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Five Key Issues Confronting Financial Services Industry Employers

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Employers in the financial services industry are faced with a growing number of employment law challenges. Whistleblower complaints are on the rise as regulatory agencies become more aggressive in their efforts to encourage employees to report alleged unlawful conduct. The Financial Industry Regulatory Authority ("FINRA") arbitration process is becoming even more unpredictable under new rules that may result in arbitration panels that are less familiar with the industry. Expanding globalization requires employers to navigate numerous immigration hurdles that arise from managing a cross-border workforce. This edition of Epstein Becker Green's *Take 5* addresses these important topics and what employers should know about them:

1. **The SEC Is Targeting Companies That Use Confidentiality Agreements That Silence Whistleblowers in Violation of the Securities Exchange Act**
2. **OSHA Has Issued Its Final Rule Governing Whistleblower Retaliation Complaints Brought Under Section 806 of the Sarbanes-Oxley Act**
3. **Internal Whistleblower Complaints Raise Important Considerations**
4. **Rule Changes Affect the Composition of Arbitration Panels in FINRA Disputes**
5. **Establishing Mobility Programs Is Essential for a Global Workforce**

1. The SEC Is Targeting Companies That Use Confidentiality Agreements That Silence Whistleblowers in Violation of the Securities Exchange Act

The Securities and Exchange Commission ("SEC") is looking closely at employment agreements, separation agreements, and other agreements that include confidentiality provisions that prevent or discourage employees from reporting possible unlawful conduct to the SEC. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank") amended the Securities Exchange Act to include protections and incentives (i.e., the whistleblower "bounty" program) to encourage whistleblowers to come forward. One of the implementing regulations of the bounty program, Rule 21F-17(a), specifically prohibits

employers from taking any action that would "impede" an employee from communicating with the SEC about potential securities law violations, including enforcing or threatening to enforce a confidentiality agreement.

The SEC Cites Potential "Chilling Effects"

On April 1, 2015, the SEC announced that it had resolved its first enforcement action against a company, KBR, Inc. ("KBR"), for using overly restrictive confidentiality provisions. KBR's compliance investigators required witnesses who were interviewed during the investigation of certain types of internal complaints to sign a statement that they were "prohibited from discussing any particulars regarding [the] interview and the subject matter discussed, without the prior authorization of the Law Department" and that "unauthorized disclosure of information may be grounds for disciplinary action up to and including termination." There was no evidence that KBR ever prevented an employee from communicating with the SEC, or ever enforced the confidentiality statement to stop such communications.

Nevertheless, the SEC found that the statement violated Rule 21F-17 and undermined its purpose by forbidding employees from communicating with the SEC about the substance of an interview without KBR's permission, lest they face discipline or even termination. In a press release announcing the action against KBR, the SEC said that "any company's blanket prohibition against witnesses discussing the substance of the interview has a potential chilling effect on whistleblowers' willingness to report illegal conduct to the SEC."

For this first action, the SEC targeted a very specific type of confidentiality agreement that was being used only in the limited context of certain internal investigations. The scope of the SEC's position will likely be further developed if and when it commences actions involving severance agreements, employment contracts, or general confidentiality agreements.

The Attorney-Client Privilege

In addition, the SEC's statement does not address the lawfulness of confidentiality agreements that a witness might be asked to sign in connection with an internal investigation that is protected by attorney-client privilege. Significantly, the SEC's reference to the "chilling effect" of confidentiality provisions that prevent witnesses from discussing interviews invites inquiry into an exception built into Rule 21F-17. That exception explicitly excludes from its reach confidentiality agreements that cover information obtained through attorney-client privileged communications, unless disclosure of that information falls under another SEC rule permitting attorneys who appear before the SEC to reveal confidential client information, without company consent, in certain extreme circumstances.

