COVINGTON

Rules Requiring UK Financial Institutions to Appoint "Whistleblower Champions" Enter Into Force

9 March 2016

Financial Services

The UK Financial Conduct Authority ("FCA") and the UK Prudential Regulatory Authority ("PRA") issued new rules in October 2015 that require certain UK-regulated financial institutions to implement whistleblower procedures and protections. One aspect of the new rules, obliging covered financial institutions to appoint "whistleblower champions", entered into force on 7 March 2016. This client alert provides further information on the new rules.

What Is the Background to the New Rules?

In June 2013, the Parliamentary Commission on Banking Standards published a report, *Changing banking for good*, which concluded that "[t]he financial crisis, and multiple conduct failures, [had] exposed serious flaws in governance" at banks. The Commission noted that "[p]oor governance and controls are illustrated by the rarity of whistle-blowing, either within or beyond the firm, even where, such as in the case of Libor manipulation, prolonged and blatant misconduct has been evident." To address these concerns, the Commission made various recommendations, including a suggestion that banks should appoint a named non-executive director "to oversee fair and effective whistle-blowing procedures, and to be held accountable when an individual suffers detriment in consequence of blowing the whistle."

In light of the Commission's recommendation, the FCA and the PRA issued a consultation paper in February 2015, which proposed the introduction of various measures to improve financial institutions' whistleblower procedures and protections. Following the consultation, the FCA and PRA published the new rules in October 2015. Announcing the publication of the rules, Tracey McDermott, the acting FCA chief executive, commented that the rules "are designed to build on and formalise examples of good practice already found in parts of the financial services industry and aim to encourage a culture in which individuals working in the industry feel comfortable raising concerns and challenge poor practice and behaviour."

Who Is Affected by the New Rules?

The new rules apply to "Relevant Firms", namely:

- UK deposit-takers with assets of £250 million or more, including banks, building societies, and credit unions;
- PRA-designated investment firms; and
- insurance and reinsurance firms within the scope of the Solvency II Directive (2009/138/EC), as well as the Society of Lloyd's and managing agents.

The rules also have effect as non-binding guidance for other FCA-regulated firms.

The FCA intends to consult on whether the new rules should extend to the UK branches of foreign financial institutions. The FCA also has indicated that it may, in the future, consider whether similar requirements should be applied more widely to other regulated firms, such as stockbrokers, mortgage brokers, insurance brokers, investment firms and consumer credit firms.

What Steps Do the New Rules Require?

The rules that entered into force on 7 March 2016 require "Relevant Firms" (as defined above) to appoint a "whistleblowers champion" who will be responsible for "ensuring and overseeing the integrity, independence and effectiveness of the firm's policies and procedures on whistleblowing […] including those policies and procedures intended to protect whistleblowers from being victimised because they have disclosed reportable concerns."

The rules state that a whistleblower champion "should have a level of authority and independence within the firm and access to resources (including access to independent legal advice and training) and information sufficient to enable him to carry out that responsibility." The FCA has noted that it will generally expect firms to appoint non-executive directors as their whistleblower champions, although firms without a non-executive director are not expected to appoint one solely for this purpose.

In addition, the rules impose several detailed requirements regarding whistleblower procedures and protections, all of which will enter into force on 7 September 2016. This includes, but is not limited to, the following obligations, the implementation of which the appointed whistleblower champion will be responsible for overseeing:

- **Relevant Firms must establish, implement and maintain appropriate and effective arrangements for the disclosure of "reportable concerns" by whistleblowers.** The term "reportable concern" is defined broadly to include, for example, breaches of internal policies or procedures, or other behaviours that are likely to harm the reputation or financial well-being of a Relevant Firm. It is not limited to regulatory matters or criminal offences, and it applies to disclosures by employees and third parties alike. The rules describe the minimum requirements of "appropriate and effective arrangements". For example, Relevant Firms must:
  - allow disclosures to be made through a range of communications methods;
  - effectively handle requests for confidentiality by whistleblowers and anonymous whistleblowing reports;
  - ensure the effective assessment and escalation of reportable concerns, including to regulators in appropriate circumstances (the FCA has noted, in this regard, that while not all disclosures will ultimately warrant formal investigation, the FCA would expect "due consideration to be given to each case and for this to be recorded");
  - adopt reasonable measures to protect whistleblowers from victimisation;
  - implement written procedures that are readily available to UK-based employees outlining the firm's whistleblowing system (Relevant Firms are not, however, under an obligation to promote their whistleblowing system to third parties);
  - provide feedback to whistleblowers about reportable concerns, where feasible and appropriate;

- prepare and maintain appropriate records of reportable concerns, and how those reportable concerns were handled;
- require regular reporting on the operation and effectiveness of whistleblowing systems to the firm's governing body, at least on an annual basis; and
- promptly report to the FCA any claim lost before an employment tribunal where the claimant successfully based all or part of their claim on either detriment suffered as a result of making a "protected disclosure" in breach of section 47B of the Employment Rights Act 1996, or being unfairly dismissed under section 103A of the Employment Rights Act 1996. The term "protected disclosure" is defined more narrowly than "reportable concerns", to encompass disclosures by workers and employees who qualify for protection under certain UK employment laws.

