



Conflicts of Interest Directors

A member of **IBL**

Definitions

A few definitions:

- Any situation in which an individual or company is in a position to exploit a professional or official capacity in some way for their personal or corporate benefit.
- A situation in which a party's responsibility to a second party limits its ability to discharge its responsibility to a third party.
- A situation that has the potential to undermine the impartiality of a person because of the possibility of clash between the person's self-interest and professional interest or public interest.

Elements that may cause a Conflict of Interest

- A situation that involves someone in a position of trust/authority in an organisation
- A situation that could create an appearance of impropriety that undermine confidence in the person, the profession or the organisation
- Competing professional and/or personal interests
- An inherent conflict of roles
- Interests that could make it difficult for her/him to fulfill his or her duties impartially

Common Situations of Conflict

- Members of the board who may have interests (earning of money or other advantage) in competing/connected organisations
- A director who sits on the board of a supplier or customer
- A director who sits on multiple boards, including competitors' boards
- A director being appointed to the board by a major shareholder
- Procurement through family connections
- Being offered a gift in order to support a motion/proposal
- Acting in a way that ensures potential gain rather than in the best interests of the company

Types of Conflicts of Interest

- Related party transaction (e.g. a company purchasing insurance cover through a brokerage firm controlled by one of its board members)
- Self-dealing (e.g. a director of company X finds himself on both sides of a deal that involves company X and another company where himself or his relatives have an interest)
- Non-arms length relationship (e.g. a company purchasing goods from a company owned by a relative even if the 2 companies are not affiliated parties or purchasing goods/services from a company that have the same parent company even if they operate independently)



Identifying Conflicts

1. Set up a self-monitoring system to prevent or circumvent conflicts of interest (e.g. drafting relevant policy)
2. Outline the specific needs of the business/organisation before developing a conflict of interest statement
3. Familiarise yourself with potential conflicts of interest

10 Questions to help identify a conflict

1. Are you a director or significant shareholder of a company which is:
 - A significant shareholder in the company?
 - In partnership with the company?
 - In a joint venture with the company?
2. Are you a significant shareholder of the company in your own right?
3. Does any external body you are associated with have any of the following relationships with the company?
 - Supplier
 - Customer
 - Competitor
 - Banking
 - Distribution
 - Ongoing, but material relationships (e.g. bidding of contract against or with company or acting as agent for the company or providing financing to the company or any of its subsidiaries)

10 Questions to help identify a conflict (contd)

4. Are you associated with any adviser to the company?
5. Are you a member of a committee or of a commission or do you have a material position with the regulator, a trade or professional body, etc?
6. Are you a trustee of the company's pension trust or a director of the corporate trustee of the pension trust?
7. Do you hold a material position with any pension fund that could itself maintain a material shareholding in the company?
8. Are you associated with an investment organisation of any nature?
9. Are you in a position that you could make a profit as a result of your directorship of the company/
10. Do you know any other circumstances that could give rise to a potential or actual conflict of interest or duties?

Why do Conflicts of Interest matter?

- Directors have a fiduciary duty to act in the best interests of their company (the shareholders as a whole and not individual shareholders)
- Failure to resolve conflict of interest can result in the Director having to account personally to the company for any loss attributable to the breach.
- Public opinion/organisation reputation

Director's role in a conflict of interest

- Directors must give undivided loyalty to the company that they serve
- Directors should not put themselves in a position that would create a conflict between their duty to act in the best interests of the company and their own personal interest
 - A director should not have any personal interest in any proposed contracts with the company
 - A director should not take personal advantage of opportunities that arise because of his association with the company

Legal Duties of Directors in relation to Conflicts of Interest

- Under the CA 2001, the Board of Directors have general duties of:
 - Establishing vision, mission and values for the company
 - Setting strategy and structure for the company
 - Delegating to management
 - Exercising accountability to shareholders and being responsible to relevant stakeholders
- Duty of loyalty calls for Directors not to:
 - Conduct transactions in which they have a personal interest
 - Accept a position in a competing company
 - Enter into contractual relations with a competing company
 - Use the company's assets, facilities for personal use
 - Use information, business opportunities received in their official capacity for personal gain
 - Accept gifts
 - Leak information

Declaring a Conflict of Interest

- As a Director, you have a duty to declare a Conflict of Interest
- When to declare a Conflict of Interest?
- **Initial Disclosure**

Directors to provide to the Company Secretary as at date they become a Director:

- Details of all securities (number and class) of the company registered in their name
- Details of all securities of the company not registered in the Director's name but in which the Director has a relevant interest
- Details of all contracts to which the Director is a party or under which he is entitled to a benefit

Declaring a Conflict of Interest (Contd)

- **Ongoing Disclosure**

Directors should provide the Company Secretary the following information:

- Details of changes in securities of the company registered in the Director's name other than changes occurring as a result of corporate actions by the company
- Details of changes in securities of the company registered in the Director's name in which he has a relevant interest
- Details of all changes to contracts to which the Director is a party or under which the Director is entitled to a benefit

Declaring a Conflict of Interest (Contd)

- **Final Disclosure**

Directors should provide to the company Secretary the following information upon the date of ceasing to be a Director:

