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Caution Advised for Language in Employment Settlement and Severance Agreements

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Over the years, the Securities and Exchange Commission has taken aim at common language in settlement and severance agreements regarding nondisclosure and confidentiality. It has been relatively commonplace for such agreements to include language that requires, for example, the settling or departing employee to agree not to disclose the employer's confidential information or trade secrets, and/or that, when disclosures are required by the employee by law, the employee will notify the company's legal department in writing. This is no longer permitted.

The SEC also forecloses language in the agreements that permit the filing of a charge with the federal agency, but attached to that a waiver by the employee of a right to any monetary recovery in connection with such a complaint or charge.

Rule 21F-17, which followed the passage of the Dodd- Frank Wall Street Reform and Consumer Protection Act, provides the SEC with its rationale. The Rule states that "[n]o person may take any action to impede an individual from communicating directly with commission staff about possible securities law violations, including enforcing, or threatening to enforce, a confidentiality agreement … with respect to such communications." Both the NLRB and EEOC have taken similar stances. Language such as that cited above can be and in some cases have been viewed as an illegal impediment to the right of individuals to communicate with these regulatory agencies.

The SEC assessed a monetary penalty of $265,000 against a publicly traded company in 2016 where its severance agreement required employees to waive their rights to monetary recovery if they filed a charge or complaint with the SEC or other federal agencies, and prohibited the disclosure of confidential employer information except under compulsion by law, after first notifying the company and obtaining its written consent. The SEC noted that in part, these provisions removed financial incentives that could encourage employees to communicate with the commission.

In a separate enforcement action involving another publicly-traded company, the SEC assessed a monetary penalty of $340,000 for the inclusion in the severance agreement of provisions that employees could freely participate in investigations or proceedings before any agency, but that they waived any individual monetary recovery. Again, the commission found that the agreement removed "critically important financial incentives that are intended to encourage persons to communicate directly" with commission staff about violations of securities law.

The SEC has not targeted closely- held businesses to date, but the possibility exists that a private company that contracts with publicly traded firms could be subject to scrutiny for these provisions. Further, even privately held companies may find themselves the subject of scrutiny by agencies such as the NLRB and EEOC.

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