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By Electronic Mail and First-Class Mail
May 8, 2013

Ms. Mary Jo White, Chairman
Ms. Elisse B. Walter, Commissioner
Mr. Luis A. Aguilar, Commissioner
Mr. Troy A. Paredes, Commissioner
Mr. Daniel M. Gallagher, Commissioner
United States Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Re: The Use of Severance Agreements to Impede Individuals from Participating in the SEC Whistleblower Program: A Growing Problem and a Recommendation

Dear Commissioners:

We are partners with the law firm of Katz, Marshall & Banks, LLP, an employment law firm based in Washington, D.C. that specializes in the representation of whistleblowers. We are currently representing a number of individuals in the preparation and submission of tips to the Securities and Exchange Commission ("SEC" or the Commission") through the Office of the Whistleblower. We are writing to address an issue that deserves the Commission's prompt attention, namely the attempted inclusion by corporations and their counsel of terms in settlement agreements with departing employees that impede would-be whistleblowers from providing information to the Commission about potential securities violations. As discussed more fully below, we believe that such provisions – which are routinely requested of employees – seriously undermine the SEC's efforts to use the whistleblower-reward program as a critical tool in the Commission's enforcement of the nation's securities laws.

I. Introduction: Incentivizing and Protecting Whistleblowers

The clear intent of Congress in establishing the SEC whistleblower-reward program was to incentivize individuals to come forward with information about violations of securities laws and the Foreign Corrupt Practices Act ("FCPA"). Section 922 of the Dodd-Frank Act also established strong anti-retaliation protections for individuals who report such misconduct. The SEC went a step further when promulgating regulations to govern the program, explicitly making it unlawful to interfere with the efforts of such individuals to provide information to the Commission. Rule 21F-17(a) provides:

> 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 (other than agreements dealing with information covered by § 240.21F-4(b)(4)(i) and § 240.21F-4(b)(4)(ii) of this chapter related to the legal representation of a client) with respect to such communications.

17 C.F.R. § 240.21F-17(a). Unlike the separate anti-retaliation provision, this rule comes into play when a company attempts to block or deter an individual from providing information to the Commission and cooperating in its investigation of that information. The rule is often violated well before an individual experiences actionable retaliation.

II. Technical Compliance with the Rule

The majority of the individuals we represent before the Commission have obtained information about possible securities violations through their employment with the companies whose conduct is the subject of their tips, or sometimes through their employment with related companies. As we know from our own experience and as a number of SEC officials involved in the whistleblower program have noted in public statements, the overwhelming majority of these employee-whistleblowers first report the same securities violations to their companies' management and when their responses were not properly addressed they then report their concerns to the SEC. As a result of their internal reporting and/or of management's learning or suspecting that the employee has also gone to the SEC, many of these whistleblowers experience retaliation for raising their concerns, and they are often involuntarily separated from their employment as a result. Some are demoted, others get fired, and some just find themselves being suddenly criticized, marginalized, or ignored in ways that make it clear that the decision to speak out about wrongdoing has placed their careers in danger despite years of exemplary job performance.

Whether the company terminates the employee as an act of retaliation, the employee "voluntarily" resigns, or the employee departs later for some unrelated reason, many of these whistleblowers end up entering into separation agreements with their former employers in order to obtain severance or other benefits. Such agreements are routinely presented to employees today, and require that the employee release any legal claims against the company in exchange for whatever benefits the company provides. A very large number of employees sign such agreements in the United States every year, often without advice of counsel.

In the eleven years since the passage of the Sarbanes-Oxley Act in 2002, we have represented scores of whistleblowers who have raised concerns about securities fraud and other financial fraud, and who have faced retaliation from their employers as a result. Since the enactment of the Dodd-Frank Act in in July 2010, we have also been routinely advising such whistleblowers about the SEC whistleblower program and, where appropriate, representing them in the preparation and submission of their tips to the SEC. In these cases, we are frequently involved in the negotiation of settlement agreements that resolve our clients' claims of unlawful retaliation, which usually arise under Section 806 of the Sarbanes-Oxley Act, more recently under Section 922 of the Dodd-Frank Act, and/or some state-law counterpart. During negotiations, we often have to respond to attempts by employers and their counsel to include language that interferes with the ability of whistleblowers to participate freely in the SEC program, or which otherwise might frustrate the Commission's enforcement efforts.