When legal counsel is performing an internal investigation into alleged unlawful activity, it is standard practice to be guided by the U.S. Supreme Court in *Upjohn Co. v. United States,* 449 U.S. 383 (1981). Based on *Upjohn*, attorneys tell witnesses that the interviews are confidential and subject to the attorney-client privilege. Moreover, attorneys typically explain that for the information to remain privileged, it is important that the witnesses not share the substance of the interview with anyone. While this is often done simply as notice rather than a written agreement, sometimes witnesses are asked to sign a statement containing the *Upjohn* notice.

Thus, the SEC's position in *In re KBR, Inc.,* would not (and should not) apply as a general proscription against the use of confidentiality agreements that apply to information learned during interviews that are part of privileged internal investigations conducted by legal counsel. As recognized in the exception to Rule 21F-17—which was conspicuously unmentioned in the SEC's Order against KBR—a balance must be struck between the SEC's investigatory mission and a company's right to the attorney-client privilege.

In sum, while the full scope of the SEC's enforcement initiative remains to be seen, employers would be wise to review the confidentiality provisions in all of their agreements proactively to ensure compliance with Rule 21F-17.

2. OSHA Has Issued Its Final Rule Governing Whistleblower Retaliation Complaints Brought Under Section 806 of the Sarbanes-Oxley Act

On March 5, 2015, the Occupational Health and Safety Administration ("OSHA") issued its "Final Rule" establishing the procedures for handling retaliation complaints brought under Section 806 of the Sarbanes-Oxley Act ("SOX"). Section 806, as amended by Dodd-Frank, protects employees of publicly traded companies, as well as employees of contractors, subcontractors, and agents of publicly traded companies, from being retaliated against for reporting fraudulent activity or other violations of SEC rules and regulations. The Final Rule addresses the comments that OSHA received in response to its interim rule, issued in 2011, and sets forth the final procedures for retaliation claims under SOX, including the procedures and timeframes applicable to employee complaints and OSHA investigations. While the Final Rule does not differ substantively from the interim rule, it crystalizes the SOX whistleblower complaint procedures and reflects an increasingly whistleblower-friendly landscape.

Verbal Complaints

One of the most important aspects of the Final Rule—and a subject of considerable concern to commenters—is its adherence to the interim rule provision permitting verbal SOX complaints. Prior to the interim rule, complaints had to be in writing and include a full statement of the alleged wrongful acts or omissions. The interim rule eliminated this requirement and permitted complaints to be made verbally and reduced to writing by an OSHA investigator. Commenters argued that this procedure transforms the investigator into an advocate for the complainant, lacks any standard for the investigator's written complaint, and increases the risk that the complainant may attempt to change his or her allegations by contending that the claims were not accurately recorded by the investigator. OSHA rejected these arguments, concluding that allowing verbal complaints is "[c]onsistent with OSHA's procedural rules under other whistleblower statues."

Preliminary Reinstatement

The Final Rule also adopted the interim rule's provision on preliminary reinstatement, i.e., reinstating the complainant to his or her former position during the pendency of a dispute. Commenters had suggested—without success—that OSHA include a provision that preliminary reinstatement should not be granted if the complainant is a security risk and that OSHA articulate specific circumstances under which preliminary reinstatement is appropriate. Instead, the Final Rule provides that, if there is a reasonable basis to believe that a SOX violation has occurred, a preliminary order will be issued that provides the relief necessary to make the complainant whole, including reinstatement to the position that he or she would have had but for the retaliation.

Moreover, as an alternative to actual reinstatement, the Final Rule permits OSHA to order preliminary "economic reinstatement" during the pendency of a dispute, which allows the complainant to collect his or her same pay and benefits without having to return to work. Significantly, OSHA intentionally omitted any mechanism for employers to recover the costs of preliminary economic reinstatement if the complainant is ultimately unsuccessful on his or her claim.

