

CONFLICTS OF INTEREST AND ETHICS IN GOVERNMENT

BRIEFING NOTE: SEPARATION OF PUBLIC AND PRIVATE INTERESTS

I. Overview:

This memo analyzes the issues that arise in the attempt to separate the public and private interests of public officials. It also analyzes the different ways in which various conflicts of interest regimes attempt to deal with these issues.

II. The Nature of the Challenge of Conflicts of Interest:

Concerns regarding conflicts of interest between a public official's private interests and their public duties ("conflicts of interest") are motivated by the underlying principle of ensuring impartiality and integrity in government decision making. Every citizen has the right to believe that their government officials – elected and unelected – are acting in the public interest and not in pursuit of their private interests. The perception that public officials are furthering their own private interests and not the public interest has a corrosive effect on public confidence in government and threatens the democratic legitimacy of government.

It is necessary to be precise in identifying various classes of conflicts of interest. All public officials will have some *inherent conflicts of interest* by virtue of being members of society. Many government decisions will affect them as taxpayers, parents, homeowners, etc. Generally, the larger the class of persons to which the public official belongs, the less we are concerned about the public official benefiting from these sorts of conflicts. However, rules regarding the use of confidential government information (or "insider information") target these sorts of conflicts (for example, a public official may know about pending tax changes that will have a significant impact on some types of publicly-traded securities and may act on this insider information in order to advance their private interests). Typically, sanctions are quite strong for these sorts of abuses.

Representational interest conflicts are another class of conflicts that are similarly unavoidable. By virtue of their membership in an identifiable group, public officials will have some interest; for example as members of a particular profession or industry (farmer, fishers), or residents of a particular community or city. As a general matter, most democratic systems of government encourage the promotion of such group interests in the public arena and elected representatives are often viewed as "champions" of their community or group. It is possible, however, that greater concern may arise when Ministers make decisions in such circumstances.

Of greatest concern is the sort of conflict that arises when a public official makes a decision where only they, or members of their family or close associates, will benefit.

III. Methods of Addressing the Challenge of Conflicts of Interest:

There are a number of recognized types of methods to address and control conflicts of interest between a public official's private interests and their public duties. These are *disclosure*, *avoidance*, and *recusal* (also called withdrawal). Each type of mechanism will be reviewed below.

A. Disclosure

Disclosure techniques generally require that certain public officials reveal their assets and liabilities. Generally, full disclosure is required to an independent official such as the Commissioners under the Canadian acts. Selected public disclosure may follow. In the country studies, we also saw that disclosure regimes were established for other matters that could potentially influence a public official's decision making such as gifts over a certain amount, offers of employment, etc.

The principle behind disclosure is the adage first enunciated by the American Supreme Court Justice Louis Brandeis that "sunlight is the best disinfectant". Disclosure promotes transparency and enables the public to better scrutinize public officials' decisions. As stated in the U.S. memo, disclosure also allows the public to feel confident that their elected representatives, and other public officials, are able to fill their public roles free from undue conflicts.

The efficacy of a disclosure regime in preventing conflicts of interest is affected by a number of factors. First, its efficacy may be limited if disclosure is only partial. Thus, there must be some process or person in place to ensure full disclosure. If disclosure is voluntary or there is no effective penalty for incomplete disclosure, this mechanism may be ineffective. Similarly, there are differences between *private disclosure* and *public disclosure*. Any regime of disclosure must take into account the legitimate privacy interests of a public official and their family but a regime that favours private or public disclosure is unlikely to be effective unless there is a well-resourced independent watchdog. Most regimes rely on legislators, the press or civil society groups to identify and publicize potential conflicts of interest. When too much information is kept confidential, accountability suffers. Thirdly, the nature of the public disclosure is important. There is a difference between making information available upon request and releasing it to the public by posting it on a government internet site. Thus, to take the example of government expenses, the Canadian federal Government now posts such expenses monthly on government department websites while in Ontario such information is available only through access to information act requests which take significant time and effort on the part of the person making the request

Further, there may be a fear that by making public declarations too thorough qualified candidates may not joining the public service because of their desire not to publicly disclose their assets.

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B. Avoidance

Avoidance requires public officials to take affirmative steps to avoid conflicts of interest, most often through the *divesting* of certain assets by their sale or by the transfer to a *blind trust*. The concept of a blind trust is that a public official transfers all assets into a trust which is managed by a trustee and the public official plays no part in the management of the business or investments under the trust. There are a number of advantages and challenges to the blind trust process.

