RECOMMENDATION 1

The Board of Directors should decide and communicate the Company’s strategic aspiration and intention to be a leader in standards of ethical business conduct among global companies.

We are committed to progressing to a recognised leadership position in business conduct by continuing to embed policies and processes across the group, and integrate them into day-to-day business practice.

We believe visible leadership is essential to embed a culture of Total Performance and Responsible Behaviour among employees at all levels and wherever they work in the world. Our Values, Code of Conduct and Responsible Trading Principles are communicated to employees through briefings, training and ongoing engagement by senior leaders.

The company introduced Responsible Trading Principles at the beginning of 2010 to ensure that the Group makes informed decisions about the business opportunities we pursue. Opportunities are assessed according to the level of risk associated with the type of product, its intended use, the end user and the country of sale. The Principles are also being used in the procurement process to assess major suppliers. Additional guidance is also being introduced on anti-bribery and anti-corruption.

Responsible Trading Principles:
1. We understand and support our customers’ national security and other requirements
2. We assess carefully our products and services with the objective that neither BAE Systems nor our customers are exposed to significant reputational risk
3. We work to BAE Systems’ Values – Trusted, Innovate and Bold - in all that we do
4. We are as open as practicable about the nature of our business.

The Responsible Trading Principles are embedded in the Company’s Operational Framework (OF), the set of mandated policies, charters and processes that guide our work. The OF has been updated to address the 23 Woolf Recommendations and, along with the Code of Conduct and our new Company Values, underpins all our business activities.

Externally, we work with the Aerospace Industries Association of America and the Aerospace and Defence Industries Association of Europe to promote the adoption of responsible business practices and are directly involved with the International Forum of Business Ethical Conduct (IFBEC) for the Aerospace and Defence Industry, which agreed common Global Principles of Business Ethics for the Aerospace and Defence Industry in 2010.
RECOMMENDATION 2

The Company should be an advocate of its own ethical standards and must adopt the principle of openness and transparency. All ethical business conduct policies and procedures must be publicly available and easily accessible. The Company should be open about the actions it has undertaken to investigate allegations of unethical behaviour and about the outcomes.

In 2010, we have focused on integrating Responsible Behaviour into our core business policies and procedures, and ensuring that these fully reflect all four elements of Total Performance - Financial Performance, Customer Focus, Programme Execution and Responsible Behaviour.

Policies relating to Responsible Behaviour are now integrated into every section of the Operational Framework (OF), the set of mandated policies, charters and processes that guide our work. This has included adding a number of new policies and strengthening existing policies, including those relating to Gifts and Hospitality, Facilitation Payments and Conflicts of Interest. The OF is available to employees via the Company’s intranet site.

Line leaders report compliance against each part of the OF twice a year through the Operational Assurance Statement (OAS). The OAS is one of the Company’s review processes to provide assurance that mandated policies and processes are being complied with.

Our Lifecycle Management Framework used across all our major projects, has also been revised to reflect the four elements of Total Performance. This means, for example, that reviews carried out at the start of projects now include consideration of responsible trading risks.

We publicly report data on the number of dismissals for reasons relating to unethical behaviour, and the number and types of calls made to our ethics helpline.

Our global Code of Conduct is available on our internet site
RECOMMENDATION 3

The Company should develop, publish and implement a global code of ethical business conduct. The Board should ensure the proposed global code is comprehensive and reflects the high standards of ethical business conduct consistent with the aspiration and intention to become a leader among global companies.

In January 2009 we launched a global Code of Conduct. The Code encapsulates the principles and standards of business conduct we expect of employees wherever they work globally. As well as setting out our standards, the Code provides all our employees with practical guidance on how to deal with ethical dilemmas that may arise, and represents an unequivocal public statement of what we stand for, and how we do business.

The Code of Conduct was communicated to employees in 2009 through team briefings. The briefings were designed to cover how the Code of Conduct applies to employees in their daily work lives and aimed to create an environment where employees feel they can speak up, ask questions and raise any issues relating to responsible business conduct. Employees were required to undertake either online or classroom-based training on the Code of Conduct.