Notice to Respondents

One helpful development for employers is OSHA's decision to clarify in its Final Rule the notice that respondents must receive when a complaint is filed, as well as respondents' right to receive the information that the complainant submits to OSHA during an investigation. The Final Rule expressly provides that, when a complaint is filed, OSHA must notify the respondent of the filing of the complaint, the allegations made, and the substance of the supporting evidence. The Final Rule also notes that OSHA "generally provides the respondent with a copy of its memorandum memorializing the complaint" and that the respondent can "request that OSHA clarify the allegations in the complaint if necessary." In addition, the Final Rule makes clear that, during an investigation, OSHA will ensure that each party receives a copy of all of the other parties' submissions to OSHA and is given an adequate opportunity to respond to those submissions.

In the light of these generally supportive and encouraging procedures for whistleblowers, it is more important than ever for employers to correctly identify, investigate thoroughly, and take appropriate steps to address internal whistleblower complaints before they become costly, full-blown whistleblower disputes.

3. Internal Whistleblower Complaints Raise Important Considerations

The number of whistleblower complaints is on the rise, according to the 2014 Annual Report to Congress on the Dodd-Frank Whistleblower Program, and defending against them can be costly and disrupt business operations. Taking appropriate steps in response to internal complaints can go a long way toward minimizing the risk that the issue becomes an external dispute at OSHA or in court.

Understanding the Objectives

A prompt investigation and an understanding of the objectives of the investigation are paramount. Employers should decide, for example, whether the goal is to create a factual record, prepare an investigative report addressing a particular inquiry or legal consideration, provide a basis for decision making, or serve as a defense in anticipated litigation—or any combination of these objectives. These considerations will determine whether the investigation should be undertaken by a non-attorney or by corporate counsel or outside counsel, or both.

For example, if the goal is simply to correct a problem internally, perhaps corporate counsel is appropriate. If, on the other hand, there is a high likelihood that the employee's complaint will lead to full-blown litigation, outside counsel may be more appropriate. In addition, employers must have a basic understanding of the privileges afforded to attorney work product and attorney-client communications. This is because the choice of investigator can impact whether, and to what extent, these privileges apply to the information adduced during the investigation, which, in turn, will determine whether such information will be protected from disclosure to third parties.

Whistleblowers in Compliance or Audit Functions

Employers should also know how to respond to the challenge raised by complaints made by whistleblowers who work in compliance or audit functions or are otherwise responsible for receiving and investigating internal whistleblower complaints. These "trusted" whistleblowers are especially problematic because, while they should be working to investigate and correct the issue internally, they may also decide to blow the whistle themselves and report the matter to outside authorities. Further, while they are generally ineligible for financial awards under the Dodd-Frank whistleblower bounty program, these "trusted" whistleblowers can become eligible for an award if the business takes no corrective action within 120 days after they make an internal complaint. They are also protected by anti-retaliation provisions of Dodd-Frank and SOX.

Training Managers to Receive Complaints

One of the most important considerations is making sure that supervisors and managers are trained and understand how to recognize and elevate a whistleblower complaint to the appropriate internal legal or compliance unit, and how to conduct themselves going forward to minimize the risk of a retaliation claim by an employee who blows the whistle. Issues are frequently first raised at the supervisory level, and the sooner that compliance and/or legal professionals receive information about a claim so that they can access the appropriate response, the sooner an internal investigation can commence, when necessary.

Further, managing an employee who has made a whistleblower claim can present a host of challenges, particularly if the employee is under-performing and therefore has been or is becoming a candidate for corrective or even disciplinary action. If a current employee raises a whistleblower complaint, it is essential that the alleged wrongdoing is not compounded by retaliation against that employee (or by actions that give the appearance of retaliation). Thus, supervisors and managers should receive periodic training regarding the laws and company policies prohibiting retaliation. They should also understand the need to have any potentially adverse employment actions vetted by the legal department before taking action.

