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SEC and State OIG Allege that Contractors' Policies, Procedures, and Agreements Suppress Whistleblowing

Article By:

Susan B. Cassidy

In a span of two days, two separate agencies took action against contractor policies and agreements that may discourage whistleblowers. On March 30, 2015, the U.S. ***Department of State Office of Inspector General*** ("State OIG") issued a report contending that certain contractor policies and agreements have a "chilling effect" on whistleblowers. On April 1, 2015, the ***Securities and Exchange Commission*** ("SEC") imposed a fine of $130,000 on a contractor for requiring confidentiality agreements that allegedly impede individuals from disclosing securities law violations. Given recent scrutiny, contractors should consider reviewing policies, procedures, forms, agreements, or practices that may impede employees' ability to report instances of fraud, waste, and abuse.

The SEC's April 1 order was based on a violation of SEC Rule 21F-17, which prohibits "imped[ing] an individual from communicating directly with [the SEC] about a possible securities law violation, including enforcing, or threatening to enforce, a confidentiality agreement. . . ." The contractor that received the fine required employees to sign a confidentiality agreement after discussions in internal investigations. Specifically, the confidentiality agreement prohibited employees from "discussing any particulars regarding this interview and the subject matter discussed during the interview, without the prior authorization of the Law Department." The SEC found that this provision, coupled with a statement that such impermissible disclosures may be grounds for termination, violated Rule 21F-17, even though it was not aware of any evidence that the provision had been enforced.

State OIG similarly took issue with certain contractor confidentiality agreements and policies. State OIG, in analyzing the practices of the 30 largest State Department contractors, faulted 13 contractors for having policies that have "a chilling effect on employees who wish to report fraud, waste, or abuse. . . ." Specifically, State OIG criticized policies instructing employees to "consult with the Legal Department" or their supervisor before answering government investigators' questions or handing over documents, or requiring consultants receiving subpoenas or other judicial demands for contractor confidential information to provide "prompt written notice" to the contractor in order to permit the contractor from seeking a protective order. State OIG also flagged separation and employment agreements that may have the same "chilling effect"—citing agreements prohibiting statements that could be "derogatory or detrimental to the good name or business reputation" of a contractor.

According to State OIG, following certain “best practices” might mitigate such chilling effects. These best practices—which exceed the requirements of the Federal Acquisition Regulation (“FAR”) for many contractors—include creating an internal hotline for anonymous reporting, displaying hotline posters, incorporating FAR anti-retaliation provisions and notifications of the right to directly contact the Government in policies, and instructing employees to cooperate with Government audits or investigations.

This follows similar action by Congress to protect whistleblowers. Prior to the passage of section 828 of the 2013 National Defense Authorization Act, which established a pilot program extending whistleblower protections to subcontractors, Department of Defense (“DoD”) subcontractors were not covered under whistleblower protections, and if a case of whistleblower retribution by a subcontractor was brought to the DoD’s Inspector General for administrative investigations, it would not have been investigated. Importantly, that Act also stipulates that whistleblower rights and remedies cannot be waived by any agreement, policy or condition of employment, which could presumably include an overly broad confidentiality agreement. Further, in December 2014, Congress passed the Consolidated and Further Continuing Appropriations Act, 2015. That Act, at Div. E, title VII, § 743, prohibits any appropriated funds from being available for any contract, grant, or cooperative agreement with an entity that requires employees or contractors to sign confidentiality agreements prohibiting or “otherwise restricting” employees or contractors from lawfully reporting waste, fraud, or abuse.

These recent actions call into question some common industry practices, and expose a tension between rules encouraging the disclosure of fraud, waste, and abuse, and a company’s ability to protect privileged information discussed in the course of internal investigations performed to obtain legal advice. For example, at issue in the SEC matter was a confidentiality provision in a form statement that the contractor used with company witnesses in internal investigation that directed employees to not share information from that interview without authorization of the Law Department or be subject to discipline up to and including termination. Neither the State OIG report, nor the SEC order addresses the legitimate need of the contractor to maintain privilege in an internal investigation. In the meantime, however, contractors should consider taking steps to limit compliance risks while balancing the need to keep confidential information protected.

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