White and Williams LLP

Employers Beware: New Developments Require Changes in Employment Agreements

By: Lori Smith, George Morrison and Michael Psathas
Corporate and Securities Alert
8.23.16

There have been a number of recent legal developments that require employers to review and consider modifications to their existing forms of employment and severance agreements. Failure to adequately comply with these changes can have significant pecuniary consequences that can ultimately affect a company's bottom line. The below discussion includes a brief summary of the U.S. Securities and Exchange Commission's (SEC) recent enforcement actions relating to anti-whistleblower provisions in agreements with employees and considerations for employers to protect their trade secret rights as a result of the Defend Trade Secrets Act of 2016 (DTSA).

SEC Sanctions Employers for Anti-Whistleblower Provisions

The SEC recently sent a clear message to employers – expect enforcement action with harsh financial penalties for including anti-whistleblower provisions in employment agreements.

As many practitioners are well aware, the Dodd-Frank Wall Street Reform and Consumer Protection Act provides certain financial incentives for employees to disclose improper conduct by employers and prohibits retaliation against such employees who become "whistleblowers." The SEC enacted Rule 21F-17 in 2011 to implement these provisions which generally prohibits impeding an employee from communicating with the SEC about possible securities law violations. Importantly, the actions by the SEC earlier this month demonstrate that the SEC intends to aggressively pursue illegal anti-whistleblower provisions in employment agreements.

On August 10, 2016, the SEC settled with BlueLinx Holdings Inc., an Atlanta-based building products distributor, after the SEC found that the company used severance agreements to require outgoing employees to waive possible whistleblower awards in the event such employees were to file a complaint with the SEC or other agencies. Although BlueLinx consented to the SEC's cease-and-desist order without admitting or denying the SEC's findings, BlueLinx was required to pay a $265,000 sanction and contact former employees to amend its severance agreements to be in compliance with the law.

In another recent matter on August 16, 2016, the SEC imposed a $340,000 penalty on Health Net Inc., a California-based health insurer, for illegally using severance agreements as a way to curb outgoing employees from talking with federal officials about company violations. Similar to the BlueLinx case, Health Net was required to notify former employees that the company does not prohibit its employees from seeking whistleblower awards from the SEC.

Stephanie Avakian, the Deputy Director of the SEC's Enforcement Division, made it clear that similar cases may be brought in the near future. "We're continuing to stand up for whistleblowers and clear away impediments that may chill them from coming forward with information about potential securities law violations," she said. As a result, employers should carefully draft employment agreements to not impermissibly restrict protected whistleblower rights or else risk financial penalties by the SEC and other regulatory agencies.

DTSA Requires Certain Notification To Protect Employer Rights

The Defend Trade Secrets Act of 2016 was recently signed into law, granting trade secret owners a private right of action to pursue in federal court any misappropriation of a trade secret. The DTSA expands federal protection for trade secrets to a level more aligned with

federal protections for trademarks, copyrights and patents.

The substantive provisions of the DTSA are consistent with the Uniform Trade Secrets Act (UTSA), a state law remedy that has been adopted in some form, although not consistently, by many states. Unlike the UTSA, the DTSA authorizes *ex parte* orders "to prevent the propagation and dissemination" of trade secrets, pending a hearing. A successful plaintiff may also obtain injunctive relief, actual damages and profits for unjust enrichment, or alternatively, a reasonable royalty for the wrongful use of a trade secret. Importantly, punitive damages and attorneys' fees are also an available remedy under certain circumstances.

The DTSA provides protection for whistleblowers, insulating them from criminal and civil liability under state and federal trade secret law for disclosing trade secrets (1) confidentially to the government or an attorney in connection with an investigation of unlawful activity, (2) with a court under seal, and (3) in connection with employer retaliation suits.

The DTSA requires that employers notify employees of this immunity in their agreements addressing protection of confidential information if such agreement was entered into (or updated) after the enactment of the DTSA. Failure to comply with such rules could preclude recovery of enhanced damages or attorneys' fees in any action under the DTSA against an employee to whom such notice was not provided.

Employers should familiarize themselves with the DTSA and develop and revise confidentiality and trade secrets provisions in their form employment agreements and standalone confidentiality and trade secrets agreements. In addition, employers should likewise confirm that they comply with the DTSA's notice requirements to preserve their right to seek attorneys' fees and exemplary damages in the event of actionable willful and malicious misappropriation of a trade secret by an employee.

Conclusion

In order to properly protect employers with respect to departing employees, employers will need to consider the implications of various provisions that in the past may have become commonplace. Recent developments in the law and the latest actions by regulatory agencies, such as the SEC, have altered the employment landscape and employers must adapt to such changes or risk potential consequences.

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