

# Whistleblower Policy – a means to better Corporate Governance

Shweta Shankar, SCMHRD

## KEYWORDS

Whistle blowing,  
Corporate Governance,  
Business Ethics,  
Organization Culture

## ABSTRACT

In today's era of globalization and technological advancement, one can easily say without doubt that corruption is one of the biggest evils plaguing our society. Corruption has become a way of life in many societies and particularly so in India. Studies have proved that GDP growth is inversely proportional to growth in corruption. Higher corruption leads to a lower GDP and vice versa. It is imperative to bring back that golden era where people were conscientious and businesses, honest and honorable.

Though many systems and processes are in place, legal and otherwise to curb corruption, they have not been able to achieve the required measure of success. However a new method of curbing corruption by way of “whistle-blowing” has been able to achieve some success in controlling corruption. Whistle blowing can be defined as the act exposing wrongdoing within an organization.

The whistle blower policy has rightly been recognized as one of the basic norms of corporate governance by most countries across the world. This essay deals with how whistle blowing is incorporated into corporate governance, talks about some major whistle blowing incidents and discusses about some initiatives that can be taken to enhance the effectiveness of whistle blowing.

## 1.0 INTRODUCTION

In a developing country like India, we find that new firms and organizations crop up by the minute. The legal procedures make it relatively easy for a person to set up an organization in India. We find that most of the big companies face problems that are more internal rather than external. Corruption and fraud act as malaises and cripple the effective functioning of big companies.

An example in case is the shocking incident at Satyam Computer Services, where Satyam's the then Chairman Mr. Ramalinga Raju took responsibility for broad accounting improprieties that overstated the company's revenues and profits and reported a cash holding of approximately \$1.04 billion that simply did not exist.[1]

Whistle blowing if encouraged could help in bringing to light such malpractices and process frauds at a very nascent stage itself.

## 2.0 WHISTLE BLOWING

Whistle blowing can be defined “as the act exposing wrongdoing within an organization to internal or external parties.” The wrongdoing can include theft, burglary, violation of safety norms, embezzlement, financial fraud etc. Whistle blowers may disclose the fraud internally, i.e. to someone within that organization or externally, i.e. to someone outside the organization like law enforcement agencies, media, public etc. Sometimes, monetary

incentives are given to encourage external whistle blowing.

The term 'whistle blower' comes from the act of a referee blowing a whistle to indicate foul play. This term was coined by the US activist Ralph Nader in the early 1970s to avoid referees being called negatively as 'snitches' and 'informers'. Whistle blowing has the potential to transform the culture of an organization positively. Whistle blowing policies can greatly help organizations that firmly believe in honest and fair trade practices.

## 3.0 WHAT IS CORPORATE GOVERNANCE?

Corporate governance is the system or structure by which organizations are managed or governed. It is the responsibility of the Board of Directors which is appointed by the shareholders of the company to ensure that the company has a sound and transparent governance system. The company and the board of directors are accountable to the shareholders. The decisions and rules of the board are subject to laws, regulations and the shareholders' opinion in meetings.

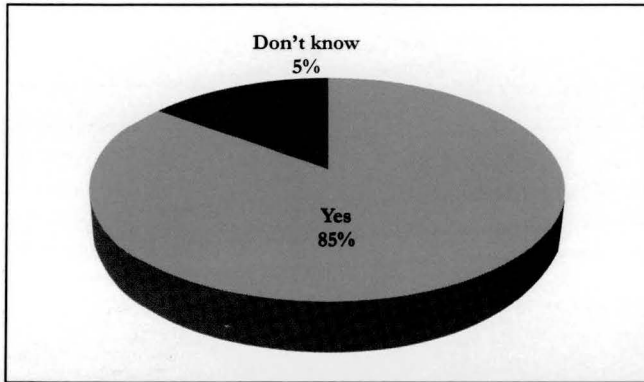
The well-being of the company is the well-being of its shareholders, and the directors are accountable for this. This is clearly spelt out in the Companies Act 1956 through its various sections and in many other legal doctrines. [2]

