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Corporate Practices for Managing Conflict of Interest in Terms of ESG Standards

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Abstract. The global agenda for the integration and development of Social care and Corporate Governance (ESG) standards determines the necessity of the legal community attention to the tasks of regulatory, methodological, organizational support for their implementation in the business companies activities in the narrow focus on the conflict of interest prevention issues. The article analyzes and evaluates the consistency of measures aimed at eliminating personal interest, corporate disputes represented in ways of conflict of interest managing between the company, its managers, and employees, including relations with counterparties and affiliated persons context appearing during its business activities. The article provides an overview of corporate practices for managing conflict of interest in companies of banking, stock exchange and investment industry. Moreover, it observes the dialectical connection of the admitted conflict of interests with the processes of determination of tort and criminogenic consequences, including those reflecting in financial, corruption, official and economic crime. The study noted the role of conflict of interest management in ensuring the company social and corporate policy in the context of protecting the interests of employees, its customers, counterparties, minimizing its possible occurrences and consequences by the forces of internal control and audit, and compliance as well. The article emphasized the differences in the conflict of interest prevention concepts which are typical for public (state) and business services. In conclusion, the study revealed the methodology content for managing conflict of interest in the business activities, based on personnel administration, compliance with ethical standards, the culture of declaring conflict of interest, and limiting proprietary information circulation.

Keywords: conflict of interest, management policy, business companies, personal interest, prevention, loss of assets, corruption risks, anti-corruption standards, financial crime, corporate governance, corporate disputes, affiliates, counterparties, information control, “Chinese wall”, compliance, banking industry, stock exchanges, investments, ESG standards.

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Корпоративные практики управления конфликтом интересов в аспекте стандартов ESG

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Аннотация. Глобальная повестка внедрения и развития стандартов социальной заботы и корпоративного управления (ESG) обуславливает необходимость внимания юридического сообщества к задачам нормативного, методического, организационного обеспечения их имплементации в деятельность компаний бизнес-среды в узком фокусе темы предупреждения конфликта интересов. В статье анализируется и оценивается состоятельность мер, направленных на исключение личной заинтересованности, корпоративных споров, выраженных в способах управления конфликтом интересов между компанией, ее руководителями и сотрудниками, в том числе в контексте отношений с контрагентами и аффилированными лицами, которые возникают в ходе бизнес-деятельности. Приводится обзор корпоративных практик управления конфликтом интересов в компаниях банковской, биржевой и инвестиционной сфер деятельности. Отмечается диалектическая связь допущенного конфликта интересов с процессами детерминации деликтных и криминогенных последствий, в том числе выраженных в финансовой, коррупционной, должностной и экономической преступности. Отмечается роль управления конфликтом интересов в обеспечении социальной и корпоративной политики компании в разрезе защиты интересов работников, ее клиентов, контрагентов, минимизации его возможных проявлений и последствий силами внутреннего контроля и аудита, а также службы комплаенс. Отмечаются различия в концепциях предотвращения конфликта интересов, характерных для публичной (государственной) и деловой (частной) службы. Раскрывается содержание методологии управления конфликтом интересов в бизнес-среде, основанной на кадровом администрировании персонала, соблюдении этических норм, культуре декларирования коллизии интересов, ограничении оборота служебной информации.

Ключевые слова: конфликт интересов, политика управления, бизнес-компании, личная заинтересованность, предупреждение, утрата активов, риски коррупции, антикоррупционные стандарты, финансовая преступность, корпоративное управление, корпоративные споры, аффилированные лица, контрагенты, информационный контроль, «китайская стена», комплаенс, банковская сфера, биржи, инвестиции, стандарты ESG.

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Introduction

The preventive potential of the conflict of interest risks containment system in business companies lies in their management. This is the mechanism that ensures the implementation of two of the three principles – Corporate and Social – in the framework of global agenda for the development of companies in ESG (Environmental, Social, Corporate)standards. These standards allowinvolving companies in solving of management issues, connected to the establishment of fair treatment to employees, counterparties, and society on one side, and to the provision of internal control and audit, information disclosure on the other one(Smirnov, 2020).