- Details of all securities (number and class) of the company registered in the Director's name
- Details of all securities of the company not registered in the Director's name but in which he has a relevant interest
- Details of all contracts to which the Director is a party or under which the Director is entitled to a benefit

Directors must acknowledge that from time to time their independence status may change. In the event of a change or of a potential change, the Director should immediately notify the Board

How to declare a Conflict of Interest

- Declaration can take the form of a general notice to the Directors of the Company
- Notice to state:
 - You are a shareholder of, or is otherwise interested in the other company or,
 - You are a member of a specified firm and you are regarded as “interested” in any contract made by the company with that firm
- The Director who has declared a conflict should not vote on any contract that he has an interest in

When an undeclared Conflict arises

- A Director should declare the Conflict of Interest at the meeting of Directors where the subject giving rise to the Conflict is first considered.
- If, as a Director, you become interested in a contract after it is made, you must declare your interest at the first meeting of Directors held after you become interested.
- Conflicts of interest are recorded in the minutes to ensure that there is a record of the conflict and how it was dealt with

Failure to declare a Conflict of Interest

- If, as a Director, you fail to declare your interest in a contract, the Court may set aside the contract on any terms that it considers appropriate.

Ways to mitigate Conflicts of Interest

- **Removal**

The best way to handle conflicts of interest is to avoid them entirely. Short of avoiding them, the best way to deal with them is:

- Disclosure
- Recusal
- Third-party evaluation

- **Disclosure**

Certain professionals are required either by rules related to their professional organisation or by statute to disclose any actual or potential conflicts of interest.

In some instances, failure to provide full disclosure is a crime.

Ways to mitigate Conflicts of Interest

- **Recusal**

Directors with a conflict of interest are expected to recuse themselves from decisions where such conflict exists.

To minimise any conflict, the Board member should not participate in any way in the decision, including discussions

- **Third-party Evaluations**

Example: hiring a third-party (independent firm) to calculate a “fair price” in cases where transactions are being considered.

Third-party evaluations may also be used as a proof that transactions were fair and conducted at arms-length..

Global Trends Dealing with Conflicts of Interest

- Fundamental Principles
 - Transparency, responsibility, accountability and fairness
- Conflicts of Interest Policy and Process
 - Transparent process for declaring conflicts of interest, with clearly defined responsibilities and accountabilities
- Personal Account Dealing
 - Some companies require a policy which imposes certain restrictions, approval procedures and reporting requirements in relation to personal account dealings
- Confidentiality
 - A company must have a clear policy on confidentiality
 - Meeting procedures-meetings where conflicts of interest are disclosed must be properly recorded in the minutes of that meeting

Global Trends Dealing with Conflicts of Interest (Contd)

- Procurement Policy
 - Policy to clearly state the company's policy on dealing with conflicts of interest
- Related Party Transactions
 - Companies must have a published policy on related party transactions
- Stakeholder Approvals and Scrutiny
 - Private voluntary standards seek out stakeholder input and as a result have greater credibility. Records of the process of dealing with a conflict of interest are available for public scrutiny
- Chinese Walls
 - A method of restricting internal flow of information between parts of a company or group of companies performing different and possibly conflicting functions

Global Trends in Implementation and Best Practice

- Board sets clear direction and culture on all related party transactions
- Board mandatory reviews related party transactions exceeding 1% of revenue
- Audit Committee reviews all material related party transactions
- Systems, processes, procedures are in place to avoid related party transactions becoming abusive
- Employees communicated a strong employee ethics policy that related party transactions are strongly discouraged

Global Trends in Implementation and Best Practice (Contd)

- Directors/Commissioners/Controlling shareholders are made personally liable for company loss if they exploit the company for personal interests
- Companies required to develop and make public the policy and procedure for the approval of related party transactions
- Financials of all subsidiaries and related entities are published on the website so that the shareholders can get a clear picture on the need and the related party transactions
- Insiders responsible for decision in the company required to make annual statements that they do not have any conflict of interest in all decisions they make and that they comply with the company's code of conduct

Other Global Best Practices

- Director's Services Contract
 - Sets out the main terms of appointment of a NED
- Director's Disclosure Obligations
 - Sets out the director's obligation of disclosing his interests (usually part of the services contract)
- Director Induction, Training, Mentoring and Evaluation
 - Proper and timely induction of new directors
 - Continuous professional development for directors
 - Mentoring of new directors by the Chairman or by a senior independent director
 - Annual board effectiveness and directors' performance evaluations
- Statement of Independence Policy
 - The primary objective of this policy is to ensure that the directors are, and are seen to be, independent

Other Global Best Practices (Contd)

- Corporate Governance Manual
 - Top down approach to the systematic implementation of the principles of performance and conformance
- Directors and Officers Liability Insurance and Professional Indemnity
 - Designed specifically to provide financial protection in the event that mismanagement claims are made
- Codes of Ethics
 - Generally conflicts of interest forbidden
 - Help to minimise problems with conflicts of interest because they can spell out the extent to which such conflicts should be avoided
- Employee Handbooks
 - Top down approach and contains all information about company policies and procedures
 - Give clear advice to employees and create a culture where issues are dealt with fairly and consistently