



By the Office of Compliance Inspections and Examinations<sup>1</sup>

**In this Alert:**

**Topic:** *Examinations of investment advisers' and broker-dealers' compliance with Whistleblower Rules.*

**Key Takeaways:** *OCIE is including in certain examinations a review of registrants' compliance with rules impacting whistleblowers and potential whistleblowers that arose out of the Dodd-Frank Act.*

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### EXAMINING WHISTLEBLOWER RULE COMPLIANCE

Staff in the Office of Compliance Inspections and Examinations (the “Staff”) is examining registrants’ compliance with key whistleblower provisions arising out of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”). The Commission has brought several enforcement actions recently charging violations of Rule 21F-17 of the Commission’s whistleblower regulations.<sup>2</sup> The Staff is examining registered investment advisers and registered broker-dealers, reviewing, among other things, compliance manuals, codes of ethics, employment agreements, and severance agreements to determine whether provisions in those documents pertaining to confidentiality of information and reporting of possible securities law violations may raise concerns under Rule 21F-17. This review is included in examinations as staff deem appropriate.

#### I. BACKGROUND

The Dodd-Frank Act amended the Securities Exchange Act of 1934 (“Exchange Act”) by adding Section 21F, entitled “Securities Whistleblower Incentives and Protection.” To implement Section 21F, among other things, the Commission adopted Rule 21F-17<sup>3</sup> under the Exchange Act, which provides that “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 . . . with respect to such communications.” Rule 21F-17 became effective on August 12, 2011.

Recent Enforcement actions have identified certain provisions of confidentiality or other agreements required by employers as contributing to violations of Rule 21F-17 because they contained language that, by itself or under the circumstances in which the agreements were used, impeded employees and former employees from

<sup>1</sup> The views expressed herein are those of the staff of OCIE, in coordination with other staff of the Securities and Exchange Commission (“SEC” or “Commission”), including staff of the Division of Investment Management and the Division of Enforcement. The Commission has expressed no view on the contents of this Risk Alert. This document was prepared by the SEC staff and is not legal advice.

<sup>2</sup> See, e.g., *In the Matter of KBR, Inc.*, Release No. 34-74619 (April 1, 2015), <https://www.sec.gov/litigation/admin/2015/34-74619.pdf>; *In the Matter of Merrill Lynch, Pierce, Fenner & Smith Incorporated et al*, Release No 78141, (June 23, 2016), <https://www.sec.gov/litigation/admin/2016/34-78141.pdf>; *In the Matter of Health Net, Inc.* Release No 78590 (Aug. 16, 2016), <https://www.sec.gov/litigation/admin/2016/34-78590.pdf>; *In the Matter of BlueLinx Holdings Inc.*, Release No. 78528 (Aug. 10, 2016), <https://www.sec.gov/litigation/admin/2016/34-78528.pdf>; *In the Matter of Anheuser-Busch*, Release No. 78957 (Sept. 28, 2016), <https://www.sec.gov/litigation/admin/2016/34-78957.pdf>.

<sup>3</sup> “Implementation of the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934,” Release No. 34-64545, <http://www.sec.gov/rules/final/2011/34-64545.pdf>.

communicating with the Commission concerning possible securities law violations.<sup>4</sup> This potential chilling effect can be especially pronounced when such documents (*e.g.*, severance agreements) provide that an employee may forfeit all benefits if he or she violates any terms of the agreement.

Remedial actions taken in recent Enforcement actions have included:

- revising documents on a going-forward basis to make it clear that nothing contained in those documents prohibits employees or former employees from voluntarily communicating with the Commission or other authorities regarding possible violations of law or from recovering a Commission whistleblower award;<sup>5</sup>
- providing general notice to employees, or notice to employees who signed restrictive agreements, of their right to contact the Commission or other authorities;<sup>6</sup> and
- contacting former employees who signed severance agreements to inform them that the company does not prohibit them from communicating with the Commission or seeking a whistleblower award.<sup>7</sup>

## II. EXAMINATIONS

In examinations where the Staff includes a review of registrants' compliance with Rule 21F-17, the Staff is analyzing a variety of documents, including:

- Compliance Manuals;
- Codes of Ethics;
- Employment Agreements; and
- Severance Agreements.