Statement of the problem

The conflict of interest in business companies has different forms. Their nature and content are defined by the corporate governance features (in prerogatives of collegiality or unity), the specifics of business processes, the range of business ties, the dispositive or imperative character of treaty relations, the balance of discrete or directive decision-making, the volume of authority, the vastness of anti-corruption restrictions andprohibitions for employees. These and other basics of company management are chosenand aimed at providing its successful functioning and development. However, these basics can produce conditions for collision of personal and corporate interests, regarding property and intangible assets – Goodwill – which belong to the company, but they are used in personal interests of employees and affiliated people.

The range of conflict of interest subjects can be wide, for instance, company's shareholders, managers, employees, holding corruption dangerous positions. More often, the conflict of interestreflects in corporate disputes, connected to the management issues or the participating of legal entity, the determination of shares ownership in the authorized capital, profit distribution, assets turnover, causing and compensation of losses, recognition and appeal of transactions or decisions, other civil legal relations in business sphere. Competitors, pseudo partners, monopolists, raiders, corrupts can hide behind the arguments, produced by the conflict of interest. In such cases, unprevented conflict is not finished and serves to mentioned beneficiaries. It can be a basis for official, economic, corruption activities. Also, it can determine the threats for the company – its bankruptcy or raider seizure.

Considering the risks of such dialectical result of conflict of interest, prevention of its tort and criminogenic features for business companies is possible if they are controlled at the early stages, butnot settled as in the public service.

Methods

To examine mentioned differences, comparative legal research of existing practices, using the synthesis method regarding concepts, analysis and evaluation of corporate regulatory acts in relation to meaningful risk classification of conflict of interest and its preventive measures are necessary.

Discussion

Different definitions do not change the essence of aims of conflict of interest prevention in neither business nor public service. For the last one the imperative of conflict of interest prevention standards, represented in requirements of anti-corruption legislation, is typical. Corruption prevention standards are unified in the laws for officials and have standard composition of acts in case of violation. Collisions of interest are similar to them. This circumstance determines the precedent nature of settlement methods. At the same time, the admitted personal interest creates negative legal consequences for officials, defined in disciplinary measures. Tort and criminogenic features of conflict of interest development are stopped and, during detectionof consequences, the prosecution of the perpetrators and the protection of violated rights is carried out in a public way, using all the potential of state legal enforcement.

In business sphere anti-corruption standards are established by the company's local acts and are determined by the sufficiency standards to achieve goals of corruption prevention according to the Article 13.3 of Feder-

al Law dated 25th December 2008 No. 273-FZ "On counteraction to corruption". The content of anti-corruption measures, including conflict of interest prevention, remains at the discretion of companies, based on the number of features (let's mention the most important):

- basics of corporate governance (reporting to shareholders or owners, the procedure of decision-making (collegial or sole), the presence of subsidiary and affiliated organizations, the system of management independence from owners and transparency of their activity, the exclusion of control and executive labor functions combination);
- state and procedure of the provision of labor resources (lack of qualified people, sources and ways of their involvement or renewal, requirements for the candidates, existing labor dynasties);
- structure of business activity (foreign economic relations, the presence of dealers and franchise, treaty principles of cooperation with counterparties);
- ethical and corporate discipline standards (requirements to official behavior, welcoming and business gifts standards, procedure for considering of appeals and communications);
- internal social policy (rewarding, bonuses, compensation and promotion programs to motivate productivity and career growth (paying for tuition, professional development courses, medical services and sport)).

The absence or inaction of one or several mentioned factors can predetermine the cases of personal interest of the employee and lead to a conflict. Early neutralization of conditions and causes, which favor the occurrence of conflict of personal and corporate interest in business companiesis connected to the issues of quality provision of corporate governance in general. The prevention of conflict of interest by the elimination of personal interest measures are used last, when the institutional factors, which help to stop it on the level of causes and conditions, do not work.