The efficacy of the trust is a function of a number of factors, some of which involve the character of the trust and others its structure. First, the trust works best with *passive investments* like securities, bonds, commodities etc., because they are not unique and easily fungible. These types of assets can easily be sold and bought such that the public official may not know the contents of the trust. In this sense the trust remains blind because the public official does not know its contents.

However, when the assets transferred into the trust consist of an active business, the trust may be less effective in preventing conflicts of interest because the public official will still be able to identify his or her private interest, despite not playing an active role in the operation of the business. In the case of very large holdings, the perceived protections against the conflicts of interest may be somewhat illusory. For example, the former Canadian Finance Minister (and eventual Prime Minister) Paul Martin built up one of the world's largest shipping companies (Canada Steamship Lines) before he entered politics. Upon entering politics and becoming the Minister of Finance for Canada he placed his holdings in a blind trust and had no involvement in the day to day operations of the company, nor in any of the company's strategic decisions. However, as Minister of Finance he would have made thousands of decisions that affected his former business. When Mr. Martin became the leader of the Liberal Party of Canada and the Prime Minister in waiting, he transferred all of his interests in this company to his sons in part to alleviate such concerns. While this seemed to satisfy his critics, it raises a further point about the extent of what should be considered one's private interests. In short, is there much difference whether a public official or his close relative will benefit from a decision by that official? Increasingly, conflict of interest codes explicitly recognize this reality.

On the structure of a trust, its efficacy will be limited if it is not truly blind – that is if the public official is able to see into the trust or worse to interfere in its operation. The identity of the trustee is critical. Ideally, the trustee would be an unrelated, arm's length third party. This is more easily accomplished in passive investments than in active ones that involve the running of a business. For active investments, this may be unrealistic and undesirable. Often it will make sense in such cases for the trustee to be a person who is intimately familiar with the running of the business. Thus, in Ontario several years ago, the Integrity Commissioner reprimanded a Minister for failing to disclose that the trustee (who was the CFO of the company in the trust) was also the treasurer of his local political party association. The problem was not that the trustee was also the CFO of the company, but rather that the Minister had failed to disclose this political connection between himself and the trustee.

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In all cases, but especially in active investments, it is important that contacts with the trustee be restricted, regularized and disclosed, lest there be an appearance of attempting to meddle in the operation of the business. Thus, in the same Ontario case (Takhar), it was disclosed that the Minister visited the place of business, meeting with his wife (the President and CEO of the company) and the CFO/Trustee for several hours. While the Integrity Commissioner found that the Minister had not violated the Act, he also found that the Minister was “egregiously reckless” in meeting at his former place of business with his wife and the CFO-trustee, virtually inviting a complaint for breach of the Act.

C. Recusal

Recusal (or *withdrawal*) refers to the non-participation of public officials in matters where they have a personal financial interest.

Recusal requirements are found in many conflicts codes. Typically, they require an open declaration of a conflict coupled with a recusal. The recusal is often noted by some civil servant and may be publicly disclosed. As a mechanism for separating public from private interests, recusal appears quite attractive. It is meant to ensure that a public official takes no part in a decision that affects their private interests. However, there are complications and costs associated with recusal.

An effective recusal regime requires more than simply that the public official not vote on the issue affecting their private interest or take part in the final decision. This is because there are many ways and opportunities to affect a decision prior to the point where it is finally made, through a vote or otherwise. It is therefore important that recusal take place at the earliest stage, prior to the matter coming for actual decision.

Effective recusal regimes, “screen” affected public officials from any information relating to the subject matter of the officials’ private interest. For instance, if the public official held shares in a public or private company, an effective recusal regime would prevent any information from coming to the affected official and also designate a responsible official for matters involving the company. It thus becomes critical under such a system to pro-actively identify real or potential conflicts of interest for the public official in order to establish such screening mechanisms in advance.

