

Public Concern at Work

Suite 301

16 Baldwins Gardens

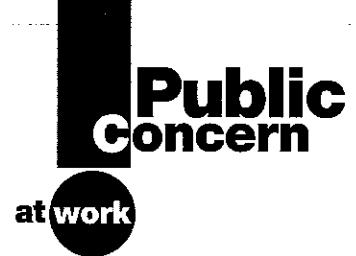
London EC1N 7RJ

Telephone 020 7404 6609

Fax 020 7404 6576

whistle@pcaw.co.uk

www.whistleblowing.org.uk



Chris Hodge
Corporate Governance Unit
Financial Reporting Council
Fifth Floor
Aldwych House
71-91 Aldwych
London WC2B 4HN

1 June 2009

Dear Mr Hodge,

Re: Revised Combined Code on Corporate Governance

We write with reference to the call for evidence for the potential review of the Combined Code on Corporate Governance and are grateful to you for allowing us to respond today, slightly after the original deadline of 29 May 2009.

We would like to take the opportunity to comment on the following issues raised in the review:

- Are there any aspects of good governance practice not currently addressed by the Code or related guidance that should be? (Q.11)
- Views on the respective roles of the chairman, the executive leadership of the company and the non-executive directors (NEDs) (Q.12)

As you are no doubt aware, Public Concern at Work is the independent authority for whistleblowing, and was instrumental in setting up the legislative framework for the protection of whistleblowers in the UK (the Public Interest Disclosure Act 1998). We operate an expert helpline for workers who have a concern about malpractice, whether that be fraud, medical malpractice or other misconduct. In 2008, more than 1500 calls were made to our helpline. We also provide bespoke training and consultancy to public and private entities including Lloyds TSB, the Bank of England and the NHS.

Our approach has always been to emphasise the importance of a good whistleblowing policy being an effective tool in risk management and corporate governance arrangements. To this end, we recently launched the BSI Code of Practice PAS 1998:2008 Whistleblowing Arrangements Code of Practice (BSICoP) in partnership with the British Standard Institution a copy of which is enclosed with the hard copy of this letter and which can also be downloaded for single use at www.pcaw.co.uk/bsi.

Making whistleblowing work

We welcome the fact that the revised Combined Code on Corporate Governance places an obligation on the audit committees of listed companies to review how whistleblowing policies work in practice, and we would like to take the opportunity to build on C.3.4 of the Combined Code by providing some guidance on how audit committees can do this.

With reference to the second issue highlighted above, we would suggest that if there is a revision of the code, there is scope for the invaluable contribution of NEDs to be enhanced in the code with reference in particular to an organisation's whistleblowing arrangements in a number of ways. First, by recognising that NEDs can be an important safety route outside line management for whistleblowers; secondly, such a route may make them more effective in scrutinising those arrangements; and finally, NEDs may have a vital role in challenging executive decisions themselves.

Reviewing whistleblowing arrangements

No matter how well-written a policy, it only works if there is commitment from senior management and the audit committee to ensure that the policy works in practice. Audit committees play a key role in setting an organisation's culture and ensuring that whistleblowing procedures are successful. The BSICoP and the guidance on the Combined Code issued by The Institute of Chartered Accountants for England and Wales (ICAEW)¹, sets out what audit committees ought to look for when reviewing their policies focussing on four main areas²:

- Whether the organisation's policy meets good practice;
- The whistleblowing concerns recorded;
- Employee awareness and trust; and
- Significant adverse incidents

The ICAEW proposed a number of questions the audit committee ought to think about when reviewing the effectiveness of a policy (see p34 BSICoP for the full list), amongst other things audit committees can ask themselves whether:

- Confidentiality issues have been handled effectively;
- Concerns have come to their attention which ought to have been raised earlier through management channels;
- There is evidence of timely and constructive feedback.

The ICAEW does not focus on how concerns are handled, but there is guidance on this in Chapter 5 of the BSICoP which explains how to address concerns. Audit committees may find this helpful when reviewing their whistleblowing arrangements.

If there is to be a review of the Combined Code, we suggest the Financial Reporting Committee recommend the BSICoP as helpful related guidance to audit committees on how to effectively review their whistleblowing arrangements as part of compliance with C.3 of the Code.

¹ Whistleblowing arrangements: Guidance for audit committees, March 2004, ICAEW

² BSI Code of practice p. 33, this can be downloaded for free at www.pcaw.co.uk/bsi

The role of Non Executive Directors (NEDs)

We responded to the Higgs review in 2002 on the role of NEDs. Our comments on this issue are all the more pertinent in light of the aims of this consultation and the recent financial crisis. Our key points for the Higgs review are incorporated into our comments below.

As stated above, because of the unique role NEDs play in the corporate governance arrangements of listed companies, they can also be an effective conduit for whistleblowing concerns. By their nature, they are intended to be independent of the interests of the organisation - their primary objective is, as the Code describes - to *“scrutinise the performance of the management in meeting agreed goals and objectives and monitor the reporting of performance”*³. If for example, the concern relates to a conduct of senior management, or a failure to deal with the concern, an NED being a designated contact on a whistleblowing policy will signal that there is a safe alternative to silence other than an external disclosure, say to the FSA, DBERR or the police.

