

Connect › Support › Advance



**The Institute of
Internal Auditors
Australia**

Whitepaper

Conflicts of Interest: A Framework

MAY 2017

Conflicts of Interest: A Framework

Contents

Background	2
- Purpose	2
- Background	2
Discussion	2
- Issue	2
- History	2
- Discussion	2
Conclusion	5
- Summary	5
- Conclusion	5
Bibliography and References	5
Purpose of White Papers	6
Author's Biography	6
About the Institute of Internal Auditors–Australia	6
Copyright	6
Disclaimer	6

Background

Purpose

It is apparent from many investigations and reports from anticorruption bodies and regulators that conflicts of interest are a major threat to governance, compliance and ethical standards and cultures and a significant contributor to corruption.

In this white paper a framework is provided to operate in a comprehensive manner to reduce the risks associated with conflicts of interest and resultant fraud and corruption.

The framework may be used in designing governance structures and internal controls to mitigate the risks associated with conflicts of interest, enhance compliance processes, assist in probity projects and help auditors and investigators. It may be applied to employees, those providing services to an organisation and those who are likely to be seen as representing the organisation.

Background

Conflicts of interest are closely associated with corruption. For example it has been noted that conflicts of interest “can be an indicator, a precursor, or a result of corruption”.¹

Conflicts of interest and corruption are intertwined as a conflict of interest exists where an official could abuse his or her position for private gain, whereas corruption exists where an official does abuse his or her position for private gain². In practice conflicts of interest exist on a spectrum of severity.³

A structured and comprehensive approach to dealing with conflicts of interest and associated fraud and corruption is considered useful for practitioners, auditors and investigators.

Discussion

Issue

Conflicts of interest are a significant contributor to corruption and should be handled appropriately by any organisation.

History

Conflicts of interest have become a key issue of public interest and debate in recent years in both the private and public sectors⁴.

It is considered leading practice to implement policies, processes and governance structures to help ensure that conflict of interest situations are dealt with ethically and within the accepted probity principles.

In many jurisdictions if a decision-maker has a conflict of interest, the decision may be vulnerable.⁵

Discussion

There are many definitions of conflicts of interest. In broad terms a conflict of interest may be considered to exist where a reasonable person might perceive that an individual may be influenced in their work to place their own interest ahead of the organisation's⁶. The definition may also be adapted for legal entities.

¹ Managing Conflicts of Interest, Asian Development Bank, Organisation for Economic Co-operation and Development, 2008, p xiii.

² P. Catchick, Conflict of Interest – Gateway to Corruption, Fraud Magazine, January/February 2014, accessed on <http://www.fraud-magazine.com/article.aspx?id=4294980862> on 12 April 2017

³ Conflicts of interest, National Audit Office, United Kingdom, 2015, p. 6

⁴ For example see OECD Guidelines for Managing Conflict of Interest in the Public Sector, OECD Policy Brief, September 2005.

⁵ For example Article 6 of the European Convention on Human rights and articles 41 and 47 of the EU Charter of Fundamental Rights enshrine the principle that decisions should be made free from actual and apparent bias.

⁶ This would include the interests of close friends and family.

Conflicts of Interest: A Framework

An example of a definition is: "A conflict of interest is a set of circumstances that creates a risk that an individual's ability to apply judgement or act in one role is, or could be, impaired or influenced by a secondary interest. It can occur in any situation where an individual or organisation (private or government) can exploit a professional role for personal or other benefit. This definition is based on generally accepted standards."⁷

Conflict of Interest Control Framework

The framework for controlling conflicts of interest is to:

1. Clarify conflicts of interest for everyone at risk so that they can recognise conflict of interest situations and know what they need to do.

2. Help people avoid the conflicts of interest that should be avoided.
3. Require individuals to declare formally and properly any conflicts of interest that they may have.
4. Require individuals to manage their conflicts of interest with their managers and monitor the situation.
5. Deal with breaches of the rules so that infringements are properly investigated and remedial action taken.

