

The Complete Compliance and Ethics Manual 2023

Conflicts of Interest

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Conflicts of interest are present in all areas of the business and professional world. They are difficult to regulate, difficult to mitigate, and can create enormous harm for organizations (although they can also, in some instances, be without cost). The complicated nature of this area emanates from several factors. First, conflicts arise in myriad ways and contexts, and there is an enormous scope of activity that is prone to conflicts. Second, there is no uniform law on conflicts of interest. Instead, the manner in which conflicts are regulated tends to be determined largely by the specific context in which the conflict arises. Third, conflicts tend to arise in highly personal contexts, which makes them difficult to identify and even harder to regulate.

What follows is a discussion of conflicts of interest, including:

- How conflicts of interest are defined,
- What constitutes an interest for conflicts of interest purposes,
- The harm caused by conflicts of interest,
- Legal guidance on dealing with conflicts of interest, and
- Conflicts of interest compliance programs.

What Are Conflicts of Interest?

Conflicts of interest are typically defined as occurring when one's personal interest interferes or competes with the interests of another to whom one owes some duty. Employees owe their employers certain duties of loyalty, and it is these employee/employer obligations with which most companies' conflict of interest policies are primarily concerned. Other duties or obligations can create conflicts, however, including the duties owed by gatekeepers, such as lawyers and external auditors, to their professions or the public.

While conflicts have existed for as long as human beings have acted on behalf of others, they have been magnified in the past few decades as organizations and individuals assume more diverse roles and change roles more frequently over time. Indeed, while conflicts are undoubtedly more highly regulated than ever, they also seem to be creating more damage than ever. The imperative for organizations to create effective conflicts compliance regimes is therefore stronger than ever, although doing so continues to pose enormous challenges to organizations.

Interestingly, unlike many areas regulated by compliance law, the existence of a conflict of interest is not something that is inherently wrong. Indeed, having personal interests and having duties to others are simply aspects of the human condition. Thus, it is not the existence of a conflict that is necessarily problematic, but instead how one responds to the conflict. This is one reason that compliance regimes are so essential in effectively dealing with conflicts. They create the infrastructure and systems that allow individuals to act ethically and appropriately in the face of conflicting interests, which are often inevitable.

Conflicts can be categorized into personal and organizational conflicts. Personal conflicts are the type that most readily come to mind when we think of compliance programs. They typically refer to the conflicts that arise between an individual employee's or director's self-interest and the duty owed to their employer. It is important to keep in mind, however, that organizations also have interests and duties, and these can sometimes compete with each other.

What Constitutes an Interest?

In designing a conflicts of interest compliance regime, one of the fundamental questions that organizations must consider is what qualifies as an interest for purposes of their conflicts of interest policies. In the broadest sense, an interest could be defined as anything of value to a person, including a financial interest, an asset, a relationship with another, a reputational interest, or even a belief. However, not all interests could or should be considered interests capable of creating a conflict. It would simply not be possible for an organization to prohibit employees from acting from any personal interest whatsoever, as organizations could neither define nor enforce such a broad mandate. Because financial interests are reasonably easy to define and regulate, they are typically the focus of most conflicts policies. Certain types of personal relationships are also often considered interests for conflicts purposes, including family and personal or romantic relationships.

In addition to practical limitations on how broadly an interest can be defined, organizations must also balance their employees' personal and privacy interests when considering how to design their conflicts of interest policies. Conflicts between personal and professional interests necessarily involve an employee's personal—private—life. The extent to which an organization chooses to interfere in an employee's personal life is an important policy decision. In addition, this area may also be regulated by law, in particular in the European Union, where privacy laws are typically more robust than in the United States. Thus, for example, from an organization's perspective, it may be very helpful to know whether an employee is involved in a romantic relationship with the employee of a supplier or competitor. However, whether an organization can or should seek that type of personal information from its employees involves important policy decisions regarding not only the organization's interests, but also the privacy interests of employees.

Harm Caused by Conflicts

While having a conflict of interest is not inherently inappropriate or wrong, conflicts nonetheless have the potential for creating enormous harm to organizations and to society at large. If an employee acts in their own interests rather than in the organization's interests, the employee may make decisions on behalf of the organization that are not as profitable as they might otherwise be, or that somehow harm the organization. For example, if a member of the procurement team chooses a supplier because it will benefit that individual personally rather than because it is the best supplier for the organization, then the organization may be spending more for a sub-optimal supplier, which obviously carries its own (potentially high) costs to the organization—not just in the direct costs of the products or services supplied, but also potentially in the form of lower quality products or services, which could create significant indirect costs. Similarly, if an executive usurps a corporate opportunity, the organization has forfeited the potential profit that that opportunity represents.

Conflicts of interest can also create the perception of unfairness, which can damage the culture of compliance at an organization. Indeed, how an organization handles conflicts of interest can be an important element of an organization's culture of compliance. In many organizations, those employees at the highest levels of the company are the employees with the greatest opportunity to profit from conflicts, and the greatest ability to harm the organization from conflicts-ridden behavior. In addition, as noted above, conflicts are inherently personal in nature. Thus, where there is a perception of a double standard (where organizations seem not to enforce conflicts policies against higher-level employees of an organization), it can be corrosive to the culture of

compliance. And, on the other hand, where an organization has a well-developed conflicts policy that is consistently enforced, the compliance culture will benefit.

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