#### 4.0 RESULTS OF PRIMARY RESEARCH

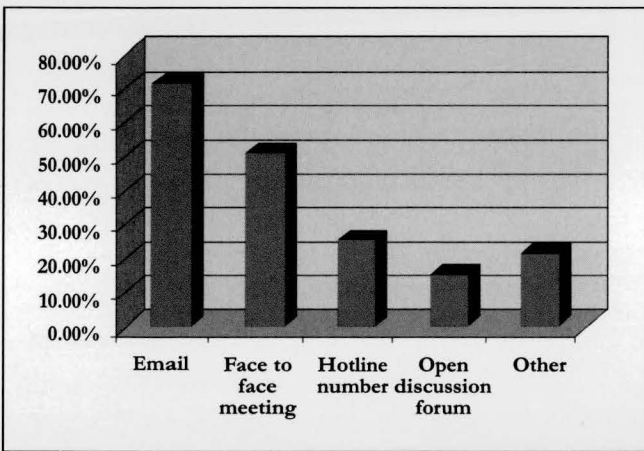
**Methodology:** An online survey was conducted in Dec, 2012. Eighty working professionals from India completed the online questionnaire. The targeted sample profile spanned across professionals employed in various organizations across sectors. Respondents were asked to respond to a set of core questions on corporate grievance reporting mechanisms.

The results of the survey are as follows:

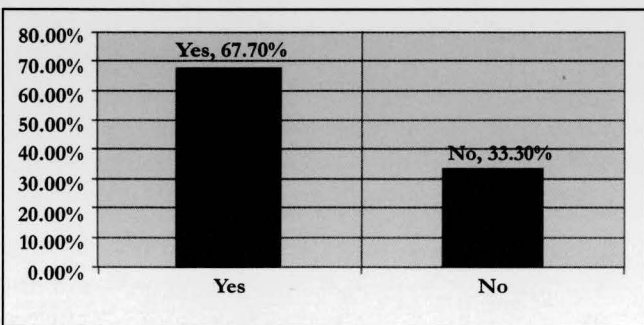
Q1 - Does your organization have a formal mechanism in place to report complaints/misconducts?



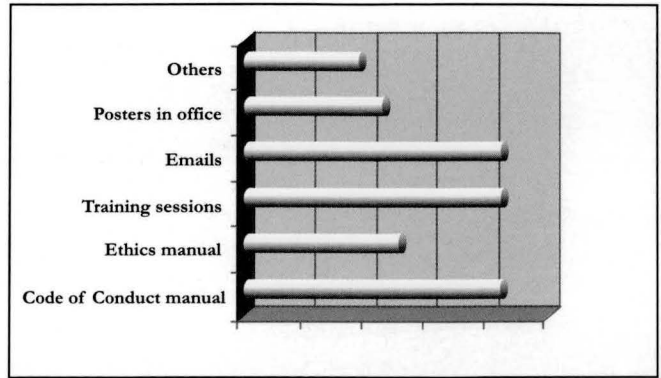
Q2 - What are the channels available in the system referred to in Q1, used to report any complaints/misconduct/ grievances?



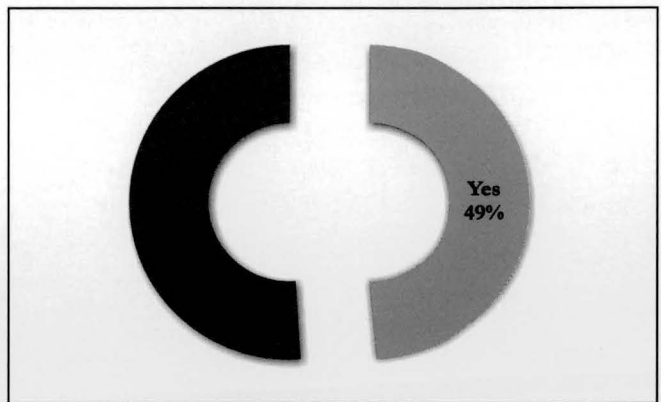
Q3 - Was the person's identity kept anonymous while reporting a grievance through the mechanism specified in Q1?



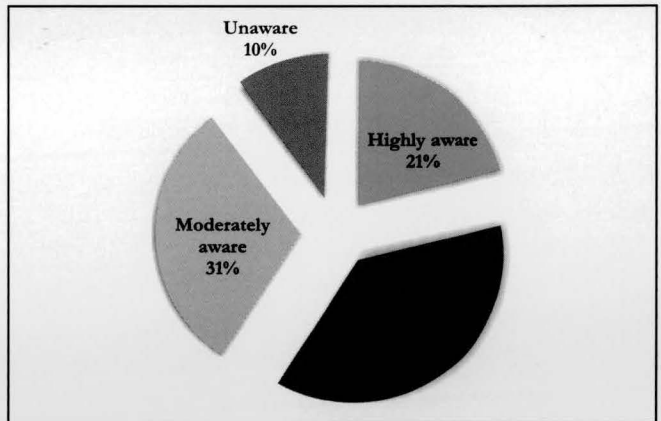
Q4 - How are employees informed of the existence of this system?



