

SEC Cracks Down on Company Policies that Prevent Employees from Reporting Fraud

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In recent [whistleblower blogs](#), we wrote about the U.S. Securities and Exchange Commission (SEC) efforts to enforce an important rule preventing employers from using employment agreements to curtail employee disclosures of securities fraud and other wrongdoing. In just the last few weeks, the SEC has stepped up its efforts along these lines and levied new penalties against two additional employers who have violated this rule by forcing outgoing employees to sign non-compliant severance agreements. These actions illustrate the SEC's continuing aggressive stance against employers who seek to impede whistleblowers from reporting to the SEC.

SEC Violations

The SEC found that two employers, [BlueLinx Holdings Inc.](#) (BlueLinx) and [Health Net Inc.](#) (Health Net), violated Rule 21F-17(a). Rule 21F-17(a) provides that no employer may take any action – including the inclusion of confidentiality provisions in its employment agreements – to impede an individual from reporting a securities law violation to the SEC. This rule provides an important protection for employees who wish to participate in the SEC's [whistleblower program](#). The program, established by the Dodd-Frank Act of 2010, provides for a whistleblower to receive between 10 and 30 percent of the amount the SEC recovers from wrongdoers if the SEC's enforcement action was triggered by the whistleblower's information. The enforcement must bring in more than \$1 million in order to trigger the whistleblower reward.

In 2014, the SEC [announced](#) its policy that it would seek out examples of agreements in violation of Rule 21F-17(a) and punish employers accordingly. The SEC has made good on its promise. In 2015, it charged KBR Inc. with violating the rule, [resulting](#) in a cease and desist order and \$130,000 penalty against the company. In 2016, the SEC investigated Sandridge Energy, Inc. (Sandridge) for entering into employment agreements that prohibited employees from participating in government agency complaints or investigations pertaining to the company. Sandridge later announced it would amend its employment agreements.

The BlueLinx Settlement

Now, in August 2016, the SEC has announced the settlement of two additional enforcement actions against BlueLinx and Health Net for their violations of Rule 21F-17. The SEC charged BlueLinx, an Atlanta building products distributor, of violating Rule 21F-17 via its agreements with its outgoing employees. Employers commonly offer departing employees severance payments in exchange for, among other things, the employees' release of legal claims against the employers. BlueLinx, however, conditioned its severance payments on the employees' agreements to waive their rights to monetary recovery resulting from charges or complaints filed with federal agencies, including the SEC. This would, of course, include forfeiting rights to an SEC whistleblower program award; therefore, this condition ran afoul of Rule 21F-17. BlueLinx will pay a \$265,000 penalty, amend its severance agreements, and contact its former employees with executed severance agreements to notify them

that BlueLinx will not prohibit them from providing information to the SEC or accepting SEC whistleblower awards.

The Health Net Settlement

A week later, the SEC announced yet another action, this one against California-based health insurance provider Health Net. The SEC alleged that Health Net, after the SEC adopted Rule 21F-17 in 2011, amended its severance agreements to include language allowing former employees to participate in government investigations, but still preventing them from seeking SEC whistleblower awards. Health Net entered into these agreements with approximately 600 employees. The company has agreed to pay a \$340,000 penalty and to contact those former employees to inform them that they are not prohibited from seeking and obtaining SEC whistleblower awards.

Preserving the Freedom to Report

With its announcement of these two actions in the span of one week, the SEC has made clear it will continue to vigilantly enforce Rule 21F-17 and take strong action against employers who discourage employees from reporting company wrongdoing. In doing so, the SEC conveys its strong reliance on company whistleblowers and the SEC whistleblower program as important resources in its regulations of the securities industry. Employees should expect the [recent trend of increased whistleblower awards](#) to continue and feel secure that there are legal protections in place to prevent discouragement of or retaliation for their reporting of employer violations.