Our Code is reviewed regularly to ensure it continues to meet best practice, the first review was completed in 2010. This included an external benchmarking report produced by the Institute of Business Ethics (IBE). A planned update for 2011 will also address any gaps associated with revised policies since the Code’s launch as well as feedback received from employees.

View our global Code of Conduct and see Recommendation 20 for an update on training.
RECOMMENDATION 4

The Board should develop its increasingly proactive role in ensuring high standards of ethical business conduct in all the Company’s activities. It should be a standing item on its agenda. There should be an explicit assessment of ethical and reputational risks in all business decisions taken by the Board. Board members should themselves be exemplars of the standards set out in the global code and receive regular briefings on emerging issues in business ethics.

During 2010, CR key performance indicators, including business conduct, safety, and diversity and inclusion, were reviewed by the Executive Committee alongside financial and operational performance.

BAE Systems’ CR strategy is driven by the Chief Executive and the Executive Committee. An element of senior executives’ (i.e. the top 250 employees in the Group) remuneration in 2010 was directly linked to CR performance with up to 15% of potential annual incentive payment dependent on meeting objectives in the priority areas of business conduct and safety. All Group level targets relating to these priority areas were met in 2010.

The Managing Director, Corporate Responsibility (MD CR) reports directly to the Chief Executive and leads our global CR team, which provides support in embedding aspects of CR throughout the Group. A cross-functional CR Forum, led by the MD CR, enables us to raise employee awareness, share best practice and drive improvements across the Group.

Our policies require us to make informed assessments and responsible decisions about the nature of our products and the opportunities we choose to pursue. Products must be assessed against four criteria: the type of product, its intended use, the end user and, for exports, the country of sale.

The Corporate Responsibility Committee, a standing Committee of the Board, monitors and reviews performance of the business conduct programme and provides oversight and reporting on standards of ethical business conduct and the management of reputational risk.
RECOMMENDATION 5

The Board Corporate Responsibility Committee (CRC) should have primary responsibility for oversight and reporting on standards of ethical business conduct and the management of reputational risk. This role should be performed as the Audit Committee performs its task of managing financial risk.

The Corporate Responsibility (CR) Committee, chaired by non-executive director Paul Anderson, is the primary committee that monitors and reviews performance of the business conduct programme and provides oversight and reporting on standards of ethical business conduct and the management of reputational risk. It also ensures that appropriate policies, systems, reporting structure and metrics are in place and reviews the effectiveness of business conduct-related policies and procedures.

Throughout the 3 year period of implementation of the Woolf Programme the CR Committee has monitored management’s progress against the milestones set for the implementation of the 23 Recommendations including the roll out of the Company’s Code of Conduct across the Company. During 2010, the Committee reviewed progress against the milestones set for the implementation of the recommendations in the Woolf Report. It also agreed how an assessment would be undertaken in the first half of 2011 of the effectiveness of the implementation of the 23 recommendations contained in the report.

The Head of Internal Audit attends all of the CR Committee’s meetings and reports regularly on corporate responsibility-related work undertaken by the Internal Audit function and the key findings from this.

The CR Committee holds a joint meeting with the Audit Committee each year to review work undertaken by the Internal Audit function and agree the programme of audit work for the following year.

The Managing Director, Corporate Responsibility attends CRC meetings and has direct access to the CRC Chairman.
RECOMMENDATION 6

The Company’s Internal Audit function should ensure that ethical business conduct and the management of reputational risk is specifically assessed in all audit reports and the results, and progress made against recommendations, provided to the CRC. The additional skills and resources required for Internal Audit should be provided to achieve this. The CR and Audit Committees should hold at least one joint meeting a year to decide on the preparation of the annual internal audit programme.

In 2009 and 2010, the Internal Audit team worked with The Good Corporation to identify the key attributes of a methodology to assess Responsible Business Conduct and Non-Financial Risk as part of all internal audits. This was implemented during 2010.