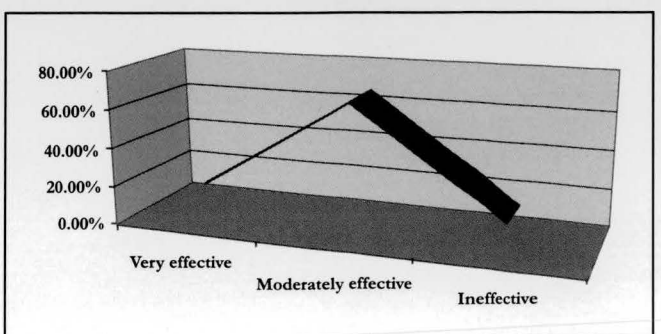
Q5 - Does your organization conduct training sessions for the employees regarding the use of this mechanism?



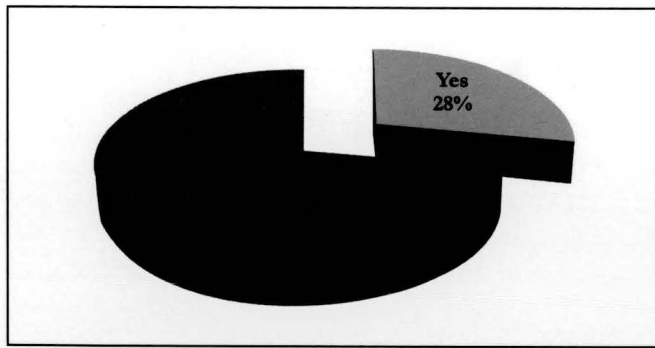
Q6 - How aware are employees of the existence of the mechanism specified in Q1?



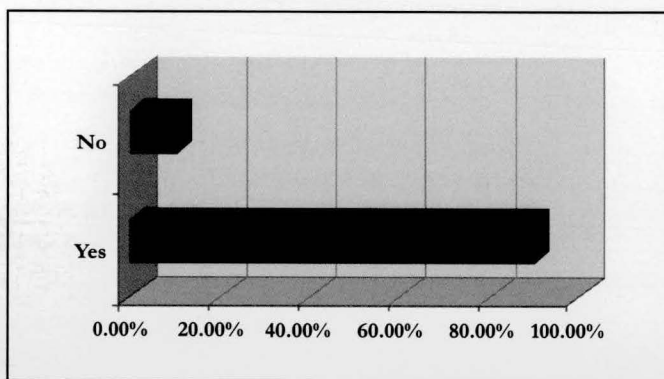
Q7 - According to you, how efficient is this mechanism?



Q8 - Has there been an instance, where you were aware of some wrongdoing but you did not report it to the concerned person in your organization?



Q9 - Do you feel the need to have a formal mechanism to report misconducts/grievances?



## 5.0 SURVEY RESULTS OF SECONDARY RESEARCH

According to a survey done by India Forensic Consultancy Services [3], Pune, at least 1200 out of 4867 companies listed on the Bombay Stock Exchange and 1288 companies listed on the National Stock Exchange as on March 31, 2007, including about 30 companies listed in the benchmark Sensex and Nifty indices had fudged their financial reports.

