

Dealing with Conflicts of Interest

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Presenter

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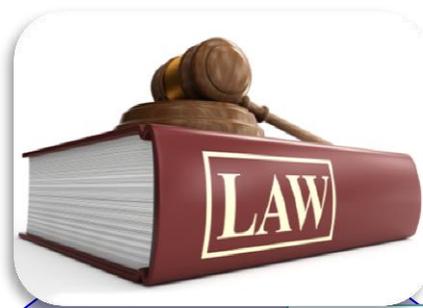


Discussion points

- The interaction between the law, best practice standards and ethics
- Legal duties
 - The Trust Property Control Act
 - The Companies Act
- The FISA Code of Ethics and of Professional and Responsible Conduct
 - Integrity and honesty
 - Independence of thought and behaviour
 - Conflicts of interest
 - Confidentiality
- Ethical decision-making
- Key learning points

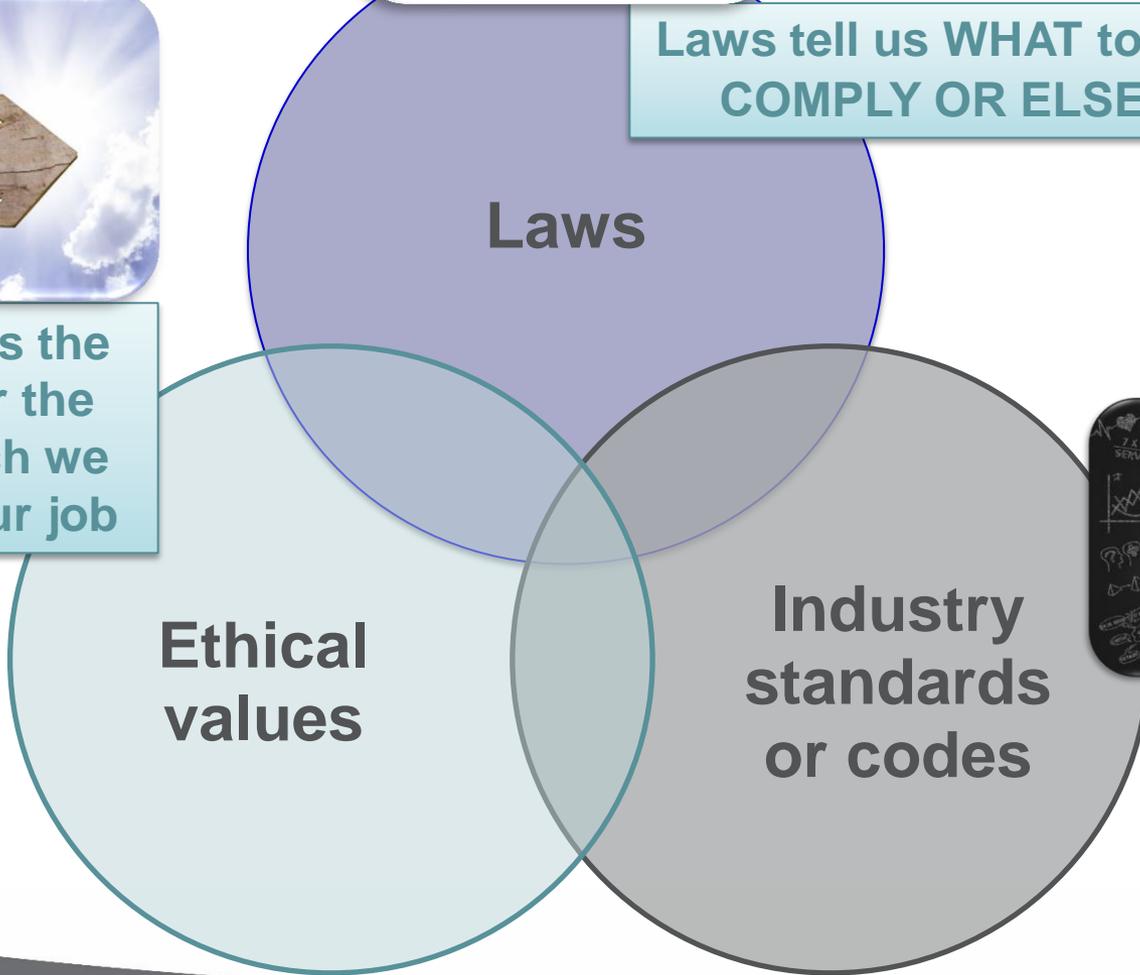
The interaction between the law, best practice standards and ethics