Such mechanisms are not without their costs. If the public official is not able to deal with particular issues, this may place significant burdens on others who are designated to make decisions in that official’s stead. If the public official is a Minister, there are further potential costs. Delegation by an elected official to an unelected civil servant raises problems of democratic accountability. Who will be publicly accountable for this issue either in the Legislature or to the press? While another Minister may be designated to answer on this file, if the Minister is not responsible for the decision making but only accountable for the decisions made by other non-elected officials this process is problematic from the perspective of democratic accountability. It is preferable if another Minister is both responsible for decision making on the affected file(s) as well as publicly

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accountable for them. This is unlikely to be a problem if the affected file(s) relate only to minor matters but if they relate to significant areas of a minister's portfolio this may not be optimal in terms of public administration. For example, in Ontario in 2003, the Minister of Finance was under investigation by the Ontario Securities Commission a body normally under his supervision. The Ontario Government addressed this problem by transferring responsibility for the Ontario Securities Commission to another Minister, although responsibility remained with the Ministry of Finance. As a result, the Minister responsible for the Ontario Securities Commission had to deal with two sets of civil servants: his own plus those from the Ministry of Finance on matters relating to the Ontario Securities Commission. While this was not an ideal situation, it was considered acceptable because of the high esteem in which the affected Minister of Finance was held by the Government and by the financial community.

Effective recusal regimes also require transparency. Especially when it comes to collective decision making that is not taken in public (such as decisions of Cabinet), it may be tempting for Ministers not to recuse themselves from the decision making process. The rationale may be that if there is no recorded vote that will ever be disclosed to the public, there is little incentive to disclose an actual or potential conflict of interest. The counterpoint to this may be that in cases of collective decision making where a public official is only one of many votes, there is little cost to the affected official to recuse themselves from the decision making process. In either event, a pro-active approach to identifying actual or potential conflicts of interest facilitates the recusal process and avoids conflicts of interest.

Moreover, a recusal regime presents the issue of the tension between experience and conflicts. There may be a public benefit to government decision making made by those with significant experience in the area. However, if a Minister has experience in the area as a result of continued private interests such as an ongoing business, the Minister may be required to recuse himself or herself from too many decisions to be effective. Thus, in the example previously provided of Canada's former Finance Minister who owned a large shipping company, it would have been problematic for him to have been the Minister responsible for the shipping industry because while he likely had the greatest expertise in the area, he would have had to recuse himself from most decisions.

D. Additional Comments Regarding Different Methods of Addressing Conflicts of Interest

As the above analysis has demonstrated, neither one of disclosure, avoidance or recusal only on their own is likely to be successful in avoiding conflicts of interest. Most conflicts regimes combine elements of each. In each case, in order for the technique to be successful, it likely necessitates some element of transparency and public disclosure as well as an independent oversight mechanism. The experience in Canada at least has been that where conflicts rules are merely advisory or lack truly independent oversight they are unlikely to be effective.

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IV. Additional Challenges:

Over the past two decades in countries like Canada and the United States, greater attention has been focused on the influence that lobbyists and campaign donors (sometimes one and the same persons) may have on the democratic process. Increasingly, regulatory reforms have introduced regimes of public disclosure of lobbying and of campaign contributions. Over the past decade Canada has significantly reformed its electoral finance laws, banning all corporate and union donations and significantly restricting individual donations. These private sources of funding have been replaced by a system of public subsidy and all donations over \$100 must be reported and publicly disclosed.

The challenge is how to impose stringent requirements to avoid conflicts of interest without preventing qualified persons from seeking public office.

In this, the United States is a bit of a paradox. It has some of the strongest conflict of interest requirements which continue to be strengthened (see the January 21, 2009 Executive Order of President Obama). It also has no problem attracting public officials for both elected and non-elected office who have significant private holdings / wealth. In part, this is due to the history and political culture of the United States which sees public service as a valuable and respected public good.

V. References:

See all references in country studies, especially United States (Federal).

Executive Order 13490 - Ethics Commitments by Executive Branch Personnel, Signed by President Barack Obama, January 21st, 2009, online: http://www.whitehouse.gov/the_press_office/ExecutiveOrder-EthicsCommitments/

The Honourable Coulter A. Osborne, Integrity Commissioner, *Report re The Honourable Harinder Takhar, Minister of Transportation and MPP for Mississauga Centre* (January 4, 2006), online: <http://integrity.oico.on.ca/oic/OICweb2.nsf/OICFramesEn?OpenFrameset>

Margaret Young, "Conflict-of-Interest Rules for Federal Legislators", Parliamentary Research Bureau, Library of Parliament (Canada) (Revised 18 May 2004).