The Corporate Responsibility (CR) Committee and Audit Committee receive regular reports on the results of audit activity and jointly approve the Internal Audit Programme. The CR Committee held a joint meeting with the Audit Committee during the year to review work undertaken by the Internal Audit function and agree the programme of audit work for the following year.

The Terms of Reference for the CRC and Audit Committee explicitly capture the requirement to jointly approve the Internal Audit Programme.

Please refer to Terms of Reference for the CR Committee or Audit Committee for further information.
RECOMMENDATION 7

Members of the senior executive team and heads of business units have both a personal and collective responsibility to demonstrate high standards of ethical business conduct and to achieve effective implementation of the global code. Both should be reflected in their performance appraisals and in the variable element of their remuneration.

Our Executive Committee leads the CR agenda, briefing employees on business conduct and our Code of Conduct.

BAE Systems’ CR strategy is driven by the Chief Executive and the Executive Committee. An element of senior executives’ (i.e. the top 250 employees in the Group) remuneration in 2010 was directly linked to CR performance with up to 15% of potential annual incentive payment dependent on meeting objectives in the priority areas of business conduct and safety. All Group level targets relating to these priority areas have been met. The performance of the operating groups in respect of the Group’s safety KPI is can be viewed here.

All Line Leaders and Functional Directors are required to submit to the Chief Executive the level of implementation of core policies in their areas of responsibility through the twice yearly Operational Assurance Statement (OAS). The OAS is one of the Company’s review processes to provide assurance that mandated policies and processes are being complied with.

In cases where a policy is judged not to be fully implemented a plan is required setting out the milestones to full compliance. The objective agreed for 2010 was that by year end all of the milestones for that year had to be met and any future milestones were on track to be met. Line Leaders and Functional Directors reported progress through their six-monthly OAS and the 2010 objective was achieved.
RECOMMENDATION 8

There should be a senior executive, supported by a sufficiently resourced team, reporting to the CEO and with direct access to the Chair of the CRC, who has responsibility for the programme to ensure and assure there are high standards of ethical business conduct across the Company.

The Managing Director, Corporate Responsibility, supports line leaders in driving the CR agenda. She reports directly to the Chief Executive and attends CRC meetings and has direct access to the CRC Chairman. This year the global CR team has supported Operating Groups in implementing our 2010 CR objectives. The team has also supported the completion of work set out under the of the Woolf Implementation programme.
RECOMMENDATION 9

The Company should develop formal processes to ensure business decisions are only taken following an explicit consideration of ethical and reputational risks. Where such risks are identified, the process should ensure any decision to proceed is taken at the appropriate level, and should include ratification by the Board.

Our policies, including our Product Trading and Pursuit of Export Opportunities policies and Responsible Trading Principles, require us to make informed assessments and responsible decisions about the nature of our products and the business opportunities we choose to pursue. Products must be assessed against four criteria: the type of product, its intended use, the end user and, for exports, the country of sale.

In 2010, we focused on integrating Responsible Behaviour and in particular the identification, management and mitigation of non-financial risk into our core business policies and procedures, and ensuring that these fully reflect all four elements of Total Performance.

Policies relating to Responsible Behaviour are now integrated into every section of the Operational Framework (OF), the set of mandated policies, charters and processes that guide our work. This has included adding a number of new policies and strengthening existing policies, including those relating to Gifts and Hospitality, Facilitation Payments and Conflicts of Interest.

Line leaders report compliance against each part of the OF twice a year through the Operational Assurance Statement.

Our Lifecycle Management Framework is used across all our major projects and has been revised to reflect the four elements of Total Performance. This means, for example, that reviews carried out at the start of projects now include consideration of responsible trading risks.