Values tell us the **MANNER** or the **WAY** in which we should do our job

Laws tell us **WHAT** to do - **COMPLY OR ELSE...**



Best practice guidelines tell us **HOW** to do things

Legal duties



Fraud

- Formal definition: **Fraud is the unlawful, intentional making of a misrepresentation that causes actual or potential damage or harm to another.**
- In other words, fraud involves deliberately **lying** or **withholding** important facts thereby causing **harm** to another.



The Trust Property Control Act Act 57 of 1988



Section 9: Care, diligence and skill required of a trustee

- (1) A trustee shall in the performance of his duties and the exercise of his powers act with the **care, diligence and skill** which can reasonably be expected of a person who manages the affairs of another.
- (2) Any provision contained in a trust instrument shall be void in so far as it would have the effect of exempting a trustee from or indemnifying him against liability for **breach of trust** where he fails to show the degree of care, diligence and skill as required in subsection (1).

A similar provision in the Administration of Estates Act does not exist, but the same level of care, diligence and skill is required and the duty to act in the best interests of the deceased estate, and the heirs and beneficiaries, also exists. (With thanks to Mr Louis van Vuren)

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SA Companies Act

Legal duties of directors and prescribed officers



Common-law duties of executives (and trustees)

- The common-law duties of company executives are to manage the affairs of the organisation with **care, skill, in good faith** (*bona fide = best interest*) and with **diligence**.
- The main duty of an executive is to **care** for the organisation.
- In other words, an executive has to act as if the organisation is an incapacitated family member in his/her care.
- “We become the heart, mind and soul of an organisation when we become a director/board member.” (Prof Mervin King)
- The same principles can be applied to the duties of trustees.

Companies Act 2008 Section 76: Standard of care

Section 76(2): A director of a company must -

- (a) not use the position of director, or any information obtained while acting in the capacity of a director -
 - (i) to **gain an advantage** for the director, or for another person other than the company or a wholly-owned subsidiary of the company; or
 - (ii) **knowingly to cause harm** to the company or a subsidiary of the company; ...

Definition of “knowingly”

“Knowing”, “knowingly” or “knows”, when used with respect to a person, and in relation to a particular matter, means that the person either—

(a) had **actual knowledge** of that matter;

(b) was in a position in which the person **reasonably ought to have** -

(i) had **actual knowledge**;

(ii) **investigated** the matter to an extent that would have provided the person with actual knowledge; or

(iii) **taken other measures** which, if taken, would **reasonably be expected** to have provided the person with actual knowledge of the matter.

- NOTE: One may not remain **supine** – you have to engage and enquire!

Companies Act 2008

Section 76: Standard of care (continued)

Section 76(3): A director of a company -

must exercise the powers and perform the functions of a director -

- (a) **in good faith and for a proper purpose** (do not exceed powers);
- (b) in the **best interests** of the company; and
- (c) with the degree of **care, skill and diligence** that may **reasonably** be expected of a person -
 - (i) carrying out the same functions in relation to the company as those carried out by that director; and
 - (ii) having the general knowledge, skill and experience of that director.

Companies Act 2008 Section 76: Standard of care (continued)

- The requirements set out in subsection 76(3)(b) and (c) will be met if the director has taken **reasonably** diligent steps to:
 - **become informed** about the matter; and
 - he/she or another he knew about **had no material personal financial interest** in the subject matter of the decision; and
 - he/she had a rational basis for believing, and did believe, that the decision was in the **best interest** of the company; or
 - he/she **relied on the opinions of persons**, such as legal counsel, retained by the company.

