Several Common Employment Agreement Provisions Could Violate the Securities Act

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In July 2016, the Ontario Securities Commission (OSC) launched its Whistleblower Program — the first of its kind in Canada. Under the Whistleblower Program, the regulator promised to pay up to $5 million to anyone who submitted a report of potential misconduct that led to an OSC enforcement action.

Since the Program's launch, however, the impact of its rules on employment agreements (contained in section 121.5(3) of the *Securities Act*) has gone overlooked. Modelled after similar U.S. rules adopted by the Securities and Exchange Commission (SEC), the OSC's rules automatically void employment agreement provisions to the extent that they preclude employees from communicating with regulators about potential securities law violations.

While employers may at first glance believe that their existing employment agreements are compliant, the scope of the prohibition is so broad that it may void several common employment agreement provisions and potentially subject employers to OSC enforcement action.

Confidentiality provisions

Provisions in employment agreements that prohibit employees from sharing confidential company information with third parties or require departing employees to return confidential company information to the employer are ubiquitous. While such provisions are often intended to protect disclosure of company information or trade secrets to competitors, they may also be construed as preventing an employee from sharing non-public company information with regulators. For example, the SEC settled charges against Anheuser-Busch InBev in September 2016 over allegations that it had violated the whistleblower rules by requiring departing employees to sign a severance agreement that obligated them to "keep in strict secrecy and confidence any and all unique, confidential and/or proprietary information and material belonging to [the company]".

Non-disparagement provisions

Another common provision in many companies' employment agreements is non-disparagement clauses that restrict what an employee may say about a company in the public domain or to third parties. As with confidentiality provisions, non-disparagement provisions may be construed as preventing an employee from providing information to regulators that would portray the company in a poor light. The SEC settled charges against SandRidge Energy in December 2016 for requiring departing employees to agree to "not at any time in the future defame, disparage or make statements or disparaging remarks which could embarrass or cause harm to SandRidge's name and reputation".

Subpoena/legal request provisions

Many companies justifiably want to ensure that they are made aware of potential legal proceedings and government investigations in advance of public disclosure. To do so, they have employees agree to notify the company of any subpoenas or other legal requests for information related to the company that the employee receives. Such provisions can be construed as violating the whistleblower rules in the *Securities Act* by precluding the employee from cooperating with regulators on a confidential basis in response to a regulator's subpoena or request for information. The SEC took this aggressive interpretation of its whistleblower rules in a settled action against BlueLinx Holdings in August 2016. In that case, the SEC concluded that the company had violated the whistleblower rules by requiring "employees either to provide written notice to the company or to obtain written consent from the company's legal department prior to" disclosing confidential company information pursuant to legal process (*e.g.*, a subpoena).

Internal investigations warnings

Oftentimes the integrity of a company's internal investigation will depend on the participants in the investigation keeping it confidential. A witness who after an interview discusses the fact of the investigation with the target or the substance of their interview with another witness can taint the findings of the investigation. To mitigate this risk, company investigators will often require that witnesses agree to keep the fact of the investigation and the substance of their interview confidential. In doing so, however, company investigators could be viewed as precluding witnesses from communicating with government regulators. In the SEC's first enforcement action under its whistleblower rules in April 2015, it settled charges with KBR over precisely this practice.

Implications

Companies subject to OSC jurisdiction should ensure that they review their employment agreements (*e.g.*, employment contracts, separation/severance agreements, release agreements, confidentiality agreements, and codes of conduct) to identify any provisions that could be construed as precluding an employee from communicating with regulators about potential securities law violations. Once companies have identified potentially violative provisions, they should consider solutions that have been effective in the U.S. context, including disclaimers or carve-outs that explicitly protect employee rights under the whistleblower rules.

While the OSC's Whistleblower Program has not been the subject of much attention lately, the regulator disclosed last year that it has received approximately 200 tips since the Program began and many of those tips are associated with active investigations. As the tips begin generating enforcement actions, the OSC may well follow its U.S. counterpart and begin examining the tipsters' company employment agreements to determine whether they violate the whistleblower rules and warrant enforcement action of their own. Companies would be well-advised to review their employment agreements to mitigate their potential risk.

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