Finally, supervisors and managers should be given appropriate support from the legal and/or human resources departments in terms of counseling and advice in dealing with the whistleblower on a day-to-day basis as issues arise, rather than trying to navigate these waters on their own.

4. Rule Changes Affect the Composition of Arbitration Panels in FINRA Disputes

For financial services industry employers that participate in arbitrations administered by FINRA, the composition of the arbitration panel may have as much, or more, of an impact on the outcome of the dispute than the facts or the law. This is because FINRA arbitrators are not bound to follow case precedent or strictly apply principals of law and can render awards based on their own notions of “fairness” or “justice.” The important process of selecting an acceptable arbitration panel, however, can be opaque, as the information that FINRA provides about prospective arbitrators often gives limited assistance to employers trying to make informed selections. Further, recent changes to the rules affecting the composition of FINRA arbitration panels, particularly in customer cases, make it even less likely that the dispute will be heard by an experienced panel.

Current Selection Procedures

Traditionally, FINRA administrators provided all parties with three lists of arbitrators from which to select a panel: 10 “public” arbitrators, 10 “non-public” arbitrators, and 10 “public” arbitrators qualified to serve as the panel chairperson. The parties would strike a certain number of arbitrators from each list and rank the remaining arbitrators in order of preference. FINRA would then choose the highest-ranked arbitrator from the two lists to form the panel, which would consist of a “public” chairperson and two panelists, one “public” and the other “non-public."

Pursuant to a rule change that took effect on February 1, 2011, and was modified on September 30, 2013, either side in a customer dispute can designate an “all-public” panel by striking all of the arbitrators on the “non-public” list. The change may negatively impact employers because “non-public” arbitrators generally have certain defined connections to, or experience in, the securities industry and can bring an insider’s perspective to bear on the dispute that may be useful in understanding an employer’s position. “Public” arbitrators, on the other hand, generally have limited knowledge of securities or financial services and are perceived as being more

sympathetic to customers. In fact, according to Regulatory Notice 13-30, FINRA found that "customers were awarded damages significantly more often when an all-public panel decided their case."

New Rules

On February 26, 2015, the SEC accepted proposed changes to FINRA rules 12100(p), 12100(u), 13100(p), and 13100(u), which set forth new definitions of "public" and "non-public" arbitrators in customer and industry disputes. The new definitions significantly limit the financial industry experience a person can have and still be permitted to serve as a "public" arbitrator. Further, the rules substantially limit the circumstances under which a "non-public" arbitrator can be reclassified as a "public" arbitrator. Under former rule 12100(p) of the Customer Code (and 13100(p) of the Industry Code), there was a "cooling off" period that prohibited an individual who was classified as a "non-public" arbitrator due to his or her affiliation with certain financial services entities from becoming eligible to serve as a "public" arbitrator until five years after he or she retired from the securities industry. Under the revised rules, the "cooling off" period is eliminated and the same individual may be permanently classified as "non-public" and, therefore, ineligible to serve as a "public" arbitrator.

Employers should be aware that these new rules will significantly reduce the number of individuals who can serve as "public" arbitrators and dramatically decrease the likelihood that an assigned "public" arbitrator will have the financial industry experience and understanding that employers in FINRA disputes often seek. For customer disputes in particular, the new rules, taken together with the "all-public" panel rule, greatly increase an employer's chances of drawing a panel of inexperienced arbitrators with limited understanding of the industry. For industry disputes, where panels still must have one non-public member, the recent rule change further shifts the balance of the panel toward "public" arbitrators with no industry experience.

5. Establishing Mobility Programs Is Essential for a Global Workforce

As the economy becomes increasingly globalized, it is important for financial services industry employers to maintain their competitive edge by developing a robust toolkit of cross-border capabilities. The ability to transfer managers, executives, and other key personnel to the United States expeditiously for short-term or long-term projects or assignments is a growing business necessity. Fortunately, U.S. immigration law contains nonimmigrant (temporary) and immigrant (permanent) visa classifications specifically for managers and executives, and provides a potential fast-track to permanent residency.