Test for compliance to the standard of care

- The duties of directors/prescribed officers can be grouped into:
 - (1) the **duty of care, skill and diligence**, in terms of which directors must manage the business of the company as a reasonably prudent person would manage his/her own affairs.
 - Previously the **common-law test** was **subjective** and applied only to the director's own skill.
 - Now, the standard of care is a mixed **objective and subjective** test, in the sense that the minimum standard is that of a **reasonably prudent person**, but a director who has **greater skills, knowledge or experience** than the reasonable person must give to the company the benefit of those greater skills, knowledge and experience;

Test for compliance to the standard of care

(2) **fiduciary duties**, being the duty of directors to act in the **best interest** of the company, to **avoid conflicts**, not to take corporate opportunities or **secret profits**, not to fetter their votes and to use their powers for the purpose conferred and not for a collateral purpose.

- There is **personal liability for breach of certain statutory duties**.
- Provision exists for relieving directors of liability in certain circumstances, either by the courts or, if permitted, by the company's constitution, but **not in the case of gross negligence, willful misconduct or breach of trust**.

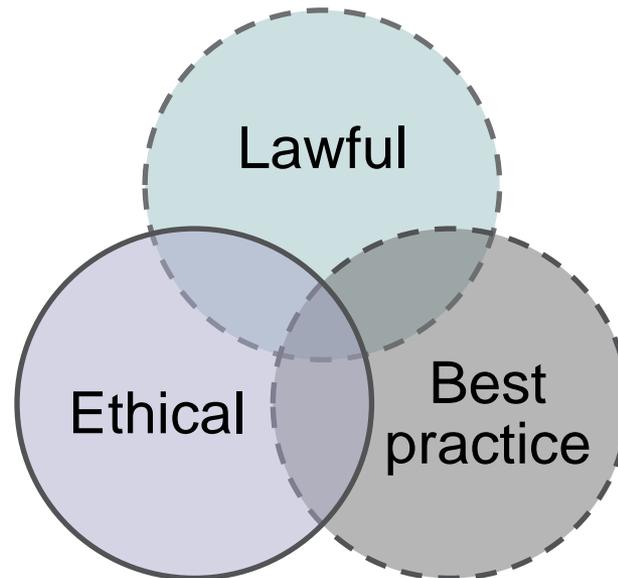
Cowan and Others v Scargill and Others [1984] 2 All ER (Ch. D)

- In the Cowan case it was held that:
 - “*The starting point is the duty of trustees to **exercise their powers in the best interests of the present and future beneficiaries** of the trust, holding the scales **impartially** between different classes of beneficiaries.*
 - *This duty of the trustees towards their beneficiaries is paramount. They must, of course, **obey the law**, but subject to that, they must **put the interests of their beneficiaries first.**” (page 760)*

(With thanks to Mr Louis van Vuren)

Industry code (best practice)

FISA Code of Ethics and of Professional and Responsible Conduct



Integrity (paragraph 1)

Integrity implies that:

- Clients and other stakeholders expects members to be **totally honest, fair and trustworthy** (stakeholders should not have to verify information).
 - Test: Would I be satisfied if I was given this information?
- *“Members owe a solemn duty to uphold the integrity and honour of the fiduciary profession and to encourage and foster **respect** for it through their conduct.”*
 - Test: How would my behaviour affect the reputation of the profession?



Defining integrity

- During a recent speech, Chief Justice Mogoeng Mogoeng, quoted the words of Montgomery van Wart in defining what integrity is and what the qualities are possessed by such persons of character.
- Prof Van Wart, Director of the Centre of Public Service at Texas Tech University, defines integrity as:
 - The willingness to talk the truth
 - being consistent
 - treating others the way one would like to be treated oneself
 - using the necessary discernment in taking decisions and
 - striving for excellence in all one does and showing remarkable candour.
- **A high level of conscientiousness will be demonstrated, they will follow through on promises and show unusual astuteness (wisdom) in meeting competing interests.**

Defining integrity (2)

- Justice Mogoeng describes the characteristics of a person with integrity as someone who **follows through on commitments, is fair in all dealings, acts with wisdom and applies diligence** in all he/she does.
- He believes that a leader with integrity will be able to:
 - Influence
 - inspire
 - direct
 - mobilise
 - encourage and
 - activate his/her followers to pursue a common goal with commitment while keeping momentum, confidence and courage.