⁷ Conflicts of interest, National Audit Office, United Kingdom, 2015, p. 6

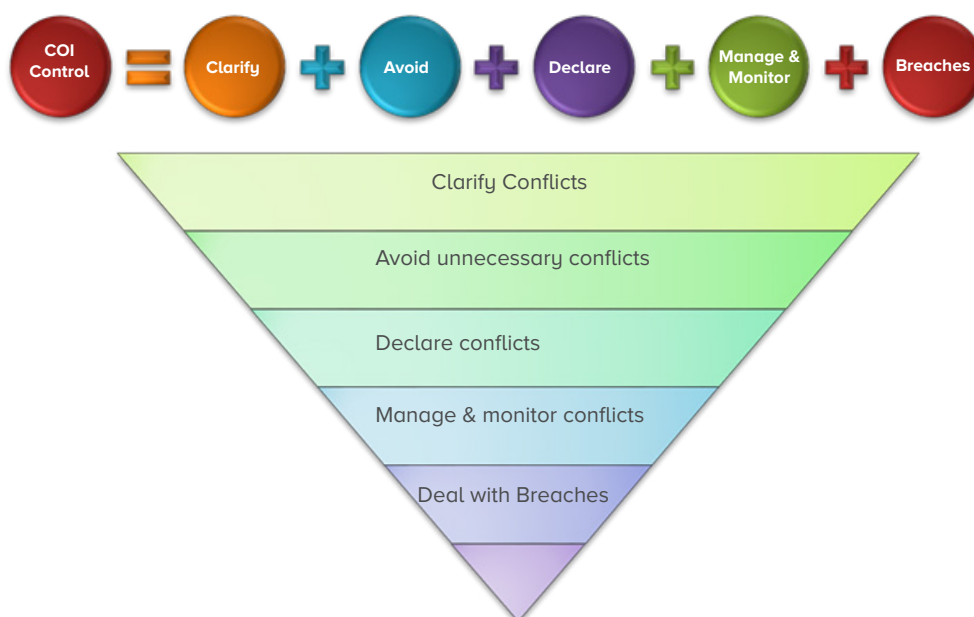


Diagram A: Process in an Organisation to Deal with Conflicts of Interest

Clarify

It is essential that people understand what constitutes a conflict of interest and what they need to do if they may have one. If they do not understand conflicts, they will not know how to avoid those that should be avoided, declare conflicts properly or avoid favouring their own interests. If people do not know how to recognise conflicts and what to do, the likelihood of corruption increases dramatically.

Activities to clarify conflicts should generally include an

appropriate section in the code of ethics/conduct, training that includes conflicts of interest and ready access to information about conflicts. The measures taken should be in line with the risks attached to possible conflicts of interest. Where the risks are high, best practice might include a policy and/or written procedures on conflicts, easy access to detailed information which includes relevant examples and likely questions, training that addresses in detail the relevant situations that may be faced, regular reminders and easy access to specialist advice.

Conflicts of Interest: A Framework

Examples of high risk activities may include tendering, hiring and other decisions with high levels of discretion and significant probity requirements.



Avoid Unnecessary Conflicts

There are many conflict of interest situations that are easily and beneficially avoided. This includes not interacting with people over whom one makes significant discretionary decisions in a way that could give rise to the perception of a personal interest. It is easy to avoid socialising with or accepting large gifts, benefits or hospitality from such people. In some industries or sectors there is a significant risk of your organisation's employees being sought out and groomed in the expectation of more favourable treatment by them in discretionary matters. Secondary employment rules should be implemented to avoid conflicts.



Declare Conflicts

Conflicts of interest should always be declared in writing. This avoids disputed accounts of what was actually said and whether the full extent of the conflict was properly declared. Conflicts of interest should be declared to people at a sufficiently senior level in the organisational structure or to a central area. If a conflict of interests register is maintained by the organisation, there should be a process to ensure that all declared conflicts are entered in the register.