In this review, the Staff assesses whether these documents contain provisions similar to those in agreements that the Commission has found to violate Rule 21F-17, including provisions that: (a) purport to limit the types of information that an employee may convey to the Commission or other authorities;<sup>8</sup> and (b) require departing employees to waive their rights to any individual monetary recovery in connection with reporting information to the government.<sup>9</sup>

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<sup>4</sup> See *In the Matter of Health Net, Inc.* (respondent's severance agreements included language requiring the signatory to waive his or her right to any monetary recovery pursuant to Section 21F of the Exchange Act); *In the Matter of BlueLinx Holdings Inc.* (respondent's severance agreements included language requiring the signatory to waive his or her right to any monetary recovery related to any government investigation); *In the Matter of Merrill Lynch, Pierce, Fenner & Smith Incorporated et al.* (language found in Respondent's form severance agreement limited the types of disclosures that the employees could make to the Commission or government authorities); *In the Matter of KBR, Inc.* (before interviewing employees in internal investigations into possible securities law violations, Respondent required witnesses to sign a confidentiality statement agreeing that they would not discuss the subject matter of the interview without prior approval of the Law Department); *In the Matter of Anheuser-Busch* (respondent's separation agreement contained language that impeded an employee of respondent's wholly owned subsidiary from communicating directly with Commission staff).

<sup>5</sup> See, *e.g.*, *In the Matter of BlueLinx Holdings Inc.*; *In the Matter of KBR, Inc.*; see also *In the Matter of Merrill Lynch, Pierce, Fenner & Smith Incorporated et al.*

<sup>6</sup> See, *e.g.*, *In the Matter of KBR, Inc.*; see also *In the Matter of Merrill Lynch, Pierce, Fenner & Smith Incorporated et al.*

<sup>7</sup> See, *e.g.*, *In the Matter of Health Net, Inc.*; *In the Matter of BlueLinx Holdings Inc.*

<sup>8</sup> See, *e.g.*, *In the Matter of Merrill Lynch, Pierce, Fenner & Smith Incorporated et al.*

<sup>9</sup> See, *e.g.*, *In the Matter of Health Net, Inc.*; *In the Matter of BlueLinx Holdings Inc.*

The Staff also assesses whether these documents contain other provisions that may contribute to violations of Rule 21F-17 in circumstances where their use impedes employees or former employees from communicating with the Commission, such as provisions that:

- (a) require an employee to represent that he or she has not assisted in any investigation involving the registrant;
- (b) prohibit any and all disclosures of confidential information, without any exception for voluntary communications with the Commission concerning possible securities laws violations;
- (c) require an employee to notify and/or obtain consent from the registrant prior to disclosing confidential information, without any exception for voluntary communications with the Commission concerning possible securities laws violations; or
- (d) purport to permit disclosures of confidential information only as required by law, without any exception for voluntary communications with the Commission concerning possible securities laws violations.<sup>10</sup>

When examining registrants' compliance with Rule 21F-17, the Staff is citing deficiencies and making referrals to the Division of Enforcement where appropriate.

### **III. Conclusion**

Registrants are encouraged to consider the issues identified in this Risk Alert to evaluate whether their compliance manuals, codes of ethics, employment agreements, severance agreements, and other documents contain language that may be inconsistent with Rule 21F-17.

The Staff welcomes comments and suggestions about how the Commission's examination program can better fulfill its mission to promote compliance, prevent fraud, monitor risk, and inform Commission policy. If you suspect or observe activity that may violate the federal securities laws or otherwise operates to harm investors, please notify us at [http://www.sec.gov/complaint/info\\_tipscomplaint.shtml](http://www.sec.gov/complaint/info_tipscomplaint.shtml).

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*This Risk Alert is intended to highlight for firms risks and issues that the staff has identified. In addition, this Risk Alert describes risks that firms may consider to (i) assess their supervisory, compliance and/or other risk management systems related to these risks, and (ii) make any changes, as may be appropriate, to address or strengthen such systems. Other risks besides those described in this Risk Alert may be appropriate to consider, and some may not be applicable to a particular firm's business. The adequacy of supervisory, compliance and other risk management systems can be determined only with reference to the profile of each specific firm and other facts and circumstances.*

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<sup>10</sup> See, e.g., *In the Matter of KBR, Inc.*; see also *In the Matter of Merrill Lynch, Pierce, Fenner & Smith Incorporated et al.*