Honesty (paragraph 1.1)

Honesty requires that:

- A member may not transfer or receive in a personal account any property of a client or anything in the possession of the client with the exception of a legal fee.
- A member may not receive or take possession of any other property of a client in any other capacity apart from the fulfilment of his/her duties as a fiduciary professional.
- A member may not knowingly communicate anything to any stakeholder which is not the whole truth.
- A member shall not withhold any information where there is a duty to communicate such information or where the information will have a material influence on a decision that the stakeholder has to take regarding matters that fall within the scope of fiduciary services.
Etc.

The true meaning of honesty

“There is more to it than simply not lying”

Article by Prof Frank J. Navran
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“Not lying”

- Prof Navran explains that there is much more to honesty than simply not lying. He includes the following in “not lying”:
 - “Remaining silent, thus implying agreement or acquiescence, with what we, in fact, do not think to be the best course.*
 - Saying enough to end a discussion on acceptable terms, while withholding some information, questions or concerns that might lead to conflict or disagreement, thereby masking those questions or concerns.
 - Agreeing to support another’s position, implying a point of view that we do not actually hold/share, in order to avoid conflict.
 - Acting in accord with another’s position, while privately sharing our disagreement with others.”

***Note:** when we remain silent when we are told a lie, we are communicating that we accept the untruth.

Reasons for lying

- Lying is always a **choice**. We lie when:
 - we want to avoid being rude or hurt someone’s feelings
 - we believe the lie will not cause any “harm”
 - we don’t want to know the truth and will rather let a lie pass because knowing the truth will place a responsibility on us, such as a boss who does not want to hear what is wrong
 - we don’t want others to know the truth or
 - it is seen as the path of least resistance.
- Because we are **human**, we make mistakes and we fear the consequences of those mistakes if they are discovered.
- We often lie because we are **proud**. We fear that people will think less of us if they knew the truth.

Reasons for Lying (2)

- Prof Navran believes that we find it difficult to tell the truth because:
 - it may require a level of honesty and/or **courage** that is beyond our reach; or
 - telling the truth in such a way that no one is harmed may require **skills** that we do not possess; or
 - certain topics, such as complicated financial calculations, may be beyond our competence or outside our comfort zone; and
 - we sometimes simply follow everyone else – it is “the way things are done around here” – no one is fully honest; or
 - **it will not be to my personal or employers benefit.**

Objectivity (paragraph 1.3)

Being objective means that:

- When giving a fiduciary opinion, a member must ensure that he/she has **no bias** in favour of, or against any stakeholder. Factually **correct** and **relevant** information may however be shared.
- Any information that is factually **correct** and **relevant to the situation** and that may have a **material impact on decision-making** may not be withheld solely because it may shed a **negative light** on the member or his/her employer.
- The CIMA website (www.cimaglobal.com), defines objectivity as:
 - *“120.1 The principle of objectivity imposes an obligation on all professional accountants not to compromise their professional or business judgment because of bias, conflict of interest or the undue influence of others.”*

(Follow the URL <https://bit.ly/2MHbhpn>.)

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Independence of thought and behaviour (paragraph 1.4)

- Being independent requires that **all facts and circumstances** with regard to the affairs of a client must be **evaluated**
 - Serving the best interest of the client should be the **primary objective**.
 - Such an evaluation should be done **independently**.
 - It may not be **unduly influenced** by an **adopted policy** of the member (or employer) which may be **detrimental** to the client.
 - Services or product supplied by the member of employer which will put the client in a **comparable** or **better position** may be used.
 - Test: Have I **applied my mind fully** and considered all relevant facts and circumstances? In other words, have I really been **intellectually honest**?

Acting with intellectual honesty

- As trustees we are ultimately **stewards** of the trust and its beneficiaries.
- We have to perform our duties with **intellectual honesty**.
- We must act **independently**.
- Independence is a **state of mind**: Am I really **objective** and **impartial** in applying my mind?
- Am I serving the best interest of the **present and future beneficiaries** and am I putting their interests first?



Conflicts of interest (paragraph 1.5)

- Avoid any conflicts of interest **or appearances** of being conflicted.
- **Take reasonable steps to anticipate** possible areas where a conflict may arise.
- No information that is **not publicly available** may be used to invest in a venture, unless it is legally permissible to do so.
- A member must immediately upon coming to know of the conflict or potential conflict **notify all interested parties**. The member may however **consult** his/her employer before making the conflict known.
- A member employed by another person or institute **may not secretly act in competition** with such employer.