In addition to the above declaration structure, conflicts of interest should also be formally disclosed for processes where probity is an important issue. Examples include hiring, tendering, high value asset disposals and the selection of entities for significant business relationships. In these cases

the declaration should always be documented and fully minuted.



Manage and Monitor Conflicts

The relevant manager should review the written declaration of a conflict and, together with the individual who has the conflict, work out a plan for managing the conflict. There should generally be guidelines to assist the managers to assess what actions are appropriate in different situations to adequately manage the conflict.

The default for serious breaches should ideally be for the employee to have no further involvement in the situation. This is not always practical and other alternatives might be considered.

The management plan should typically include the requirements for the employee to:

- always place the organisation's interests ahead of any personal interests;
- not communicate with other employees or entities acting on behalf of your organisation in a manner that could be perceived as trying to influence their conduct or decisions in relation to the matter;
- not obtain documents and information from the organisation relating to the particular decision, transaction or matter;
- not use the organisation's resources, or those of an entity acting on behalf of or for the organisation, for their personal interests in a conflict of interest situation;
- monitor the conflict of interest situation;
- make a new declaration in a year's time if the conflict still exists; and
- make a new declaration if the employee's personal interests or role in the organisation changes significantly.

Where a person no longer deals with a matter because of conflicts of interest, that matter should generally not be

Conflicts of Interest: A Framework

handled by a subordinate. The person handling the matter should never be supervised on that matter by the person with the conflict.

The management plan should be signed by both the manager and the employee. If a register of conflicts of interest is maintained it may be appropriate to have a copy of the management plan placed in the register.

The manager should periodically monitor that the employee is complying with the management plan.



Deal with Breaches

Breaches of the code of conduct or policy requirements should result in the matter being properly investigated and where appropriate, action being taken. The action may include disciplinary action, discretionary decisions being reconsidered, contracts being cancelled or renegotiated, administrative action being taken against entities associated with the employee's personal interest, legal action against the employee or other entities, reporting to regulators or anti-corruption bodies and preparing police briefs if criminal acts appear to have occurred.



Conclusion

Summary

The framework for controlling conflicts of interest is to clarify conflicts of interest for everyone at risk so that they can recognise conflict of interest situations and know what they need to do, help people avoid the conflicts of interest that should be avoided and require people to declare formally and properly any conflicts of interest that they may have, manage their conflicts of interest with their managers and monitor the situation and deal with breaches of the rules so that infringements are properly investigated and remedial action taken.

Conclusion

If conflicts of interest are not dealt with properly, the risks associated with fraud and corruption are likely to increase significantly.

Bibliography

- Conflicts of Interest and Risk Governance, Carlo V. di Florio, U.S. Securities and Exchange Commission, 2012, <https://www.sec.gov/news/speech/2012-spch103112cvdhtm> accessed on 12 April 2017
- Managing Conflicts of Interest in FMA Agencies, Australia National Audit Office, 2014, Canberra
- Managing Conflicts of Interest in the Public Sector – Guidelines, 2004, Independent Commission Against Corruption and Crime and Misconduct Commission Queensland
- Managing Potential Conflicts of Interest Arising from the Bank's Commercial Activities, Reserve Bank of Australia, <http://www.rba.gov.au/payments-and-infrastructure/payments-system-regulation/conflict-of-interest.html> accessed on 12 April 2017
- Related party transactions - Regulatory Guide 76, Australian Securities & Investments Commission (ASIC), 2011

References

- Managing Conflicts of Interest, Asian Development Bank, Organisation for Economic Co-operation and Development, 2008
- P. Catchick, Conflict of Interest – Gateway to Corruption, Fraud Magazine, January/February 2014
- Conflicts of interest, National Audit Office, United Kingdom, 2015

Conflicts of Interest: A Framework

Purpose of White Papers

A White Paper is an authoritative report or guide that informs readers concisely about a complex issue and presents the issuing body's philosophy on the matter. It is meant to help readers understand an issue, solve a problem, or make a decision.

