Today's presentation

• Overview of conflicts of interest
  • Types
  • Applicable legal standards
  • C&E program responses
  • What social science teaches about COIs
• Studies and articles discussed today can be found at www.conflictofinterestblog.com

"Behavioral ethics"

• Part of larger (and very mainstream) field of behavioral economics that identifies cognitive biases (unknown or underappreciated ways in which we don’t act as we think we will)
• With behavioral ethics, focus is on ethical shortfalls
• It is both like a conflict
  • "Cognitive bias"
• And directly relevant to COIs
  • In the area of disclosure and management
Behavioral ethics (cont.)
- September 2015: President Obama signs executive order promoting behavioral science
- The UK government is a leader in this area
- Is this the behavioral ethics moment?
- Great place to learn more: www.ethicalsystems.org

Why COIs matter – a lot
- They are the most common type of C&E “case” at many organizations
- Frequently the most difficult to resolve due to personal nature of issues presented
  - E.g., cases involving family
- Can suggest a lack of trustworthiness generally
  - Recent study shows that employees who engage in insider trading (a form of COI) more likely to engage in other wrongdoing too
  - Implications for Board COIs are particularly serious

Why COIs matter
- Addressing COIs properly has broad implications for C&E programs
  - Impact on “organizational justice”
  - Need to consider harm element broadly
  - Practice pointer: make sure this is addressed in your program assessment
COIs and the law

- No single overarching legal regime
- Rather, for any given situation relevant law could be based on combination of
  - Fiduciary duty of loyalty (a legal “default” requirement)
  - Contractual provisions (possibly incorporating company policy)
  - Statutes and regulations (in some settings – e.g., government work)
  - Professional rules
- Laws are not always consistent
  - E.g., case against governor of Virginia

COIs, law and culture

- The murky legal landscape puts extra burden on C&E professionals
- Practice pointers:
  - Be fairly detailed in your code and/or policy because this is not always a clear-cut area to employees
  - Be alert to cultural differences
  - E.g., in some societies hiring relatives is seen not as a disloyal step but a way to promote loyalty to the company

Overlap with other risk areas

- Totally based on COIs: corruption
- COIs as “soft core” corruption
- Often the only difference of concealment (or a specific criminal law)
- Partly based on COIs
  - Fraud
  - Insider trading
  - Misuse of company resources
- Will discuss training implications in a moment
COIs and the future of C&E

- More focus in recent years than ever due to:
  - S-Ox and attention to fraud
  - FCPA
  - Health care/life sciences enforcement actions
- And this is likely to continue for several reasons
  - Ever expanding need for businesses and government to become efficient
  - COIs operate like a tax on businesses...and us all
  - Spread of anti-corruption enforcement globally focuses attention on COIs
  - As business relationships become more complex, opportunities for COI often increase

COIs – two dimensions: individual

- Harm is to the employer of the individual with a COI
- Common examples
  - External compensation (employee of/advisor to supplier)
  - External ownership (of supplier, customer or competitor)
  - Family employment (hiring, supervising)
  - Gifts, entertainment and travel
  - “Corporate opportunities” (director cases)

COIs – some less common types

- Any other outside employment or consulting (i.e., regardless of whether it involves a competitor, supplier, etc.)
- Relationships with union officials
- Holding government office (presumably on a part-time basis)
- Relationships with the company’s external auditors
- Practice pointer: tie what’s in code of conduct and training to risk assessment results
Other dimension: organizational

- Tend to be bigger cases than individual ones
- Harm is to a third party
- Examples
  - FCPA, other bribery
  - “Alliances” in IT industry
  - Government contracting – dual roles
- Not always harmful
  - Many ad agency COI cases

Organizational COIs

- Can be dangerous because “everyone does it” perception coupled with prosecutorial lag
- The securities analyst cases
- Practice pointer: Make sure this part of your risk assessment

Does disclosure cure COIs?

- One problem: “Moral licensing” behavioral concept
- Another: misperception that professionals and other important people not affected by COIs
- Studies show that COIs do have an impact on ethical decision making by
  - Directors
  - Doctors
  - Auditors
  - Compensation consultants
  - Many others
- Powerful professionals may face extra amount of peril
Disclosure (cont.)

- A less common problem: “reverse conflicts of interest”/overcompensation
- But illustrates the complexity of the area and need for vigilance
- Practice pointers
  - Educate employees on harmful effect of COIs
  - Reduce tolerance for waivers – consider a “clear showing that permitting the COI is in the best interests for the company” standard
  - Have independent/central function for reviewing waiver requests and managing approved COIs

COIs - structured risk assessment

- This is different than a COI audit
- Need due to:
  - High likelihood
  - High impact (in some instances)
  - Complexity/variety
  - Sensitivity
- Need not be a stand-alone process: okay if part of general C&E risk assessment
  - But might get lost in broader ERM one
  - This is also true of other C&E risk areas

What's the point in assessing COI risks?