It is our observation that most employers, and certainly their counsel, understand that they cannot insist on the inclusion of settlement terms that would expressly prevent a current or former employee from communicating with the SEC. Our clients have regularly been presented with severance agreements requiring departing employees to represent and agree that they "ha[ve] not and will not share non-public, proprietary or otherwise confidential information of the company with any third party." Most employers will agree to modify such a prohibition with language such as, "Nothing in this agreement shall be construed to prevent the employee from communicating with, or participating in an investigation by, any government or law enforcement entity." Despite the broad understanding that an employer cannot expressly prohibit an employee from communicating with the Commission, however, the qualifying language that some employers include in severance or separation agreements still allows the employee to communication with the Commission only if compelled to do so, which is clearly inconsistent with the new SEC rule. The following is commonly seen in employer-proposed agreements:

> Employee agrees that he will not use or disclose any Company information at any time subsequent to the execution of the Agreement, except as required by law. Company information does not include information or knowledge which Employee is required to disclose by order of a governmental agency or court after timely notice of the order has been provided to the Company.

As more companies and their counsel become familiar with the SEC regulations governing the whistleblower program, we would hope to see fewer terms of this type that blatantly violate the new rules by impeding individuals in their communications with the SEC. We also appreciate the public statements that the Office of the Whistleblower leadership have made indicating that they intend to aggressively enforce the rule against impeding whistleblowers, and we expect to see an enforcement action in the future that will go a long way towards deterring the most flagrant violations of the rule.

III. Indirect Impediments and Disincentives to Whistleblowing

While companies and their counsel are largely avoiding attempts to prohibit outright an individual's communicating with the SEC, our law firm and other that represent SEC whistleblowers are nonetheless seeing an increase in proposed settlement language that is intended to achieve the same result in a more roundabout and crafty manner. The language that defense counsel have proposed often attempts to impose on whistleblowers one or both of the following types of restrictions: (1) the requirement that the whistleblower renounce the right to receive any award the SEC might make as the result of a successful enforcement action; or (2) the requirement that an employee disclose to the company all past or future communications with any third party, including government agencies, and/or that the employee agree to cooperate with the company in any ensuing investigation. We believe that both of these types of provisions violate SEC Rule 21F-17(a) and/or (b), and we believe the Commission needs to send a clear signal to employers and employees to that effect.

A. The Requirement to Forego a Whistleblower Reward

As noted above, the primary purpose of the whistleblower reward program is to incentivize individuals to come forward with information concerning securities or FCPA violations about which the SEC would not otherwise know. While frequently criticized by employers and corporate counsel as a "bounty hunter" program that encourages employees to gather information regarding actual or potential violations and report it to the SEC rather than allowing the company the opportunity to investigate and correct problems internally, the whistleblower-reward program represents an acknowledgment of the powerful personal, professional, reputational and financial risks faced by an individual who chooses to investigate and disclose misconduct by his or her employer.

Some settlement provisions require an employee to waive the right to recover monetary compensation in connection with any action brought by an administrative agency against the defendant, thereby removing the incentive Congress established for a would-be whistleblower to come forward. The following are examples that are modeled on actual language that employers routinely include in settlement or severance agreements:[1]

- Employee agrees not to accept, recover, or receive any back pay, damages, or any other form of relief that may arise out of or in connection with any administrative remedies pursued independently by any other person or any federal, state, or local governmental agency or class represented.