The Group is currently reviewing its policies and procedures in preparation for the implementation of the new UK Bribery Act 2010. We believe that our policies, including those covering advisers, facilitation payments, gifts and hospitality, conflicts of interest, offset and lobbying will comply with the requirements of the Act, although we will review them against guidance from the UK Ministry of Justice when it becomes available.
RECOMMENDATION 10

Policies and procedures in areas of potential ethical risks should be regularly reviewed, with particular attention to the areas of greatest risks. The planned programme of reviews by the Company should ensure a consolidated and comprehensive suite of policies consistent with the global code, providing employees with a clear pathway to understanding how the Company's standards of ethical conduct can be applied in day-to-day business situations.

In support of the Group’s strategy, the Board promotes a common corporate culture of Total Performance and identity as set out in the Operational Framework. This is based on principles of good governance, a set of definitions, values, policies and processes that guide our work and behaviour, and a clear system of delegated authority. The Operational Framework is mandatory across all wholly and majority-owned businesses and describes the Group’s approach to its organisation, culture (including its vision, values and ethical principles of business conduct), governance framework, core business processes and delegated authorities.

The Operational Framework:
- Sets out the BAE Systems organisation, top-level roles and responsibilities and delegated authorities
- Sets out our Vision and Values
- Mandates policies and processes to be used across the Company
- Is approved by the BAE Systems Board

We have embedded Responsible Trading Principles into our Operational Framework and policies have been enhanced to address the Woolf Committee recommendations. We shall review all policies at least every three years to ensure they remain current and reflect the standards expected of a global company.

Achieving a culture of Total Performance depends on all our employees living a common set of Values – Trusted, Innovative and Bold – in their day-to-day work. We recognise the importance of shared values and a global Code of Conduct across our increasingly diverse global business.

To further support this, a new category was introduced to our employee recognition scheme, known as the Chairman’s Awards. The new award is ‘Supporting our Total Performance Culture’ and is to recognise employees who have shown outstanding success in implementing our Total Performance culture. Employees are our greatest asset and this category rewards the efforts of those who best represent the Company’s commitment to maintaining a culture that promotes positive values in every aspect of its business.

For more information on our global Code of Conduct and on training to help embed it across the Group, as well as other training to embed responsible behaviour see also progress against recommendation 20.
RECOMMENDATION 11

The Company should ensure that the new process for selection, appointment and management of advisers is fully codified and integrated into the mandatory policy and procedures of the operational framework, and that appropriate guidance and training in the process is provided to all relevant employees. This should make explicit:

- a requirement to undertake face-to-face interviews, involving a company lawyer, as part of the due diligence process with all advisers whose activities require the interaction with potential customers;
- a general presumption that the identity of such advisers will be made known to potential customers; and
- endorsement by the Board of the adviser panel’s recommendations and their explicit approval of any decision to make an appointment contrary to the panel’s advice.

In 2007, we created a Business Development Adviser Compliance Panel for the review and assessment of adviser appointments. The appointment of advisers for business development, security, offset and lobbying activities (with the exception of certain domestic lobbyists in the US whose appointment is subject to separate legislative controls) is reviewed and assessed by the Panel, chaired by independent lawyers. All such advisers appointed in 2010 were appointed in accordance with our global adviser policy.
RECOMMENDATION 12

Advisers engaged to assist in Offset arrangements in export contracts should be subjected to the same due diligence and approval process as Advisers on the principal export contract. Offset contracts should be subject to a due diligence process requiring an explicit assessment of ethical and reputational risks and be capable of being audited for this. The Company should also be proactive in encouraging greater scrutiny and transparency by governments of the Offset elements of defence contracts.

The appointment of all Advisers, including Offset advisors are now subject to the Business Development Adviser Compliance Panel (see more detail in response to Recommendation 11)

The revised policy on offset (agreements with export customers to generate work or create capability in their country) requires us to ensure that robust procedures are in place for assessing and committing to such agreements. The underlying principles applicable to all Offset activities and arrangements are that they are:

- Undertaken in accordance with our Code of Conduct
- Clearly owned by line management with Executive oversight
- Consistent with the policies of the Customers and have a value proportionate to that of related contracts
- Fully assessed for financial and non-financial risks, with appropriate mitigation
RECOMMENDATION 13

The Company should continue to forbid facilitation payments as a matter of global policy. While it may not be possible to eliminate such payments immediately in some countries, management and employees in those countries need to be supported to ensure all such payments are reported to senior executives and to the Board, and the means developed to eliminate them completely over time.

