Ethics Reporting for Compliance and Beyond

Jane Garthson

The front line knows best what actually happens in workplaces, and honest workers are frequently concerned about the practices they see around them. Yet workers rarely tell their company. Why? Because they quite rightly are not sure who to trust, and whether they will be safe.

This article looks at the criteria you might consider in deciding how to encourage ethics reporting in your organization, regardless of any legal imperative that applies to you. The title does not mention “whistle-blowing” or “ethics hotlines” because I have learned that ethics reporting systems are evolving to meet employee and company needs. Everyone is better off if systems are available to employees to get advice on their options, learn more, and to make positive suggestions, rather than just reporting fraud and other problems.

Ethics reporting services across Canada, such as ClearView Strategic Partners Inc of Toronto and ConfidenceLine of Calgary, say that more and more companies are improving the ethics reporting systems they make available to employees. In response to legal changes and media attention, companies are increasingly responsible for knowing what is happening and taking corrective action. Senior executives signing off on corporate information and Audit Committees charged with oversight both need reassurance about whether or not their internal controls are working, and whether they can trust the numbers. Their credibility is on the line. If fraud, environmental violations, sexual harassment and / or other problems are occurring without their knowledge, they may face pressure to explain why they did not have better ethics reporting systems in place. Even if the problems are not serious enough for police, regulator or media attention, they may be significantly harming productivity and shareholder returns.

The legal requirement that does apply to many Canadian companies is generally called Bill 198. It is provincial legislation related to the Ontario Securities Commission. The specific statute, Keeping the Promise for a Strong Economy Act (Budget Measures), 2002, has a broad scope affecting companies seeking to be listed on the TSE. Bill 198 is not explicit about ethics reporting, but it has lead to a regulatory requirement respecting Audit Committees, which states the following, in section 2.3.(7). An audit committee must establish procedures for:

a) The receipt, retention and treatment of complaints received by the issuer regarding accounting, internal accounting controls, or auditing matters; and

b) The confidential, anonymous submission by employees of the issuer of concerns regarding questionable accounting or auditing matters.

Bill 198 came into force on March 30, 2004, with a compliance date no later than July 1, 2005. By that time, I believe, relatively few organizations were set up for employee complaint anonymity, regardless of how effective they perceived their employee communications channels to be. Employees unsure about whom to trust may fear that their handwriting or voice on the phone might be identified. Computer-literate employees in addition know that e-mails are stored, traceable and accessible to management via IT systems administrators. So it is likely that many organizations were not ready for compliance unless they had already acted, perhaps because of U.S. operations coming under Sarbanes-Oxley section 301 requirements.

In any case, executives sensitive to disclosure requirements, and the impact of signing off on corporate reports, want to ensure that they learn of problems as early as possible. Most realized that employees were justifiably reluctant to blow the whistle without protection from reprisal. Executives in government and nonprofits, often subject to greater scrutiny, also wanted better information channels.

What then do companies want and need in a high quality ethics reporting system that goes beyond legal requirements, such as those in Bill 198 and SOX? A key need is enhanced, multilingual, secure, and reliable Employee Complaint Reporting systems, with both internal and external reporting channels options. It should enable employees to choose whom to trust by allowing them to speak with a live person, to report concerns over the Internet. An Employee Complaint Reporting system should, I suggest, have the following properties:

- Confidentiality & Trustworthiness: it should include ways for employees to ensure that senior individuals they think might be involved do not see their complaint

- A complete, tamper-proof audit trail

- Strongly linked to the company's Code of Conduct / Ethics program, company policies and processes, including the ability to handle multinational operations; but data storage in Canada. (If stored in USA, it would be subject to U.S. laws such as the Patriot Act)

- Robustness (minimal to no down time; business continuity plan)

- Reliability in gathering and distributing information, using a highly secure, up-to-date technology with logical and physical intrusion detection built into the systems design

- Integrated complaint monitoring and case management technology

- Potential for ongoing communication with complainants to seek clarifications, let them add additional occurrences and learn the resolution of their complaint

- Value for money proposition

There is no legal requirement to use a third party, but companies may not find it cost-effective to build secure enough systems and assign enough staff internally. Employees will bring forward complaints within a company, but not usually those where they fear reprisals. Companies based in major cities may also choose a provider in close physical proximity to facilitate building a relationship, but many will not have that choice. They might also look at related services they can get from the same provider, such as investigative services, program communications assistance or corporate governance.