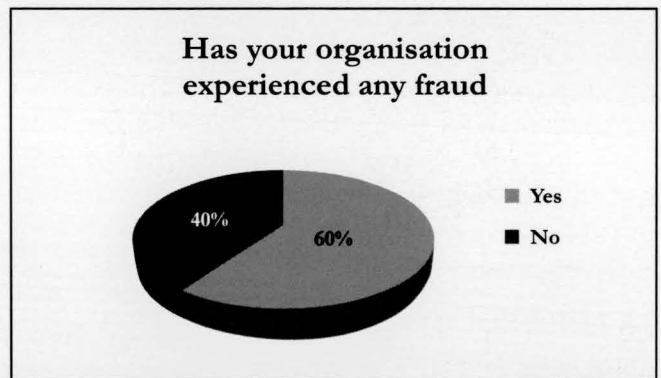
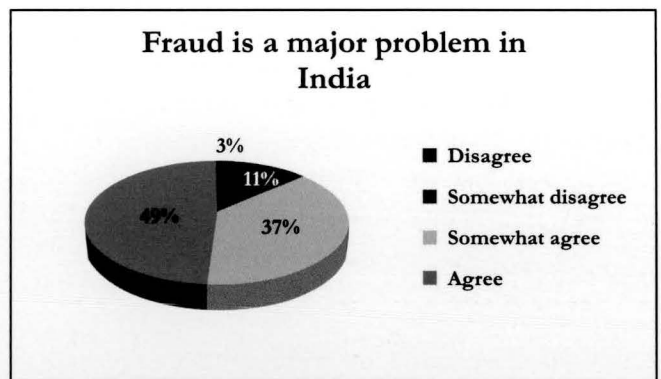
The study investigated 11 sectors, viz. real estate, retail, banking, manufacturing, insurance, public sector undertakings, mutual funds, transport and warehousing, media and communications, oil and gas and information technology.

The manufacturing sector, which contributes about 28 per cent of India's gross domestic product, is the one most affected with fraud mainly due to the peculiar nature of the business and the procedural complexities inherent in this sector. Real estate and public sector undertakings came second.

The motive for committing accounting statement frauds, according to 73 per cent of 340 chartered accountants who were respondents to the findings of the study, was to exceed expectations of stock market analysts. Other reasons for the fraud include credit-hungry firms manipulating application data in order to qualify

for credit.

The results obtained from the KPMG India Fraud Survey Report 2008[4], are as follows:



- Nearly half of the respondents (49 percent) believed that they have communication channels in place for anonymous reporting of suspected fraud and misconduct. However, only 15 percent of the frauds were detected through anonymous reporting. This indicates that even if organizations believe that they have a good reporting mechanism, the employees may not necessarily feel safe in reporting misconduct.

## 6.0 ROLE OF WHISTLE BLOWING IN ENHANCING CORPORATE GOVERNANCE

By analyzing the KPMG report, we realize that a majority of the employees feel that most white collar crimes happen from within an organization than from an external body. Organizations are huge and it is difficult for just a few people to ensure that fair and honest practices exist across functions in the organization.

The best and most efficient method to ensure that fraudulent happenings are exposed is by involving the employees of the organization. The people working in the company can be encouraged to report crime, malpractices or theft that happens in their department to an autonomous body which functions primarily for this purpose.

Let us now look at the type of people who become whistle blowers. Interestingly, research shows that whistle blowers are not unhappy or disgruntled employees. Rather they seem to score high on conscience. They think



ethically and find it difficult to adhere to unethical practices. In a way these people put the interests of others and the society above their own as they do realize that by reporting fraudulent activities, they are putting their own selves and their careers at risk. But history has shown that whistle blowers are usually ostracized, punished or humiliated. Many of them even lose their jobs.

Punishment of whistle blowers has now become a serious issue and we find that most of these whistle blowers are either suspended, dismissed, fired, humiliated, harassed or demoted. In some cases, it takes the form of extreme employee bullying wherein an entire department turns against a single individual.

This is the main reason that forces normal employees to turn a blind eye towards corporate crime that happens right under their noses. People fear for themselves, their jobs and their families. So when they see that they do not get any protection for exposing crime, they refrain from reporting fraud or corruption. In a country like India which ranks 94 out of 176 countries in the 2012 Corruption Perceptions Index, created by Transparency International[5], this definitely does not augur well for our future.

### 7.0 THE PROCESS OF WHISTLE BLOWING

The process of whistle blowing essentially has five basic steps as are depicted in the Figure below:(Figure1)

### 8.0 FAMOUS CORPORATE WHISTLE BLOWERS

A hero of the present times, Julian Assange, founder and editor-in-chief of Wiki Leaks has more than 1.2 million individual leaks to his name.

W. Mark Felt also known as Deep Throat remains the most famous whistle blower of all times. Back in 1972, he discovered President Nixon's illegal involvement in the dealings at the Watergate Hotel. He leaked this to the Washington Post and this subsequently led to the resignation of President Nixon and arrest of the then White House Chief of Staff.

Another famous whistle blower is Linda Tripp who leaked to the press that Monica Lewinsky had committed a perjury in concealing her relationship with President Bill Clinton.

In the corporate sector, Sherron Watkins, the former vice president of Enron reported the illegal fraudulent accounting practices in her company.

