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Treasury Committee evidence session on inventive structures and executive remuneration in the banking sector: Submission from Public Concern at Work

Public Concern at Work (PCaW) is the independent authority on public interest whistleblowing. Promoting individual responsibility and organisational accountability are at the heart of the charity's work and PCaW has been instrumental in putting whistleblowing on the good governance agenda. PCaW's approach has been endorsed by the Nolan Committee on Standards in Public Life. PCaW were asked by MPs to develop the statutory framework for whistleblowing, the Public Interest Disclosure Act 1998 (PIDA), which was widely supported by banks who recognised its value as an early warning system.

PCaW was set up in response to a spate of disasters in the 1980s and 1990s including financial disasters such as the collapse of Barings' Bank, Enron and Worldcom. These scandals resonate with the recent banking crisis and it is appropriate to refresh and renew some of the key messages from the past. What was clear from the inquiries into the above disasters is that staff knew of the risks and were either too scared to speak up or spoke to the wrong people in the wrong way.

PCaW makes the following recommendations:

1. The FSA should look at any compensation agreements brought about under PIDA and assess whether there is any underlying concern that it is appropriate for them to address.
2. That the FSA encourage companies to put in place robust whistleblowing arrangements and avoid compensation agreements sidestepping good practice.
3. The FSA should promote PIDA as a good governance tool and highlight the invalidity of gagging clauses.

FSA oversight of compensation arrangements and settlements.

The recent crisis has also confirmed again that no company is immune from risk and all workplaces are in danger of unknowingly harbouring wrongdoing. When this is rightfully brought to the attention of the organisation the system should support and underpin that information being dealt with properly and appropriately. This includes ensuring that compensation packages do not bury any concern or risk raised that has formed the basis for an employee's departure, something which occurs on a systematic basis at present.

When PIDA was introduced the register of employment claims was public. In 2004 the government reversed this situation and now any claim made under PIDA is shrouded in secrecy. This generates two serious risks: firstly that under this shroud employees are able to effectively extort as large a settlement as possible if they are able to find information that the company would find potentially embarrassing if made public; and secondly, in times when organisations are more sensitive and keen to avoid any adverse publicity, those with a vested interest in the organisation may find it easier to pay off an employee in these circumstances rather than address any underlying wrongdoing. This in turn inhibits proper regulatory oversight and the ability to remedy a wrongdoing before lasting damage is done.

By way of example, two recent pieces of information have confirmed our concern that the above risk is by no means imaginary and has become practice on the ground:

1. On 13 January 2008 the Financial Times carried a report that the former head of Cantor Fitzgerald's spread-betting unit was bringing a claim under the Public

Interest Disclosure Act alleging that he had been dismissed following raising concerns about legal and financial irregularities in the firm. A week later the Financial Times reported that the £15 million dispute had been settled and that the employee had withdrawn his allegations. It is unknown whether there was a serious matter costing investors, consumers and taxpayers hundreds of millions of pounds or whether it was some insignificant matter that the employee had blown up out of all proportion in order to leverage the maximum compensation he could get. Under the current framework – no one knows. Not the general public, jittery investors, nor regulators interested in financial matters in the City, yet there may be a very strong public interest reason that they should know.

2. There is emerging evidence that financial services firms are admitting to settling PIDA cases specifically to avoid scrutiny by the regulator. In a survey of City financial services firms by law firm Osborne Clarke "Whistleblowing – Sword or Shield'[1], 10 percent of respondent firms admitted that a business reason relevant to their decision to settle a whistleblowing claim was "Triggering an FSA investigation", with a smaller percentage citing "Concession that there may have been regulatory breaches".

Firms are freely admitting that when a concern is raised internally, one of the reasons they will attempt to settle it is to avoid any investigation or action on the part of the regulator and that this includes cases where the firms are aware they have been guilty of a regulatory breach. That such a brazen answer was given by respondents indicates an alarmingly ingrained culture and requires review.

In the handful of PIDA claims that enter the public sphere by way of a public hearing and are not buried in settlement, we would recommend the FSA look at the underlying concern to the claim to assess if there is any substance to it and if so, that any malpractice has been addressed. The FSA may further wish to consider whether financial institutions should be required to report to the FSA any claims brought against them under PIDA so that any underlying wrongdoing engages the appropriate regulatory oversight.

[1] Osborne Clarke October 2008

Good practice around the disclosure and transparency of compensation arrangements within financial institutions

The terms on which an employee will continue or leave employment is a matter for them. However, in the absence of any public register or other source of information the FSA may want to consider how to address the issue that most organisations will be inclined to settle out of court, or prior to any claim, to avoid any damaging publicity. The FSA may want to consider how companies communicate the underlying reasons behind outgoing executives and good practice on the disclosure and transparency of any such arrangements within financial institutions is imperative.

Gagging clauses

As part of the process of increasing proper regulatory oversight the FSA should embrace useful legislation and promote PIDA as a useful good governance tool and may want to ensure that employees are properly aware that gagging clauses within compensation packages are invalid under PIDA and cannot override a protected disclosure. This means, for instance, that a firm cannot impose a gagging clause, which would prevent an employee from raising a serious concern with the FSA. Clear guidance from the FSA will not only encourage ex-employees to communicate with their regulator where appropriate but it will additionally discourage any employer that might attempt place onerous clauses in compromise agreements that might bury serious concerns in settlement.

If you require any further information on this issue please contact myself or Francesca West (fw@pcaw.co.uk), Senior Policy Officer, via email or on the number above.

Yours sincerely,

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