- In the event that any agency, self-regulatory organization ("SRO") or court assumes jurisdiction of any lawsuit, claim, charge or complaint on Claimant's behalf, or purports to bring any legal proceedings against the Company, on Claimant's behalf, he promptly will request that the agency, SRO or court withdraw from or dismiss the lawsuit, claim, charge, or complaint with prejudice, and in any event, he waives his right to any form of recovery or relief in any such proceedings on his behalf.

These provisions reflect a practice that pre-dates the Dodd-Frank Act. Employers have for some years included such language in severance and settlement agreements with employees to prevent the employee from accepting a settlement payment, releasing all claims, and then recovering additional damages or relief from the defendant as a result of a class action brought by another employee or an enforcement action brought by the Equal Employment Opportunity Commission ("EEOC"). This practice grew out of case law and EEOC policy prohibiting employers from requiring employees to waive their right to file charges with the EEOC in light of the EEOC's mission of enforcing the nation's anti-discrimination laws, but allowing employees to waive their right to further recovery from the employer after agreeing to settle their individual claims. *See* EEOC Guidance on "Understanding Waivers of Discrimination Claims in Employee Severance Agreements" (Apr. 4, 2009), Sec. III., available online at http://www.eeoc.gov/policy/docs/qanda_severance-agreements.html.

Some of the proposed terms we are seeing may just reflect a continuation of the practice regarding the EEOC, and terms such as the third provision above, which focuses on actions brought "on the Claimant's behalf," should not be interpreted to prevent recovery based on an enforcement action brought by the SEC on behalf of the United States government.

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[1] Due in part to Rule 408 of the Federal Rules of Evidence and its state-level counterparts, which prevent the introduction into evidence of offers of compromise, settlement discussions among parties are generally treated as confidential. In addition, parties to settlement routinely agree not to disclose the terms of settlement agreements except in limited circumstances. For these reasons, the examples we cite in this letter do not quote verbatim from proposed or actual settlement agreements that may include the names of parties and other identifying information, but accurately reflect the language that is pertinent to the issues we raise herein with the Commission.

Nevertheless, such terms, which appear today in the majority of agreements that employees who receive severance or settlement payments sign upon leaving their employment, may impede the employee from submitting information to the SEC by making the employee believe, even if incorrectly, that he or she is required to forego the right to recover an award from the SEC.

Since the establishment of the SEC program, some employers and their counsel are insisting on language that more explicitly requires an employer to waive his or her right to receive an award from the SEC. We have seen a number of employers insist on the inclusion of language in settlement agreements that reads as follow:

- Employee hereby irrevocably assigns to the federal government, or relevant state or local government, any right Employee may have to any proceeds, bounties or awards in connection with any claims filed by or on behalf of the government under any laws, including but not limited to, the False Claims Act and/or the Dodd-Frank Act (and/or any state or local counterparts of these federal statutes or any other federal, state or local *qui tam* or "bounty" statute) against the Company. Employee also represents and promises that Employee will deliver any such proceeds, bounties or awards to the United States government (or other appropriate governmental unit).

We believe that it is imperative that the SEC take a firm stand against contractual language purporting to require anyone to forego an award from the SEC, whether the language purports to require the waiver of "further recovery" or the assignment of any award. These restrictions serve no purpose other than to impede the employee in providing information to the SEC. There is no similarity between the EEOC process and the SEC whistleblower reward program. When an employee agrees to accept a settlement payment from the employer as full and fair consideration for a release of discrimination and other claims, there is no public-policy reason not to allow the employee to waive the right to further payment from the employer. The employee has received compensation from the employer for any harm the employer has caused the employee, and has specifically agreed not to receive additional payment for the same harm.