Such concept of conflict of interest management in business companies is reasonable. The argument is the paradigm of difficult substitutability of qualified specialists who have narrow competencies, rare experience of top managing or employees who replace positions exposed to corruption risks. Their professional growth in the company, training at its expense, or even recruiting from outside are expensive. The personnel value of these people is formed by an asset which is expressed in their intellectual property objects with exclusive rights, and which are in demand for the company's business processes. Also, there is another situation, when it is necessary to give these people the access rights to company's delicate information (commercial secret, information of limited circulation, official or confidential information). In this case, it is highly undesirable to dismiss an informed person, involved in the conflict as soon as it creates risks for company's stability and its competitiveness. This actualizes the tasks of conflict of interest management in the preventive maintenance of control measures, monitoring the performance of labor functions, access restriction to delicate information, changing job responsibilities.

It is notable that dismissal of officials for not taking measures to prevent or resolve conflicts of interest, including the cases when it creates prerequisites for corruption, is one of the anti-corruption tools.

In business companies such approach is counterproductive and presumption of guilty principle, connected to not taking measures to prevent conflict of interest, is excluded, regarding employees. The execution of anti-corruption standards is provided by the implementation of organizational and managerial measures, provision of conditions for non-acceptance of behavior forming their violation, but not by the enforcement under the threat of responsibility. Even though the conflict of interest prevention is mutual obligation of employer and employee (as well as in public service), mainly employers take the initiative because they are interested in provision of interest balance, saving personnel, their protection from third-party influence, prevention of conflict consequences.

Theconceptual approaches to conflict of interest prevention are unchangeable in business sphere. At the same time, models and methods of their occurrence risks managing are different in business companies. The exam-

ple of industries shows similarities and differences of the best practices of conflict of interest governance. It is possible to study corporate prevention policiesbecause of their transparency and availability for research in the form of public documents.

• ***Banking industry***. The experience of PJSC "SBER" is suitable to illustrate the conflict of interestmanagement examples in banking activity sphere. Being a part of compliance risk management system, the content of organizational, methodological, regulatory standards of conflict of interest prevention is fixed in a separate local corporate act – "The conflict of interest management policy of Group of companies PJSC "SBERBANK" (here – Policy) (Policy, 2019).

The experience of the company is twice as significant because the Policy applies as to banking activity as to entire internal ecosystem which covers services and sales, IT-industry, media and entertainment, logistics and real estate, medical and educational content, digital resources for everyday and business life. The Policy obtains universal features of standards action in a wide range of space and people, showing the effect of the globalization of internal corporate law. It covers and regulates relations which are beyond the borders of classical activity in financial and credit sphere. This circumstance allows not only to illustrate typical cases of conflict of interest prevention in banking industry, but it also to transmit their universality for business environment in general. This effect is also achieved because the Policy is incorporated with the purposes of preventing the manifestations preceding the conflict of interest, which are considered by the compliance risk management system (legal, reputational, foreign economic) (Compliance risk, 2013; Loss of business reputation risk, 2015; Legal risk, 2017; Participating, 2018).

The prerogative of conflict of interest management (also potential) is not determinedin solidary obligations of the employee and the employer's representative, but in functional tasks of special department – compliance committee. This approach excludes the scenario in which conflict of interest risk, mutually unsettled by employer and employee, leads to tort qualification, committed by the last one. Such situation is typical for officials – not taking preventive measures is correlated with their presumption of guilty.

Corporate conflict of interest management system is expressed in management procedures of informational and control purpose. They allow to preventively exclude the causes and conditions of situations which lead to the occurrence of personal interest. At the same time, these measures do not include significant employees' obligations which reflects institutional, "on top", principle of conflict of interest management.

The following management measures are potentially effective inprocesses administration of managerial activity:

− creation of organizational structure, which clearly separates the responsibility, authority and reporting spheres;

− formation of collegial bodies and holding their meetings considering the principle of conflict of interest prevention;

− implementation of making collegial decisions practice on the most important and extensive issues.

These are the control components of conflict of interest management system:

− the practice of double control (the four-eyes principle);

− multi-level system of internal control (excluding the opportunity of hiding violations, risks, factors, and their evaluation as insignificant).

The informational procedures of conflict of interest management are expressed in:

− providing principle of department independence and "official necessity" in distribution of informational flows;

− establishment of informational barriers ("Chinese walls").