And more famously we all know the story of Cynthia Cooper, former Vice President of Internal Audit at WorldCom who exposed the hundreds of false accounting entries in the company's financial statements. Her book 'Extraordinary Circumstances: The Journey of a Corporate Whistle blower' chronicles the struggle she underwent to expose this massive fraud.[6]

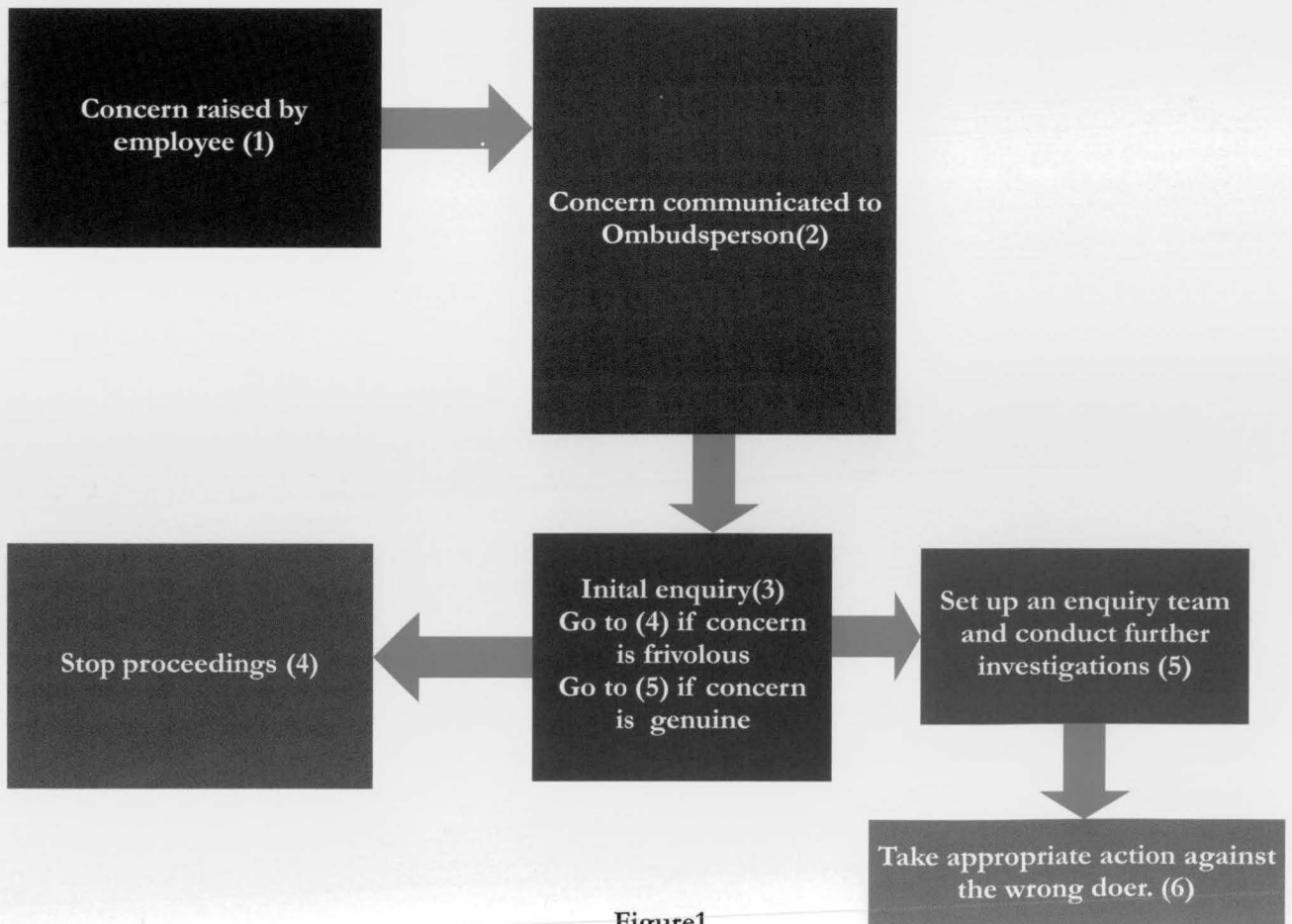


Figure1

## 9.0 BUT, WHAT REALLY HAPPENS TO THESE WHISTLE BLOWERS?

Reality is shocking and sometimes stranger than fiction. Let us look at some cases.

