings Inc.*, the SEC extends the same analysis to severance agreement clauses that require an outgoing employee to forego any whistleblower award, including a bounty award under the Dodd-Frank Wall Street Reform and Consumer Protection Act, that may result from a successful SEC enforcement action arising from an employee's report to the SEC of independent information about a possible securities law violation.

Recommendations for Employers

Publicly traded employers and all other companies regulated by the SEC should consider reviewing their severance agreement templates and confidentiality agreements to ensure they do not include language that violates SEC Rule 21F-17(a). Severance agreements should contain express language allowing an individual who has entered into a severance and release agreement to: (1) freely communicate with the SEC about the individual's knowledge of any possible violation of SEC rules or law; and (2) recover any bounty award from the SEC that is separate and distinct from, and is not offset by, any severance pay the employer has agreed to provide to the individual. On the other hand—and although the SEC has not given clear guidance on this issue—language providing that the departing employee who is receiving severance pay and benefits is waiving any right to any other monies from the employer—as opposed to recovering an award paid by the SEC— would not appear to violate SEC Rule 21F-17(a).