- **Relevant Firms must provide appropriate training to UK-based employees, all managers of UK-based employees wherever the managers are based, and all employees responsible for whistleblowing arrangements.** For example, Relevant Firms should inform all UK-based employees about the mechanisms for disclosing reportable concerns, provide examples of the events that might give rise to reportable concerns, and offer information about sources of external support, such as whistleblowing charities. In addition, Relevant Firms must ensure that their tied agents and appointed representatives inform any UK workers about their ability to make protected disclosures to the FCA.
- **Relevant Firms must communicate to UK-based employees that they may disclose reportable concerns to the FCA or the PRA, as well as the methods for doing so.** In particular, Relevant Firms must emphasise that reporting to external regulators is not conditional upon a report first being made using internal procedures, and that internal and external reporting mechanisms may be used simultaneously or consecutively, in any order. This must be communicated in an employee handbook or an equivalent document.
- **Relevant Firms must not request warranties from their workers that require the sharing of information about protected disclosures.** In particular, workers should not be required to tell Relevant Firms about any protected disclosures that they may have made, or to warrant that they have no knowledge of any information that could form the basis of a protected disclosure. Neither are Relevant Firms permitted to adopt any measures that are intended to prevent workers from making protected disclosures.
- **Relevant Firms must include a term in any settlement agreement with a worker that makes clear that nothing in the agreement prevents the worker from making a protected disclosure**. The rules include suggested wording that could be included in settlement agreements.
- **No employee reporting obligations.** Although the foregoing standards ensure a process for covered persons to issue whistleblowing reports, the FCA and the PRA have made clear that the new rules do not impose any affirmative obligation on staff to file reports.

Conclusion

As noted above, the FCA recognised when it published the rules last year that they "build on and formalise examples of good practice already found in parts of the financial services industry." Many regulated financial institutions will already have in place policies and procedures that meet many of the requirements imposed by the new rules.

For firms that have not yet developed formal whistleblowing programs, the new rules introduce a set of baseline standards, supplementing other pre-existing guidelines that the UK authorities have issued previously in other contexts. This includes, for example, the *Whistleblowing: Guidance for Employers and Code of Practice*, published by the UK Department for Business, Innovation and Skills in March 2015, which sets out general whistleblowing policy standards for UK industry, many of which parallel the new FCA and PRA rules.

Many whistleblowers already benefit from legal protections for public interest, "protected disclosures" under the Public Interest Disclosure Act 1998, and the Employment Rights Act 1996 has for many years prohibited victimisation or dismissal of whistleblowers who made certain categories of protected disclosures. The new rules do not alter those protections, but do require the adoption of measures that tie into those laws. In particular, the mandatory training requirement and the need to adopt measures to protect confidential disclosures may provide an impetus for more whistleblowers to come forward, as well as the reassurance that protected disclosures will be treated in confidence.

There is evidence to suggest that, even prior to the introduction of the new rules, whistleblowing is becoming a more common practice in the UK. The most recent FCA annual report, for example, shows that there has been a marked increase in the number of whistleblowing cases handled by the FCA or its predecessor, the Financial Services Authority, in the past several years. There were just 138 whistleblowing cases in 2007/8. By 2014/15, the figure had risen to 1,340 cases.

Similar trends are reported elsewhere. In the United States, for instance, the Securities and Exchange Commission ("SEC") reports an increase from 334 whistleblower reports in FY 2011 to 3,923 whistleblower reports in FY 2015, with 72 reports made by UK-based whistleblowers. However, in contrast to the UK position, the US trend has been driven, at least in part, by generous "bounty-hunter" provisions that grant whistleblowers significant financial rewards for tips that result in successful enforcement actions. In FY 2015 alone, the SEC paid more than $37 million under its Dodd-Frank whistleblower programme.

The UK Government committed in its December 2014 Anti-Corruption Plan to "explore whether there is more that can be done to incentivise and support whistleblowers in cases of bribery and corruption." However, the FCA and PRA have shown no appetite to introduce a comparable incentive scheme in the UK, having announced in July 2014 that "introducing incentives for whistleblowers would be unlikely to increase the number or quality of the disclosures." For now, at least, UK regulators appear to be focused on non-financial measures that can encourage whistleblowing — as illustrated by the new rules that entered into force earlier this week.

If you have any questions concerning the material discussed in this client alert, please contact any the following members of our firm's UK financial regulatory, white collar, and employment law practices:

UK Financial Regulatory / White Collar Practice

Robert Amaee	+44 20 7067 2139	ramaee@cov.com
Sarah Crowder	+44 20 7067 2393	scrowder@cov.com
Charlotte Hill	+44 20 7067 2190	chill@cov.com
David Lorello	+44 20 7067 2012	dlorello@cov.com
Ian Redfearn	+44 20 7067 2116	iredfearn@cov.com

UK Employment Practice

Christopher Bracebridge	+44 20 7067 2063	cbracebridge@cov.com
Christopher Walter	+44 20 7067 2061	cwalter@cov.com