Defining a conflict of interest

- The Oxford Dictionaries describe a conflict of interest as: *"A situation in which the concerns or aims of two different parties are incompatible",* or *"a situation in which a person is in a position to derive personal benefit from actions or decisions made in their official capacity".*
- The Business Dictionary says a conflict of interest is: *"A situation that has the potential to undermine the impartiality of a person because of the possibility of a clash between the person's self-interest and professional interest or public interest."*
- In other words, a conflict of interest arises when a person has a personal interest in a decision in which he/she is involved in, and he/she puts his/her personal interest before the client's best interest.
- Objectivity, independence and **professional judgement is impaired for self-serving purposes.**

Confidentiality (paragraph 2.3)

- A member **shall not reveal any information** about the affairs of a client to anybody not legally entitled to such information.
- A member shall take all **reasonable precautions** to ensure that no information about the affairs of a client is revealed to anybody not legally entitled to such information.
- A member may not **reveal** or **make use of** any information, not in the public domain, of any stakeholder, without the **express consent** of the stakeholder (party).



Ethical decision-making



Being ethical

- To be ethical is to:
 - Do right and not wrong
 - Be fair and not unfair and
 - Do good and not bad
- But ethical conduct is not only concerned about doing what is right, good and fair, but also about:
 - Being **responsible**
 - Considering the **interests of others** and
 - **Upholding formalised or known professional standards** in a particular workplace or profession.

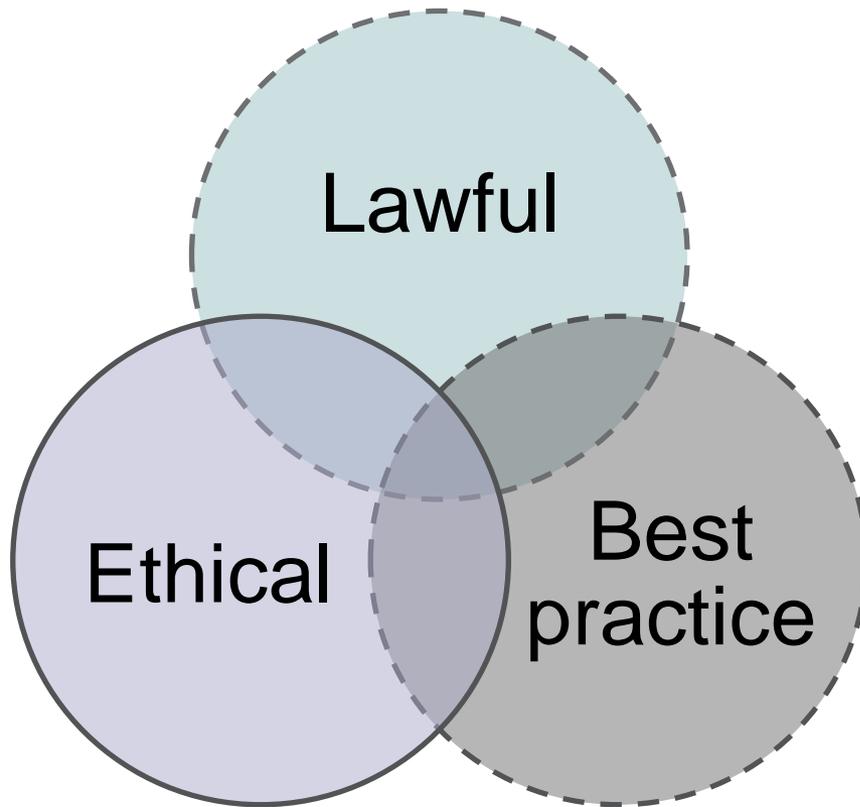


Test yourself

When you are not sure if something is ethical, ask these questions:

- Would my decision prejudice my client in any way?
- Can I be completely honest and transparent about it?
- What would my family, colleagues or manager say if they found out what I am doing?
- Would it affect my or my employer's reputation negatively if others found out?
- Would this be seen as professional?
- Would I be happy if I was treated this way?
- Is there a possible conflict of interest?

Use the three-legged chair test



Why are people dishonest?

[Video about dishonesty by Prof Dan Ariely](#)



Conclusion

Key learning points



Thank You