- Closer home, we have Manjunath Shanmughan, an IIM graduate who was employed with the Indian Oil Corporation Ltd [IOCL], who was murdered on 19-Nov-2005 for sealing a corrupt petrol station in Uttar Pradesh.
- Satyendra Dubey, an IIT graduate who was employed with the Nation Highway Authority of India [NHAI], wrote an open letter to the then Prime Minister Atal Bihari Vajpayee exposing the unfair dealings in highway constructions. He was later found murdered on 27-Nov-2003.
- Myron Mehlman, who was employed with Mobil, found that the gasoline being sold by the company in Japan contained benzene in excess of 5% and this was dangerous. He was subsequently fired in 1999.

From this, it is pretty evident that strong whistle blower protection acts need to be formulated and acted upon.

## 10.0 THE INDIAN WHISTLE BLOWERS POLICY'S LEGAL JOURNEY

Laws and regulations put together for the legal protection of whistleblowers is termed as 'whistleblower's protection'. On August 26, 2010 this bill was introduced in the Parliament and was passed by the Lok Sabha on December 27, 2011. It was introduced in the Rajya Sabha on March 29, 2012 and is currently pending there.

## 11.0 AREAS WHERE WHISTLE BLOWING CAN BECOME MORE EFFECTIVE

No company is immune to crime or fraud and we see that increasingly most companies are adopting a whistle blower mechanism to encourage employees to report crime. I believe that any organization, from private to non-profit, across industries will benefit from adopting anonymous reporting mechanisms. It is an important initiative for organizations that wish to improve their corporate governance, risk mitigation measures and ensure good compliance to policies and ethics.

Whistle blowing can prove to be effective in all types of organizations.

- For whistle blowing to be more effective, it is very important for the company to enlist the support of its top management. According to the trickle-down effect, this is the best way to communicate to the employees that the company actually believes in whistle blowing.
- The whistle blowing policy has to be very clear and effective communication of the policy to the users has to take place. This can be done by frequently sending

e-mails and dedicating a hot line number purely for this purpose.

- Users should also be given training sessions on the types of corporate crimes that can take place, how to spot crime and how to report it. In many cases it is found that employees are not trained enough to be able to spot crime that happens right before their eyes.
- These trainings have to be conducted periodically and it has to be given to employees of all ranks – starting from the house cleaning staff to the top management officials. Awareness can also be raised by conducting video making or poster designing contests with 'wiping corporate crime' as the theme. This will generate a lot of interest among the employees and is sure to catch the attention of many.
- Once a concern/complaint has been lodged with the whistle blowing committee, it is essential that an initial inquiry is made at the earliest. If the concern turns out to be genuine, then a detailed investigation has to be carried out and the wrong doers have to be awarded appropriate punishment.

Most importantly, it is imperative to reward the whistle blower. This can be done by publicly acknowledging his act and giving him incentives/prizes. But in some cases, the whistle blower would prefer to not reveal his identity; these shall be treated as exceptions.

## 12.0 WHEN IS WHISTLE BLOWING ETHICAL?

Whistle blowing is considered to be ethical under the following 5 conditions[7]:

1. When the company, through a product or decision can cause considerable harm to the public, or break existing laws.
2. When the employee identifies a serious threat of harm, he/ she must report it.
3. When the employee's immediate supervisor does not act, the employee should exhaust the internal procedures and chain of command to the board of directors.
4. The employee must have documented evidence that is convincing to a reasonable, impartial observer that his/her view of the situation is correct.
5. The employee must have valid reasons to believe that revealing the wrongdoing to the public shall result in changes necessary to remedy the situation.

On the other hand, if there is evidence that the employee is motivated by the opportunity for financial gain or media attention, or that the employee is carrying out some personal vendetta against the company; then the legitimacy of the act of whistle-blowing must be questioned.

### 13.0 VOLUNTARY INITIATIVES BY COMPANIES

Companies can do a lot of things in this regard. As whistle blowing primarily helps in better and more efficient functioning of a company, it is in the best interests of the company that it encourages whistle blowing by setting up appropriate mechanisms.

According to a study performed by Price Waterhouse Coopers in 2011, every company can follow a basic five step model (given below) for encouraging effective whistle blowing from its employees.

#### 1 Gaining top level commitment-

This is the first and the most important step in creating an efficient whistle blower policy. There should be a trickle-down effect and that is possible only if the top management of the company is wholly committed to implementing this policy.

