Confidentiality Agreements Could Run Afoul of Whistleblower Protections

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Last month, the Securities and Exchange Commission took its first-ever enforcement action against a company for whistleblower retaliation. The next agenda item for the SEC, as it lays down the law regarding the treatment of potential whistleblowers may be a crackdown on non-disclosure agreements.

Companies of all sizes, across many industries, require employees to sign confidentiality agreements that prohibit them from discussing anything about their former employer. A tech giant, for example, doesn't want the specs of its new tablet leaked throughout the Internet; a hedge fund wants to retain a competitive advantage by protecting its investment strategy. Non-disclosure agreements, however, are increasingly becoming used as a tactic to discourage whistleblowers from going to the government and, in the case of SEC tips, collecting a bounty.

Among the companies under scrutiny for having whistleblower-silencing confidentiality demands is Kellogg, Brown and Root, a Halliburton subsidiary and defense contractor. The SEC is investigating its use of these agreements. The company recently lost a legal bid to classify such agreements under the umbrella of attorney-client privilege.

A recent Washington Post report also found that International Relief and Development, a non-profit that collected more than $1 billion in tax dollars for war-related projects, tried to silence employees from reporting to government agencies. According to the report, Stephen Cohen, associate director of the Division of Enforcement at the SEC, said: “I’m very concerned about these kinds of agreements. It is likely that a lot of people are not coming to us because of these agreements. Anything that inhibits a person's desire to come forward to tell us about violations of the law is deeply troubling.”

Lawyers who work with whistleblowers are increasingly concerned about the practice too. “We see a seemingly endless array of efforts by companies to come up with new ways to dissuade individuals from providing information to the government,” says David Marshall, a partner at the law firm Katz, Marshall & Banks who specializes in whistleblower cases. “Many of them are couched in terms that look, at first blush, like they might be legitimate, but they can also be used to interfere with speaking with the government.”

Others say while the agreements may say they forbid former employees from providing information to the government, they might not have much legal standing. “Companies are trying to use them, even though I don't think you could ever have a non-disclosure agreement supersede statutory law or individual rights,” says Brian Dickerson, an attorney with the whistle blower-focused law firm Roetzel. “I don't see how you will get the agreements to stick.”
There is no question that the SEC has the tools it needs to pursue the use of confidentiality agreements to thwart whistleblowers. In creating its bounty program, it went one step beyond the Dodd-Frank Act authorization to include the following language: “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.”

“That was the first time, to my knowledge, that an agency told corporations they could not use confidentiality agreements, which are routine for corporate employees, to prevent employees from speaking out,” Marshall says.

Worst Practices

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The use of these agreements also runs contrary to the Federal Sentencing Guidelines and its expectations for compliance programs, Dickerson says. “I'd hate to be the lawyer who has to go into the Department of Justice to say they are complying with the U.S. Sentencing Guidelines, which require a compliance program that is effectively implemented, and even though they have a whistleblower hotline there is also a rule that says employees can't use it. It is contrary to the intent of their own compliance program and that's what most of these companies fail at.”

Some companies may be rethinking confidentiality agreements in general, given the speed and ease at which information now travels. Companies that try the confidentiality gambit may be on a fool's errand, Dickerson says. “It is old school thinking to think you can keep people quiet with so many media outlets and blogs available to them, never mind going directly to the SEC,” he says.

An example of a non-disclosure agreement that Marshall came across in one case, reads:

“[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).”

No-Collect Clauses
Marshall says an increasing number of companies are trying more creative tactics. “What we've seen is a lot more of companies realizing they can't include an agreement that prevents an employee from reporting information to the SEC,” he explains. “Instead, they try to dissuade reporting to the SEC indirectly by trying to remove the incentive that was established in the whistleblower program.”

They are doing that by demanding, carefully crafted contracts as part of severance agreements and exit interviews. “They might say that nothing in the agreement will prohibit you from providing information to government authorities or cooperating in an investigation,” Marshall says. “However, in the event that you receive any compensation or award, you agree to waive it. In the event that they participate in one of these bounty programs, they have to say they won’t collect.”

Other clauses may require an employee to immediately notify the company if they receive any contact from a regulator or investigating agency.

Marshall, in a comment letter to the SEC, compared its program 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 to the arrest of a bank robber. “A company should not be able by contract to require a whistleblower to forgo 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,” he says, adding that he thinks a court, at some point, would find these agreements null and void.

These maneuvers are contrary to the intent of what regulators and lawmakers intended. “The idea is not to foment prosecutions of companies; it is to encourage compliance internally so things don't have to be dealt with by regulators, Marshall says.

Things can be problematic, however, for companies that impose non-disclosure agreements for legitimate reasons, but fail to see the whistleblower ramifications. “We recommend that you have to, at least annually, have an audit where you have all your department heads in there, including human resources, and your compliance officer is going through everything to make sure that the policies and procedures all reflect the goal of the company,” Dickerson says. “If you don't do that, this can fall through the cracks and be looked at negatively if there is an investigation.”

“Nobody looks a these investigations in foresight; it is all 20/20 hindsight,” he adds. “You have to think that way when you do your review.”