- To help with:
  - Drafting/revising code provisions/policies
  - Creating/enhancing training/communications
  - Identifying COI risks for auditing, monitoring, certifying and other forms of checking
  - E.g., for each of these – who, what, where, how, when
The point in assessing COI risks

- Designing/refining approaches to disclosure, waiver and management
- Third-party issues
- All other COI-related elements of the C&E program
- Other points about COIs and risk assessment
  - A less fraught context for dealing with COIs than an audit or investigation
  - Also useful for documenting good faith
- And a point about risk assessments generally: the success of a risk assessment can be measured (in part) by how much information from it an organization actually uses

Boards of directors

- Two needs:
  - Avoid their own COIs
  - Be alert to top management COIs
    - Was the board complicit in the CEO’s dealings, or merely “ill-informed and negligent”?
- Related party transactions
- Need to look beyond pure financial interests: the Oracle case

Training senior managers on COIs

- Start with an attention-getting hypothetical case, perhaps showing how harmful even well-meant COIs can be
- Identify generally the types
- Describe legal and business imperatives for strong C&E efforts in these areas
- Discuss how employee perceptions of COIs by managers can undermine faith in the C&E program as a whole
  - Organizational justice
- Review applicable company policies and procedures regarding COIs
Training (cont.)

- Examine particular compliance challenges for this risk area, including the
  - Tendency of individuals to rationalize conflicts
  - Difficulty due to personal nature of COIs
- Explain what a manager’s specific role is to ensure COI-related compliance
  - Use red flags
  - Going beyond duty of loyalty to a culture of care
- Connect COI issues to other risk areas of significance – such as corruption, fraud and insider trading/confidential information

Training others?

- Base decision on risk assessment
- But for some functions it is a no-brainer
  - E.g., Procurement
  - Should you train everyone?
    - In some companies, Yes – but in many, No
- A related issue – COI other communications
  - A standard practice: holiday “no-gift” letters
  - A less standard practice: the COI quiz

Certifications

- “Employees are often confused about COIs and don’t think they have one when they do or at least when there is an appearance of a possible conflict. [Certifications] seem to be a good way to help employees focus on specific activities that can present a conflict” (from a C&E officer, writing to the COI Blog)
  - Need not be for whole workforce
  - Whether/who/what should be a function of the risk assessment
  - Can be part of larger certification
  - Practice pointer: consider if your organization has the resources to follow-up on all “yes” answers?
COI policies and procedures

• Practice pointer: have a stand-alone policy
  • Elevates importance of the area
  • Can include more process than in a code – important for organizational justice
  • Forces resolution (important for senior personnel COI)
  • Driven by the risk assessment, e.g.,
    • For significant G&E matters (e.g., Super Bowl tickets) process should look closely at state of play of commercial relations with recipient’s company
  • Awareness of G&E standards in codes of major customers as part of ongoing process

Policies and procedures (cont.)

• Practice pointer: address not only actual and apparent COIs, but also potential ones
  • A new and troubling question: do standard COI policies violate labor law? Remington Lodging & Hospitality, LLC d/b/a The Sheraton Anchorage (NLRB June 2015)

Management

• Consider use of technology for management of COIs
  • Can be both operationally useful and symbolically important
  • But not necessary for all companies - again, depends on risk assessment
    • For some companies a spreadsheet is fine
  • Make sure high-level people are involved
Third party compliance

• Supplier codes
  • Make sure there is required “push down” within supplier organization
• Consider requiring
  • Certifications
  • COI training
• Audit rights
• All as dictated by risk assessment

One more COI issue

• COIs in C&E investigations
• Make sure that independence is built into investigative protocols
  • Can be a particular issue with HR investigations
• Do you audit this area?

“Moral hazard”

• Not quite a COI, but can be just as important to C&E program
  • As with cognitive bias, it is conflict-like
• Concept has been around since the 19th century – and was more economic than ethics-related
  • Originally concerned insurance
  • Took on new urgency with financial industry meltdown
• Government’s prosecution of companies but not individuals is a moral hazard problem
  • Will this change with new enforcement policy?
Moral hazard – three implications for C&E programs

• Focus more on how compensation approaches might create C&E risks
• Should be part of risk assessment
• Should consider structured monitoring of it
• Consider intangible moral hazard interests
• Political activities example
• Most important: argues in favor of stronger board oversight of C&E program generally because too many managers have short-term focus