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SEC Brings First Enforcement Action Warning Employers Against Imposing Confidentiality Terms That Could Deter Whistleblowers

On April 1, 2015, the US Securities and Exchange Commission brought its first enforcement action against a company for asking employees to agree to confidentiality terms during internal investigations. *See* In the Matter of KBR Inc., Admin. Proc. File No. 3-16446. Despite the fact that it is common for companies to request confidentiality to protect the integrity of an investigation, the SEC took this action after a period of prolonged lobbying by the plaintiff's whistleblower bar. This action is consistent with recent statements to the news media made by SEC enforcement personnel. We discuss the impact of this ruling below.

The SEC alleged KBR Inc., a Houston-based technology and engineering firm, with violating a whistleblower protection regulation, Rule 21F-17, that prohibits companies from taking any action that would deter whistleblowers from reporting possible securities violations to the SEC. The SEC's press release accompanying the enactment of Rule 21F-17 warned that the SEC would "vigorously enforce this provision."

The SEC alleged KBR with asking employees interviewed in internal or other investigations to sign confidentiality statements that included language informing them that they could be disciplined or terminated for disclosing specific information about their interviews without prior approval from KBR's legal department. The SEC found that the language in KBR's confidentiality statements violated Rule 21F-17 because the investigations included allegations of possible securities law violations.

Notably, the SEC did not find that KBR had ever enforced this language or otherwise attempted to prevent employees from reporting securities law violations to the SEC. Nonetheless, the SEC's press release announcing the resolution asserted that any comprehensive requirement barring witnesses from discussing an internal investigation "has a potential chilling effect on whistleblowers' willingness to report illegal conduct to the SEC."

Without admitting or denying the charges, KBR agreed to pay a $130,000 penalty to settle the SEC's charges. KBR also agreed to amend its confidentiality statement with language clarifying that employees are free to report possible violations to any federal agency without approval from company lawyers or fear of retaliation. Specifically, KBR agreed to add the following language to employee confidentiality agreements:

"Nothing in this Confidentiality Statement prohibits me from reporting possible violations of federal law or regulation to any governmental agency or entity, including but not limited to the Department of Justice, the Securities and Exchange Commission, the Congress, and any agency Inspector General, or making other disclosures that are protected under the whistleblower provisions of federal law or regulation. I do not need the prior authorization of the Law Department to make any such reports or disclosures and I am not required to notify the company that I have made such reports or disclosures."

It should be noted that this provision speaks only to federal law and does not address state whistleblower laws by permitting cooperation with state authorities. Many states have various whistleblower statutes of

their own, particularly for state qui tam actions, which often come with their own anti-retaliation provisions. Accordingly, companies should consider well-crafted savings clauses broad enough to capture communications in state enforcement matters as well.

The SEC's enforcement action in this matter has implications for a wide range of agreements containing similar confidentiality language, such as non-disclosure agreements, employment agreements and employee severance agreements.

While the SEC's enforcement action was brought against a public company in this instance, the SEC regulations at issue are broad enough to extend to virtually any US business, and businesses based outside the United States remain subject to SEC regulations to the extent they do business in the United States or have US subsidiaries. In the wake of this order, companies must ensure that any confidentiality provisions in employee agreements explicitly clarify that they do not impede employees' or other potential whistleblowers' opportunity to report possible violations of law without notice to company counsel.

The SEC's action is necessarily limited to the securities laws and the SEC whistleblower rules, but the same logic could apply equally to other federal whistleblowing regimes, including the False Claims Act. The Commodity Futures Trading Commission adopted rules very similar to the SEC's, for example. Thus, other regulators could take a position similar to the one espoused by the SEC, and companies should consider the impact of other regulations when drafting confidentiality agreements.

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