Author's Biography

Written by: Barry Davidow
BCom, B.Acc, MTaxLaw, ACA, CFE, CRMA, PFIIA, Advanced Diploma of Government (Management), Diplomas in Risk Management and Business Continuity, Government (Fraud Control), Government (Investigation) and International Financial Management.

Barry is a Director of Fraud Prevention & Governance Pty Ltd and has over 20 years' experience in internal audit, fraud and corruption control, investigations, governance and compliance. He has contributed to books on fraud control, computer fraud, communications and sociology. He co-authored the IIA Australia white papers on Fraud Risk Indicators, Corruption Indicators in Internal Audit and Corruption-related risks in decision-making.

Matthew Lyon
BComm, CPA, MIAA

Matthew has been involved in internal audit for 10 years in the NSW Government. Prior to this he was Financial Accountant for Catholic Education Office Parramatta. He spent 15 years with the Audit Office of NSW, the last four as engagement manager. He has also served in a number of charities and the Wollongong Council Audit and Finance Committee. He co-authored the IIA Australia white papers on Fraud Risk Indicators, Corruption Indicators in Internal Audit and Corruption-related risks in decision-making.

Edited by: Michael Parkinson
BSc (Hons), Grad Dip Computing, PFIIA, CIA, CRMA, CISA, CRISC

About the Institute of Internal Auditors–Australia

The Institute of Internal Auditors (IIA) is the global professional association for Internal Auditors, with global headquarters in the USA and affiliated Institutes and Chapters throughout the world including Australia.

As the chief advocate of the Internal Audit profession, the IIA serves as the profession's international standard-setter, sole provider of globally accepted internal auditing certifications, and principal researcher and educator.

The IIA sets the bar for Internal Audit integrity and professionalism around the world with its 'International Professional Practices Framework' (IPPF), a collection of guidance that includes the 'International Standards for the

Professional Practice of Internal Auditing' and the 'Code of Ethics'.

The IPPF provides a globally accepted rigorous basis for the operation of an Internal Audit function. Procedures for the mandatory provisions require public exposure and formal consideration of comments received from IIA members and non-members alike. The standards development process is supervised by an independent body, the IPPF Oversight Council of the IIA, which is appointed by the IIA–Global Board of Directors and comprises persons representing stakeholders such as boards, management, public and private sector auditors, regulators and government authorities, investors, international entities, and members specifically selected by the IIA–Global Board of Directors.

IIA–Australia ensures its members and the profession as a whole are well-represented with decision-makers and influencers, and is extensively represented on a number of global committees and prominent working groups in Australia and internationally.

The IIA was established in 1941 and now has more than 180,000 members from 190 countries with hundreds of local area Chapters. Generally, members work in internal auditing, risk management, governance, internal control, information technology audit, education, and security.

Copyright

This White Paper contains a variety of copyright material. Some of this is the intellectual property of the author, some is owned by the Institute of Internal Auditors–Global or the Institute of Internal Auditors–Australia. Some material is owned by others which is shown through attribution and referencing. Some material is in the public domain. Except for material which is unambiguously and unarguably in the public domain, only material owned by the Institute of Internal Auditors–Global and the Institute of Internal Auditors–Australia, and so indicated, may be copied, provided that textual and graphical content are not altered and the source is acknowledged. The Institute of Internal Auditors–Australia reserves the right to revoke that permission at any time. Permission is not given for any commercial use or sale of the material.

Disclaimer

Whilst the Institute of Internal Auditors–Australia has attempted to ensure the information in this White Paper is as accurate as possible, the information is for personal and educational use only, and is provided in good faith without any express or implied warranty. There is no guarantee given to the accuracy or currency of information contained in this White Paper. The Institute of Internal Auditors–Australia does not accept responsibility for any loss or damage occasioned by use of the information contained in this White Paper.