Considering administrative and control measures that are not difficult to interpret, let's focus on multifunctional capabilities of "Chinese wall" in the conflict of interest management system. Its content comprises company's business process organization principle which ensures the access and transmission of information, required for the execution of official activity by the employee or the department, ex-

posed to risks of conflict of interest occurrence, according to established rules. The object, creating risk, is information, the item is advantages of its owner. Subjects of these relations are departments and employees. The access to the information, which is necessary for execution of job duties, is possible only with multi-level approval. The ones who get the access are assigned the status – "above the wall", which entails the establishment of control and informational barriers. Here they are:

– *separation* of access to different data categories in informational systems among the users from different departments;

– *usage*of code wordsduring transmission of price-determining information and supervision of employees with access to it;

– *imposing confidentiality obligations* on people who have access to insider information, access restriction to it;

– *usage* of "official necessity" principle in distribution of informational flows;

– *monitoring* of transactions with securities in personal purposes, carried out by employees, who have access to proprietary information.

These measures of providing informational barriers reflect the sense of conflict of interest risk management. The primacy of "soft" measures is obvious. They are not connected to significant changes in employee's responsibilities, his discharge or reduction of obligations, transformation of statutory labor rights, entailing obligations or minimizing social professional guarantees, for instance, in case of rotation (implemented to prevent nepotism and favoritism of officials). At the same time, "soft" measures complete traditional methods in public service (transfer of employee, discharge, change of obligations). The standard of systematical conflict of interest declaration is distinguished: during applying for a job, when the situations occur, annually, preventively (before the events or obtaining information).

Such sequence (management, then settlement) shows the preventive sense of conflict of interest risks containment systems in business companies.

• ***Stock exchange industry***. The significance of this sphere for the conflict of interest prevention analysis is determined by some features. Stock market is a trading platform, and it originally has a wide range of participants with different interests: from external – investors, sellers and buyers as traders, representatives of the state control, to internal – brokers, shareholders, managers, specialists (analysts, economists, actuaries, depositories). In such extensive circle, affiliated links between all the participants have a high probability of extraordinary manifestations of collision of interest. Their prevention is dialectically connected to stock exchange tasks on excluding the unexpected risks which negatively influence the clients' wealth.

The conflict of interest prevention in stock exchange industry is crucial because of high level of crime, which are latent and has low disclosure. The conflict of interest of stock market participants can cultivate not only financial complex crime such as legalization of criminal means or manipulation of market, but also corporate official and economic crimes.

Specific of stock market activity, diverse circle of participants, objective and subjective phenomena of economic life, for example market volatility, quickly changing evaluation of assets liquidity, which depends on unexpected factors (politicians' statements, natural disasters, technogenic catastrophes, shareholders' health) create many conflicts of interest risks.

The example is "Moscow Exchange MICEX-RTS" (here – Exchange). The purposes of conflict of interest prevention are expressed in its Policy, described in a regulatory document (approved by the Supervisory Council of PJSC Moscow Exchange, dated 28.12.2018, Protocol No. 13) (here – Exchange Policy).

The features of the Exchange Policy are based on the conflict of interest management on isotropic basis (with the participation of independent directors) and on informational analytical provision, for example:

– collection and analysis of information about interconnected and connected parties, including the affiliated ones with important shareholders of the Exchange;

– collection and analysis of data about the structure of supervisory, collegial and sole executive bodies, affiliated society on the subject of conflict of interest;

– monitoring of legal disputes with the participation of the Exchange shareholders, members of governance body, affiliated society, depositories;

– informing of the Supervisory Council members about transactions with conflict of interest and members of the Management Board and shareholders about transactions which they are interested in. This information is transparent. It is posted on the Exchange website with the open access for all employees.

– if the employee finds an interesting transaction for members or with conflict of interest, the Supervisory Council is informed to get a transaction approval.