Our Facilitation Payments Policy states that employees will not make (or allow others to make on our behalf) facilitation payments (irrespective of whether or not they are permitted by local laws). Employees are required to decline and report any request for such payments - recording them in writing on locally held registers which are accessible by Group General Counsel.

For more information on training on responsible behaviour see progress against recommendation 20.
RECOMMENDATION 14

The Company should implement central registers (by individual country) to enable information to be collected and monitored on aggregate spend on gifts and hospitality to individuals and overall to each customer. Aggregate spend by individual country on gifts and hospitality should be reported annually to the CRC. The policy on gifts and hospitality should be circulated to customers, contractors and suppliers and the Company should agree and document acceptable standards and expectations of behaviour with each customer government. A global policy on corporate donations should be developed, consistent with the global code and the policy of openness and transparency.

Our updated Gifts and Hospitality Policy sets out clear requirements for employees including limits on the giving and receiving of gifts and hospitality, together with recording of these activities.

Our policy also requires that Gifts and Hospitality Registers are held at all appropriate business levels, with access provided to Group General Counsel to ensure effective oversight.

We have amended our Company Giving Policy to provide clear guidance on all Company donations, including support for registered charities, approval limits and reporting of information.

See also progress against recommendation 20.
RECOMMENDATION 15

The Company should:

- for all new majority joint ventures require the adoption of its global code and associated policies and procedures, or equivalent standards;
- for all new minority joint ventures, mergers and acquisitions, undertake a due diligence assessment of standards of ethical business conduct compared to those of the Company, and ensure to the extent possible that equivalent standards are put in place;
- for all new key contractors, require the adoption of its global code and associated policies and procedures, or equivalent standards in all of its collaborative activities; and
- for all existing relationships, implement a programme to achieve the above.

It is our aim that there is clear understanding and a shared set of Values governing how we do business with our joint ventures. We continue to assess the approach taken by joint ventures and key suppliers as part of our programme.

Guidance has been introduced to help procurement teams apply our Responsible Trading Principles, and criteria relating to business conduct, safety and environmental management have been integrated into supplier selection criteria and ongoing supplier management.

In 2010, we provided our top 1,000 suppliers with a copy of our Code of Conduct and we encouraged them to work to equivalent standards. In the covering letter suppliers were reminded of the importance of their involvement in ensuring the principles and standards outlined in our global Code of Conduct are adhered to. The letter also asks that suppliers contact the Company if they feel there are any important differences in the way our organisations conduct our respective businesses, or if they require any clarification.
RECOMMENDATION 16

As part of the programme to ensure that equivalent standards are in place for joint ventures and with key contractors, the Company should extend to them appropriate access to its ethics helpline.

We provide our Code of Conduct, which includes details of our Ethics Helpline facility, to our top 1,000 supplier (see recommendation 15). The Code, is also available on-line.
RECOMMENDATION 17

The Company should ensure an explicit assessment of proposed lobbying positions or campaigns against the values and standards in the global code, and that regular reports on this are submitted to the CRC.

Our policy on lobbying governments and other bodies has been revised to require all those lobbying externally on BAE Systems' behalf to comply with our Code of Conduct. All lobbying activities are currently recorded within the markets in which we work and reports are reviewed by the Corporate Responsibility Committee.
RECOMMENDATION 18

The Company should make explicit its commitment to take a proactive approach to instigating internal investigations into allegations of unethical behaviour and to the disclosure of any material findings to the relevant authorities. Aggregate information on disciplinary actions for unethical behaviour should be included in internal and external publications.