Information flows and NED oversight

We see much benefit in encouraging companies to nominate an NED as a senior designated contact in a whistleblowing policy. Allowing staff to by-pass the management line and raise their concern to a NED has a number of positive outcomes:

- Board level accountability would be strengthened. This will encourage the requisite leadership on whistleblowing arrangements and serious whistleblowing concerns;
- It is demonstrated to staff that concerns are taken seriously and there are safe alternative routes to speak up if there is a fear of reprisal at line management or senior management level;
- Oversight is increased, encouraging managers to deal well with concerns; and
- The likelihood of staff raising concerns at an early stage will be increased, both detecting and deterring malpractice.

From the point of view of organisational accountability, whistleblowing can and does play a key role in ensuring that the flow of management information works effectively. This is because it provides a failsafe to any actual or perceived monopoly over information, which may exist at any level of any organisation.

As it is under PIDA, whistleblowing by an employee to an NED will be protected as an internal disclosure under section 43C (for which, put simply, the protection applies where there is a genuine and reasonable suspicion of corporate wrongdoing). While it is not our view that NEDs should be the first or second port of call under a company's whistleblowing policy, we do see much merit in companies being encouraged or required to nominate an NED as having a role overseeing the company's whistleblowing arrangements and as a senior designated contact in the policy. We add that such an oversight role would, in our view, readily lend itself to be part of the annual review of internal controls required by the Combined Code. As such this could appropriately be given to the audit committee.

³ FRC Combined Code, p. 5, June 2008

As importantly, such an NED role is likely to encourage the Board to view its whistleblowing arrangements more as a cultural issue than as one of tick-box compliance. This will help the Board not only to assert its accountability down through the company but also to demonstrate it - and also the role and efficacy of its NEDs - to shareholders and other stakeholders.

The mere fact a manager knows that it is safe and accepted for one of his team to raise a concern at a higher level has a number of beneficial outcomes. First, it makes it more likely that he will make himself open and accessible to genuine concerns. Secondly, in a case where the concern may cause him some discomfort, there is a very strong incentive that he deal and is seen to deal with the problem effectively - thus giving good reasons why any temptation to sweep serious wrongdoing under the carpet should be resisted. Thirdly, it is our view that for many people the most powerful deterrent to engaging or condoning serious wrongdoing is the fear and shame of being caught, rather than the legal consequences that may follow. Fourthly, where there is any serious wrongdoing such a culture makes it more likely that it is detected early.

This means that in a case where the concern relates to the conduct of senior management or its failure to deal with a serious matter, the whistleblowing policy will signal that there is a safe alternative to silence other than an external disclosure to, say, the FSA or DBERR. The oversight role of the whistleblowing policy and of concerns raised and addressed under it will ensure that, where necessary, there are sufficiently open and unrestricted information flows and communication channels to the NEDs.

NEDs as whistleblowers

We do not doubt that many NEDs are able to effectively challenge executive decisions and we imagine that in some instances they will have successfully exposed serious problems.

That said, there is both considerable evidence and a strong public perception from instances of serious corporate failure here and abroad that NEDs have not been able to challenge executive decisions or expose serious problems. This may well be because they are unsure whether or how to do anything about their concerns, or because they are fearful of the personal consequences they may suffer if they are seen to rock the boat. The significance of this last reason to the efficacy of NEDs has been recognized by recent calls for an investigation into whether NEDs concerns were silenced at the Royal Bank of Scotland.

We would add here that there is at present a significant lacuna in the law in relation to the protection of NEDs. As such NEDs have little incentive to raise their concerns thus discouraging boardroom whistleblowing. An executive director who is dismissed, forced out or victimised because he justifiably raises a genuine concern about corporate wrongdoing is protected under the Public Interest Disclosure Act. He will receive an award of compensation based on what is just and equitable and on any actual financial losses suffered. However no similar protection is afforded to NEDs, as they are not in law employees or workers.

Although PIDA is part of employment law, it should be noted that the usual ceiling on unfair dismissal awards and requirements for a minimum length of service do not apply. On these issues we would encourage the FRC to work with the DBERR who

remain the responsible department for employment relations and legislation. We recommend increasing the scope of PIDA so that it provides protection for NEDs that is comparable to that enjoyed under PIDA by their executive colleagues. We say comparable because certain PIDA protections - such as the option for a re-employment order - would not be suitable for an NED. In this respect it is important to note that PIDA already covers a wider range of workers than other pieces of employment law and is well suited to protect NEDs. Since commencement the Act has protected consultants, GPs and other professionals who provide services to the NHS and their self-employed status is directly analogous to that of an NED.

Increasing the scope of PIDA is likely to be vital to the success of our previous recommendation to increase the role of NEDs in whistleblowing arrangements.

To summarise we make the following recommendations:

- The BSI code of practice be the basis for recommended guidance to audit committees on how to meet good practice in their whistleblowing arrangements;
- Organisations be encouraged to name one or more NEDs as a senior designated contact in their whistleblowing policies; and
- A review is needed of how the law can be amended to protect and encourage NED whistleblowing.

On a final note, we are in the process of undertaking a survey of employers about their compliance with good practice for their whistleblowing arrangements - we anticipate that some data on this will be available by the end of June. Do let us know if you would like us to send you the key results.

We do hope that our comments prove useful for the review. Please do not hesitate to contact us should you require any further information.

Kind regards,



Cathy James
Acting Director
cj@pcaw.co.uk