Bell faced that choice, and approximately a year ago added an outsourced option through ClearView Strategic Partners Inc. David Wolinsky, Bell Canada's Assistant General Counsel, said employees are still learning about the ClearView option. As Bell has had an internally managed Help Line in place for many years, its employees are now perhaps more familiar with an internal system that lets them speak to a live person. That choice will remain open.

Bell has built a strong ethics framework that predates Sarbanes-Oxley, including its long established Help Line, a detailed Code of Business Conduct, ethics e-training for employees and a reporting tool for both employees and outside persons to report issues relating to accounting irregularities, such as violations of federal or provincial laws, misappropriation of the company's property or fraud. However, it wanted to make sure everyone was comfortable bringing new issues forward, so Bell could address them quickly and effectively. That meant giving employees a completely anonymous method for raising concerns without fear of reprisals.

Wolinsky explained that Bell's preference was for people to call for advice on how to apply the Code of Business Conduct and the company's various policies, rules and procedures to their own action. Bell's "ask before acting" philosophy is consistent with leading edge integrity organizations. The calls may therefore cover a wide range of issues or activities such as whether or not a particular second job would be give rise to a conflict of interest, in addition to identifying behavior that could be contrary to the Code.

Individual employees in any organization are really helped by such systems, designed to be there for them when normal channels are not working or they just want to understand a situation better before using normal channels. Employees can report sensitive work-related matters like theft, harassment and lack of workplace safety, and see actions taken. Staff frustrated with their own chain of command can even take suggestions for product and process improvements forward. In nonprofits, volunteers could be given access to the same system.

Employees may not see every problem resolved to their satisfaction. If however the tools are in place for them to be heard, they are made aware of the outcome of any review process undertaken in response to their concerns, and they can be contacted to provide additional information (when needed), then they are likely to consider the systems in place to be legitimate avenues for their concerns. Tangible outcomes that some may have seen in serious cases include internal or external audits, investigations by security personnel or police and even dismissal of someone who may be abusing their authority. More often, they might see a change to corporate policy, such as a clarification of acceptable procurement practices.

It may matter more what they do *not* see – their company in the news for unethical behaviour, or a photo of their CEO in handcuffs. David Wolinsky said that Bell Canada takes pride in being recognized as an ethical company, so it is very important to have all employees take the Code of Business Conduct to heart. It gives the company a chance to avoid serious problems.

Why are companies going beyond their legal requirements? Phil Enright of ClearView Strategic Partners said that his clients were passionate about ethics and wanted to help everyone do the right thing, rather than catch the few doing wrong. A focus on the positive, and an approach based on learning, would engage and involve far more employees than any whistle-blowing system.

Ray Renaud of ConfidenceLine in Calgary acknowledged that many companies started with compliance, but quickly saw the potential for productivity increases and for aligning proper corporate behaviour with policies. His services help companies incorporate their core values into every level of their business. He strongly believes in linking an ethics reporting system directly to the Code of Conduct.

However, companies may need some hard and negative facts to prompt them to act. Research based on 1,134 cases of occupational fraud cited in the 2006 report of the Association of Certified Fraud Examiners on Occupational Fraud and Abuse showed that:

- Occupational frauds are more likely to be detected by a tip than by other means such as internal audits, external audits or internal controls
- Organizations with anonymous fraud hotlines suffered median losses one-half of those of without hotlines
- Certified Fraud Examiners estimate that a typical organization loses 5% of its annual revenue to fraud (the report stressed this was not backed up by hard numbers)
- Frauds committed by owners or executives caused a median loss 13 times as large as the median loss caused by non-management employees
- 30% of occupational frauds were committed by accounting department employees
- 20% were committed by upper management and executives
- Less than 8% of perpetrators had prior convictions

Accounting department employees, I feel, are also the first to know about many of the frauds, and may feel very discouraged when abuses are condoned over long periods. They could be the best users of ethics reporting systems!

Perhaps these figures, and other details from the report, will help convince any members of management or the audit committee who still doubt the value of a good ethics reporting system. If not, consider the value proposition involved just in terms of identifying a problem early, while it is small, instead of after it blows up. Even better, consider whether employees who can easily ask for guidance will do the right thing first time. We could even hope that this approach could change senior management behaviour too, and prevent behaviour that costs the company and our economy so dearly.