The element of Exchange Policy is a normatively defined list of measures, aimed to prevent the conflict of interest. They consist of permissive measures with restrictions: make transactions and operations, conclude trust management agreements regarding financial instruments with no access to insider information; make transactions with the Exchange shares by prior agreement with the Service of internal control and if there is no restrictive period for transactions, which is established to prevent personal interest of employees. This measure is temporary, it does not create an imperative prohibition for realization of personal property rights and interests as the Exchange trader. The exclusivity of conflict of interest prevention measures is due to stock market industry specifics, they are expressed in these prohibitions:

– do not use program complexes, assets of the Exchange, confidential and official information, got as a result of implementation of job obligations in personal interests;

– do not take part in any commercial or business activity which includes the usage of the Exchange property to get a personal benefit;

– do not work on the basis of civil legal agreement in companies, if the job is connected to the usage of Exchange assets and is executed during working hours;

– do not make transactions with opponent companies which can cause property damage to the Exchange and do not be a member of governance body in such companies.

The declaration of conflict of interest by the Exchange employee has administrative features. The information is analyzed by the Service of internal control which formulates and transmits recommendations to the director. So, the employee is a passive participant of conflict of interest prevention mechanism.

• ***Investment industry***. In this case, investments are represented in generalized content, which covers the activity of investment funds management companies. When the participants of investment services have a collusion of interest, it obstructs the execution of obligations by the management company or fund to provide services in honest, fair and professional way in client's interests.Provision of such services seems to be twice as difficult as soon as the sphere of assets placement aimed to make a profit is objectively exposed the probability of loss of investments andincome. The loss is produced both by the external integral risks, for example legislative, political, social, economic, financial, criminal, ecological, to which many special, long-running researchesare devoted (mainly economic)(Kulakov, 2004; Vaichulis, 2008) and by poorly studied internal factors, caused by the conflict of interest. The amount of such investment assets loss because of these factors may exceed negative consequences of integral risks, which can be predicted.The conflict of interest cases in this industry are latent and represented in officials' one-side actions (inaction) of investment companies (funds). These actions are:

– making a profit or escaping of financial losses at the expense of the client;

– providing services to the client or making a deal on his behalf which does not correspond to his interests;

– commitment in promoting the interests of one client against the interests of another one;

– getting reward from another person for the provided services etc.

By legal nature and content, mentioned conflict of interest cases are typical for another sphere of confidential provision of professional services, for example advocacy and mediation. The perspectives of development of corporate governance practices of conflict of interest are rather topical, despite the fact that there are industry Codes of Professional Ethics which con-

tain particular standards of conflict of interest prevention.

The requirements to identify and govern the conflict of interest in the sphere of investments are defined by the Central Bank of the Russian Federation (Guidance, 2020). Their institutional features deserve special attention.

For managing companies in the investment sphere prevention of conflict of interest is an obligation and the decisions to refuse prevention are disclosed no later than one day on the website. First of all, they inform the client whose rights are exposed to the risks and regulated in detail. That is how the transparency principle and risk control are provided. At the same time, a list of circumstances, excluding the conflict of interest qualification, was established, for example making a deal on unfavorable terms; making a permitted deal; making a deal with exceeded frequency in order to ensure the fulfillment of duties, defined in the contract with the client.

These circumstances have a propensity for corruption. It can consist in a subjective evaluation of facts (which allow to ignore the grounds and terms of the transaction) or in decisions with legal and linguistic ambiguity[1] (which is connected to the usage of vague and unstable concepts, semantic formulations: "favorable trends of investment climate", "risks of long-term investments limitation"). The argument which helps to exclude the propensity for corruption is classical requirements to investments as to "operations, based on detailed analysis of facts, the security of invested funds … in recognition of all the others as speculation" (Graham, 2014: 45).

Conclusion

Considering the multiplicity of business companies' field of activity and their affiliation to one or another industry (manufacturing, goods supply, provision of services), the concept of conflict of interestgovernance practices are not very different. The existing uniqueness of corporate governance policy is determined by the specific of objects, exposed to risks of loss, content of legal relations and circle of people, representing the participants of the conflict. The nature of conflict of interest is unchangeable which allows to consider the presented review and the content of governance practices as a suitable model for other companies.

[1] In the sense that is given in the Russian Federation Government Decree dated 26.02.2010 No. 96 "On anti-corruption expertise of regulatory legal acts and projects of regulatory legal acts" (Decree, 2010).

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