We include aggregate information about employees dismissed from the Group for unethical conduct within our externally published Annual Report 2010. The information for 2010 can be seen in our 2010 Annual Report.
RECOMMENDATION 19

Any proposals for the appointment of third parties to provide the Company’s Security Division with information should be subject to the same process (including Panel review) as for advisers. Regular reports on the activities of the Security Division, and compliance with ethical policies and procedures, should be provided to the CRC.

The appointment of all Advisers, including Security advisers, is subject to the Business Development Adviser Compliance Panel (see more detail in response to recommendation 11)
RECOMMENDATION 20

A well-resourced training programme, in which every person in the Company participates, should be undertaken as part of the implementation of the global code and revised and repeated at regular intervals. Specific training modules should also be developed for senior executives and business unit leaders. Systems for monitoring these programmes should be developed so that they are able to provide the necessary assurance to the CRC as to their effectiveness.

Training to ensure employees understand and comply with the Code of Conduct forms a core part of raising awareness and developing a culture of total performance throughout the business. This includes an induction for newly hired staff and regular refresher courses for employees (see footnote 1). We have also issued the latest version of the group’s Integrity in Business Dealing training, an on-line course covering our Gifts and Hospitality, Facilitation Payments, Company Giving and Conflicts of interest policies that is required to be taken by executives.

See also recommendation 3 and 5.

1. Employees are required to attend refresher training during the 12-month period to May 2011 – more than 50% had already been trained by the end of 2010. New employees receive a copy of the Code and are required to complete the training as part of their induction.
RECOMMENDATION 21

The Company should take a more proactive leadership role in its engagement with the defence industry, governments, NGOs and other external interest parties to develop initiatives that will address the key ethical and reputational issues affecting the defence industry.

BAE Systems is a member of both the Aerospace Industries Association of America and the Aerospace and Defence Industries Association of Europe and has been directly involved with the International Forum of Business Ethical Conduct (IFBEC) for the Aerospace and Defence Industry, which agreed common Global Principles of Business Ethics for the Aerospace and Defence Industry in October 2009. The Global Principles bring together key elements endorsed by member companies of the U.S. Defense Industry Initiative on Ethics and Business Conduct and the Common Industry Standards for European Aerospace and Defence.

BAE Systems, together with other leading multinationals, is supporting a new Centre for Law and Ethics at University College London. The Centre, established in October 2009, aims to promote debate on business ethics and help companies promote an ethical corporate culture. BAE Systems is a Supporter of the Centre and our Chief Counsel, Compliance and Regulation, sits on the Advisory Committee and events held through 2010 included Ethical performance of business; Business reputation – ethics in the downturn; The governance of autonomous systems and The moral limits of markets.

During 2010 we also engaged with Socially Responsible Investment analysts via road shows and also held a number of stakeholder dialogue sessions with NGO’s and other interested parties.
RECOMMENDATION 22

The Company should be as open and transparent as possible in communicating all of its activities. Where this is not possible the Company should explain the reasons why.

We have committed to being as open as practicable with external stakeholders.

See also progress against recommendation 21.
RECOMMENDATION 23

The Board/CR Committee should commission and publish an independent external audit of ethical business conduct and the management of reputational risk in the Company within three years and at regular intervals thereafter.

We communicated our response to the Woolf recommendations externally during 2010, via our internet site and face to face briefings. We shall continue to communicate externally explaining our approach and the changes that we are making.

We are planning an external assurance of our Woolf Implementation Programme during the second half of 2011, post the end of the 3-year period.

The Ethical Leadership Group, an ethics consultancy, has been commissioned to carry out an independent assessment of the Group’s Business Conduct programme and to review the work undertaken in response to the Woolf Committee recommendations. This is based on a document review, interviews with the Chairman, the Chief Executive, the Chairman of the CR Committee and senior managers in each home market, and over 60 employee focus groups across our businesses. This review covers the Group’s global operations and is expected to be completed by April 2011.