Employers, however, must be careful in selecting a visa classification appropriate to the terms and conditions of employment, noting that classifications carry different tax, benefit, and short-term and long-term employment implications. Employers should also be aware of the potential mechanisms that they can utilize to facilitate the international transfer of their vital managerial and executive resource population, making short-notice transfers as quick and seamless as possible.

The L-1A Nonimmigrant Visa Program

Most often, companies transfer their managers and executives from their operations abroad to their U.S. operations through the L-1A nonimmigrant visa program. As a general rule, L-1A classification requires that (1) the U.S. and foreign entities have a qualifying parent, subsidiary, or affiliate relationship; (2) the employee has been employed abroad by the foreign entity for at least one of the last three years in a managerial, executive, or specialized knowledge capacity;

and (3) the employee will be transferring to the United States to serve as a manager or executive.

Criteria for Obtaining an L-1A Nonimmigrant Visa

To take advantage of the L-1A program, employers should carefully document their corporate organizational structure in a manner demonstrating that the size and scope of their operations warrants the services of an L-1A manager or executive. Employers that apply for an L-1A visa without a clearly documented structure may be faced with requests for additional evidence that can delay the application process substantially.

Employers should also take care in defining a manager or executive's role and responsibilities. The U.S. Citizenship and Immigration Services ("USCIS") and the U.S. Department of State tend to focus on particular factors in adjudicating L-1A applications, including whether the individual has any direct reports, budgetary authority, and discretionary decision-making authority in policy formation and/or day-to-day company operations.

While these criteria are seemingly straightforward, the financial services industry's increasing tendency toward heavily matrixed management structures does not always align with the USCIS's understanding of a personnel manager. Therefore, it is important in these cases to strengthen the managerial argument by carefully identifying a discrete and organizationally important "function" or area of operations that will be managed by the employee.

Drawbacks to L-1A Classification

When considered as part of a larger global mobility strategy, L-1A classification can have notable long-term and programmatic benefits, including:

- the possibility of an expedited green card process (foregoing the often lengthy and expensive labor certification ("PERM") process) for managers and executives who were also employed in managerial or executive positions with the qualifying entity abroad;
- the avoidance of annual quotas associated with the H-1B visa program;
- the ability to streamline the transfer of managers and executives by obtaining L-1 Blanket Petition approval from the USCIS, which reduces onboarding time by enabling employees to apply for L-1 visas directly at a U.S. Consulate or Embassy;
- high predictability for senior managers and executives so that organizations can plan for transfers and rely on set timelines; and
- the potential for keeping L-1A managers and executives transferred to the United States on a foreign payroll, facilitating relocation packages and the retention and continuity of social benefits.

Alternatives to L-1A Classification

L-1A classification is not a one-size-fits-all category, however, and the filing costs, time limitations (including an overall seven-year period of stay), and tax implications (L-1 holders are generally held to the same tax standards as U.S. citizens and green card holders) may not make business sense for managers and executives traveling to the United States on a short-term basis. In developing an internal immigration program, employers should be aware that there may be alternative solutions available, including:

- intermittent L-1A status for managers and executives who spend less than half their time in the United States during the year, which eliminates the seven-year time limitation and may lessen or eliminate U.S. income tax liability by qualifying them as nonresident aliens; and

- B-1 Business Visitor or Visa Waiver classification for managers and executives travelling to the United States on a very short-term basis to attend business meetings or conferences, participate in short-term trainings, negotiate contracts, or perform activities related to membership on a U.S. board of directors.

In sum, it is increasingly important for financial services industry employers to establish an internal immigration program to streamline the global mobility of business-critical employees as an essential tool in the cross-border toolkit. These steps can be just as vital to long-term growth as the development of cutting-edge analytics, IT capabilities, and portfolio management techniques.

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