In the SEC whistleblower program, it is the government and not the employer that pays an award to the employee. The whistleblower's right to an award is a statutory right that has nothing to do with the legal dispute the employee settled with the employer. The right to an award is triggered by the SEC's recovery of more than $1 million from the company in an enforcement action, and although the amount of the award is tied to the amount the SEC recovers, the employer does not pay the award to the whistleblower or pay any additional moneys to the government to satisfy the SEC's obligation to the whistleblower. The award money comes from a fund that the SEC has established for that purpose. Moreover, the SEC pays an award to a whistleblower not as damages for harm the employer subject company has caused the employee (for which the employee has received payment), but rather to reward the employee for providing the Commission with information that has led to a successful enforcement action that furthers the public good. Because the only benefit inuring to a company that obtains a waiver of an employee's right to recover an award from the SEC whistleblower program is to remove the whistleblower's incentive and thus to prevent or thwart SEC action against the company, deterring the employee from reporting to the SEC is clearly a company's only motivation for imposing the waiver on the employee. There is no legitimate justification for allowing companies to impede whistleblowers in this manner.

In this sense, the SEC program can be analogized to a law enforcement agency's practice of posting a notice of monetary reward on the bulletin board in the post office for anyone providing information that leads law enforcement to the arrest and prosecution of a bank robber. A company should not be able by contract to require a whistleblower to forego an award from the SEC any more than a bank robber should be able by contract to require members of the community not to accept an award for turning him in to the authorities in response to a wanted poster in the post office.

We believe that it is likely that a court would find a contract void as against public policy to the extent it requires an individual to forego an award from the SEC, whether as "further recovery" or by assignment,[2] but that does not prevent such contracts from impeding individuals in providing the Commission with information about securities violations. The great majority of such agreements will never end up in court because individuals who have signed them will believe they are barred from receiving an award from the SEC, and they will have no incentive to stick their necks out and risk a breach-of-contract lawsuit and the harm to their careers that whistleblowers commonly suffer. The deterrent effect of the language can, in itself, serve as an impediment to a would-be whistleblower.

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[2] In general, "a promise [will be found] unenforceable if the interest in its enforcement is outweighed in the circumstances by a public policy harmed by enforcement of the agreement." Town of Newton v. Rumery, 480 U.S. 386, 392 (1987). In the whistleblower-reward context of *qui tam* lawsuits under the False Claims Act, courts have held that pre-filing releases of the right of a whistleblower to report wrongdoing and receive a reward are unenforceable. In the leading case, United States v. Northrop Corp., 59 F.3d 953 (9th Cir. 1995), the court emphasized the vital importance of financial incentives in the reporting and successful prosecution of fraud on the government. The court ultimately held that, where the information had not yet been reported to the federal government, a provision in a private settlement agreement purporting to waive a relator's ability to sue and to recover a reward under the False Claims Act was invalid.

By prohibiting impediments that include "enforcing, *or threatening to enforce*, a confidentiality agreement," 17 C.F.R. § 240.21F-17(a), the SEC has already recognized the importance of preventing the chilling effect that employer actions can have on would-be whistleblowers. The Commission should expand the language in Rule 21F-17(a) to make clear that employers also cannot impede an individual by extracting promises to waive, forego, or assign to someone else any award that the SEC issues as a result of a successful enforcement action. The only reason a company would include such a provision in a severance or settlement agreement is to impede the other party from communicating with the Commission. Allowing companies to enforce such promises, or even to achieve the deterrent effect that including them in agreements with employees can have, is contrary to the manifest intent of Congress in instituting the program and the Commission in promulgating rules pursuant to the Dodd-Frank Act.

B. The Requirement to Disclose or Refrain from Engaging in Communications with the Government

In addition to contractual provisions purporting to require whistleblowers to forego their right to awards, we are seeing in our practice an increase in employers insisting on provisions that place various restrictions, limitations or conditions on departing employees' communications with the SEC. These provisions not only impede individuals from providing information to the Commission, but also frustrate the SEC's ability effectively to investigate tips.

One employer tactic towards this end is to require an employee as part of a settlement or severance agreement to certify, in effect, that he or she has not submitted a tip to the SEC. We commonly see language along the following lines in employer-drafted agreements:

> Employee represents that he has not filed any lawsuit, claim, charge, or complaint regarding the Company with any local, state, or federal agency, self-regulatory organization, or court.