This policy should not be incorporated just for the sake of implementing a policy. The top managers of the company should sincerely believe and be committed that this policy would encourage employees to speak up against crime, which in the long run would only prove beneficial to the company.

A research has found out that people prefer working in an organization that has moral and ethical values to one that is purely profit minded.

Further, the responsibility of the top level management does not end with initiating such a policy; but the ultimate responsibility of the operational functioning of the policy must also rest with them.

#### 2. Developing a whistle blowing policy-

Once top level commitment has been achieved, we can move ahead and develop a strong whistle blower policy. While formulating this, we must keep in mind the risks associated (like fraud, environmental damage, corruption etc.) and try to mitigate them. The survey results indicate that 30% of the companies had informed their employees about the policy through code of conduct and ethics manuals while 27% of them had employed trainings and inductions.

- Access to whistle blower policy - This includes the methods and means by which this policy can be made available to the employees. This can include manual of ethics and values, code of conduct etc. Induction trainings too can be conducted.
- Charters with the whistle blower policy can be hung in every department.
- Who are the users? – The primary intended users are definitely the employees of the company. In addition, third parties like suppliers, lenders, distributors and customers too should be given access to the policy; as fraud can happen at any

level in an organization. According to the survey, 57% of the companies do not give access to external parties.

- Channel to report crime- A dedicated team (say probably a team from the HR department) can be set up for dealing with these types of complaints. Crimes can be reported through e-mails or personally face to face. Hot line numbers too can be dedicated for this cause. 13% of the companies had a dedicated hotline number for reporting fraud; while 28% of the companies say that their employees prefer e-mails. The employee should be free to use the channel he/she is comfortable with. It is more important to communicate to the employees that they must report crime and they can do it through any of the above mentioned channels.
- Protection to whistle blowers - From the point of view of the employees, this probably would be the most important part of the policy. Employees should feel safe and secure. Many studies have shown that the biggest reason why employees do not expose crime is because they fear retaliation and humiliation from their colleagues. The company should adopt a zero tolerance stance to victimization of whistle blowers. As we saw earlier, whistle blowers are many a time subjected to harassment, suspension, denial of promotion and sometimes even dismissal. 19% of the participants cited perceived risks as one of the reasons for not reporting crime.

#### 3. Designing reporting mechanisms-

This involves an effective system which allows employees to formally communicate their concern. This would be followed by investigation. It is also important to apprise the employee the results of the investigation. Feedback is highly important; and this instills confidence in the employee.

#### 4. Embed the policy-

Whistle blowing must be viewed as a process rather than as an event. The culture of reporting crime must be embedded in the very work culture of the organization and instilled in every employee's mind. This objective can be achieved by conducting frequent training sessions. Informal meetings with the top management can also help in this regard. 54% of the respondents said that whistle blowing helps in improving organizational transparency and employee morale.

#### 5. Monitoring and evaluation-

Once a whistle blower policy has been developed, maintaining it is very important. The policy must periodically be reviewed for any possible loopholes or



failings. The policy also needs to be updated on a continuous basis to take into account the changing environment.

Evaluation involves assessing the policy from various aspects and taking corrective measures wherever required. These functions should be done by an external party who is independent of the policy.

#### 14.0 CONCLUSION

Whether we believe whistle-blowers to be heroes who suffer personal hardship to bring media attention to unethical behavior in organizations, or we take the opposing view that they break the oath of loyalty to their employer, the fact remains that employees are becoming increasingly willing to respond to any kind of unethical behavior in their organization. The choice for an employer is to ignore them and face possible public embarrassment later on and even financial losses, or to create an internal whistle blowing system that allows whistle blowers to be heard and their concerns addressed before the issue escalates to an external whistle blowing case.

To sum the issues discussed in the essay, it would be wise for all employers to put the following mechanism in place:

1. A well-documented process to document how such concerns are handled – a whistle-blower committee, clearly identified procedure to respond to the concerns, assurances of confidentiality, and non-retaliation against the employee.
2. Establish clear channels of communication – employee hotline, e-mail system etc.
3. Prompt and thorough investigation of genuine complaints
4. Detailed report of investigations and the actions (if any) taken.

Above all, employers must have a commitment to follow through on any and all concerns registered with the committee. For a whistle blower mechanism to work, trust must be established between the employees and their employer; – trust that information can be given anonymously and without any fear of retaliation.

#### 15.0 REFERENCES

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