An employee who has submitted information to the SEC cannot confidently make this representation because the TCR ("Tip Complaint or Referral") form filed with the SEC can reasonably be considered a "complaint." In fact, the form itself requires the filer to answer a number of questions about his or her "complaint."

Faced with such language, an employee who has submitted a tip to the SEC Office of the Whistleblower must either refuse to sign the agreement and forego any severance or other benefit offered by the agreement, insist on a carve-out for the SEC tip and effectively alert the employer to the likelihood that he has submitted one, or sign the agreement as is and risk having suit filed against him if the employer learns of the employee's tip. This provision also impedes the employee who has not filed a tip but who knows of potential securities violations and is weighing the pros and cons of reporting the same to the SEC. If the employee knows that the employer will require such a certification upon separation from the company, he will likely be deterred from providing information to the SEC because of the dilemma he will face upon his departure – an event which may come soon if, like many whistleblowers, he reports his concerns internally and encounters retaliation that forces him out of his job. In both situations, the employee is impeded in providing information to the SEC, and where the employee has submitted a tip and requests modification of the language quoted above, the SEC's investigative options are limited by the fact that the employer has learned that an investigation may be underway or forthcoming.

Some employers are also requiring departing employees to agree, either explicitly or in effect, to keep the employer informed of communications with the SEC and to cooperate with the company in any investigation by the SEC. We are seeing an increase in these types of contractual provisions, through which the employer can limit or manage a whistleblower's participation in an SEC investigation. Here are three examples of language that employers have proposed for inclusion in agreements governing the post-termination conduct of departing employees:

- Employee will inform the Company within ten (10) days of receipt of a subpoena or inquiry requesting information relating to the Company and will cooperate with the Company in any investigation, regulatory matter, arbitration and/or any third-party lawsuit in which the Company is a subject or party.

- Employee agrees that he will assist and cooperate with the Company in connection with the defense or prosecution of any claim that may be made against or by the Company, or in connection with any ongoing or future investigation or dispute or claim of any kind involving the Company, including any proceeding before any arbitral, administrative, judicial, legislative, or other body or agency, including testifying in any proceeding to the extent such claims, investigations or proceedings relate to services performed or required to be performed by him, pertinent knowledge possessed by him, or any act or omission by him.

- If Employee is requested to respond to an inquiry or provide testimony before the Securities and Exchange Commission (SEC) about this Agreement or its

> underlying facts and circumstances, Employee (or his attorney) should fulfill his obligation to inform the Company of such request, as set forth in this agreement, only after Employee has responded to the inquiry or provided the testimony sought.

These provisions appear intended to, and have the effect of, ferreting out any communications an employee may have had with the SEC, forcing the employee to disclose the information he has provided to the SEC, and allowing the company to manage – and therefore to discourage – the employee's further communications with the Commission under the guise of "cooperation."

Mandatory disclosure and cooperation with the employer in an SEC investigation, especially when those requirements apply to an individual who has submitted a tip to the Commission and is a cooperating witness in its investigation, are inconsistent with free and open communication with the Commission and contravene several SEC rules. In addition to "impeding" the employee from "communicating directly" with the Commission in violation of Rule 21F-17(a), such contractual terms allow the company to make an end-run around Rule 21F-17(b), which reads as follows:

> If you are a director, officer, member, agent, or employee of an entity that has counsel, and you have initiated communication with the Commission relating to a possible securities law violation, the staff is authorized to communicate directly with you regarding the possible securities law violation without seeking the consent of the entity's counsel.

17 C.F.R. § 240.21F-17(b). The purpose of this rule is to allow the SEC unfettered access to individuals who have come forward with information about potential securities violations. The Commission places enough importance on not allowing employers to filter, manage or restrict its communications with a whistleblower to promulgate a rule that arguably bypasses state ethics rules against contact with represented parties. The SEC's rules ensuring direct communications between SEC staff and whistleblowers will have little effect if companies can require whistleblower to notify them of each and every inquiry from SEC and to cooperate with management in responding.

Contractual terms mandating disclosure and cooperation also impinge on the ability of individuals to submit tips to the SEC anonymously using the procedures set forth in Rule 21F-7(b). These procedures, which Commission staff took great pains to design into the program and which will be critical to its success, will be rendered meaningless if companies are allowed to require whistleblowers to notify the company and cooperate every time the whistleblower or his counsel received an inquiry, possibly even an email or a telephone call, from SEC investigators.

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In addition, such provisions hamper the Commission's investigative techniques by making sure that the likely target of an investigation has notice of the investigation from its inception and before the SEC has formally notified anyone of its inquiry.

IV. Conclusion and Recommendation

Employers' practices requiring employees or former employees to agree to settlement or severance provisions such as those described in this letter pose a serious threat to the success of the SEC whistleblower program. Whether enforceable or not, the inclusion of such terms in severance agreements and settlement agreements has a chilling effect on individuals who would provide information to the SEC about potential securities violations. This is especially true for would-be whistleblowers who have signed such agreements without the benefit of counsel, as countless employees do every year in the United States. In a difficult job climate, the widespread use of provisions like those described above, which are routinely presented to employees who may be given only a few days to decide, often without counsel, whether to sign employer-promulgated agreements or forgo severance packages that might cover their mortgages and other expenses until they find new employment, undermines the incentives and protections Congress and the Commission intended to afford to whistleblowers. At the 2012 annual convention of the National Employment Lawyers Association, whose members represent plaintiffs in employment disputes and whistleblower actions, numerous attorneys expressed concern that such provisions would shut down the ability of large numbers of employees to participate in so-called "bounty" programs by effectively removing the incentives that Congress established as a way to encourage participation.

We respectfully urge the Commission to promulgate a regulation or issue an opinion to combat these anti-SEC and anti-whistleblower tactics now, while the program is young. Such regulation or opinion should make clear that enforcement of confidentiality agreements is not the only prohibited means of impeding a whistleblower from communicating with the SEC. For example, the Commission could add the following underlined language to § 240.21F-17(a) to clarify the scope of the protection:

> No person may take any action to impede an individual from communicating directly with the Commission staff about a possible securities law violation<u>, or to affect the rights of an individual who does so. Prohibited actions include, but are not limited to: (1) enforcing, or threatening to enforce, a confidentiality agreement (other than agreements dealing with information covered by § 240.21F-4(b)(4)(i) and § 240.21F-4(b)(4)(ii) of this chapter related to the legal representation of a client) with respect to such communications; (2) requiring that an individual waive, assign, or otherwise relinquish his or her right to a whistleblower award</u>

> under the provisions of Section 21F of the Securities and Exchange Act of 1934; (3) requiring that an individual disclose or report to any third-party, including a former employer, any inquiries, subpoenas, or request for information the individual receives from the Commission, or from any agency working with the Commission, concerning any possible securities law violation; and (4) requiring an individual to assist or cooperate with any third party in responding to or defending itself in an SEC's investigation.

By issuing a regulation or an opinion clarifying the breadth of actions that the Commission views as likely to "impede" communication with the Commission, the SEC could stem the growth of an apparent effort to discourage whistleblowers from providing information to the Commission, which is what Congress sought to incentivize through the SEC whistleblower-reward program that it established through the Dodd-Frank Act.

We believe strongly that the SEC whistleblower program is a critically important tool in the government's arsenal to prevent and remedy securities violations and related misconduct. We appreciate the Commission's consideration of this important issue, and would welcome the opportunity to discuss these matters further with the Commissioners at your convenience.

Sincerely,

David J. Marshall

Debra S. Katz

cc: Mr. Sean McKessy, Chief of the Office of the Whistleblower
Ms. Jane Norberg, Deputy Chief of the Office of the Whistleblower