

been avoided? Do professionals have a greater duty to their profession or to their employer?

- How might the laissez-faire market perspective, represented by Milton Friedman, evaluate the

subprime mortgage fiasco? What responsibility do consumers have in this?

- Why should investors and clients trust the word of financial analysts and credit ratings firms?

READING 9.1

CONFLICT OF INTEREST

John R. Boatright

CONFLICT OF INTEREST

A conflict of interest is a situation in which a person has an interest that interferes with that person's ability to act in the interest of another when that person has an obligation to act in that other person's interest. This definition contains several crucial elements.

First, there must be an obligation to act in the interest of another. This kind of obligation is characteristic of fiduciaries, agents, and professionals (who are commonly agents and sometimes fiduciaries), all of whom are in positions of trust. A physician or an attorney, for example, like a trustee of a fund or a real estate agent, agrees, usually for a fee, to exercise specialized knowledge and skills for the benefit of another. As a result, there is an obligation, either explicit or implicit, to serve that other person's interest.

Second, there must be an interest that interferes, actually or potentially, with the ability of a person with such an obligation to act in another person's interest or, in other words, to exercise specialized knowledge and skill solely for the benefit of that person. The interest that interferes is usually some prospective financial gain, but it can be anything that a person values, such as family well-being or public recognition. A situation in which an interest actually leads a person to fail in an obligation to serve another's interest is usually called an *actual* conflict of interest, whereas the mere presence of a conflicting personal interest but no failure to fulfill an obligation is called a *potential* conflict of interest.

Third, interference means that the person fails or is likely to fail to serve the interest of another in a manner that meets some expected or required standard. A person with a conflict of interest may fulfill the obligation in question, either in full or in part. A conflict of interest may still be present, though, as long as the ability of the person to serve the interest of another is compromised to a significant extent.

Examples of conflict of interest include a physician who orders a test from a lab in which he or she is an investor; a judge hears a case in which a family member is a party; an executive owns stock in a supplier of her or his company; an accountant audits a company in which he or she holds stock; the administrator of a trust invests funds in a company that she or he owns; and an insurance broker is paid commissions by the insurer he or she recommends to a client. In each case, the person's objectivity or independence is compromised. The ability of that person to fulfill an obligation to serve others is reduced by a countervailing, personal interest.

The inability to fulfill an obligation in a conflict of interest is different from merely having a bias or a conflict of obligations. Thus, a judge who is biased against criminal defendants may fail to render justice, but the interference in this case comes from an attitude rather than some personal interest. The judge's judgment is biased but not influenced. Furthermore, an executive who has an obligation to choose the best supplier and also to favor a minority supplier has a conflict, but the conflict, if there is one, is between obligations that cannot both be fulfilled.

Not only persons but also organizations can be in conflict of interest situations. Law firms, advertising agencies, and investment banks, for example, serve many clients, and an interest in one client may interfere in the organization's ability to exercise unbiased judgment or unstinting diligence on behalf of another. For accounting firms to provide audit and consulting services to the same clients is often cited as a conflict of interest because they have an incentive to perform lenient audits to retain the more lucrative consulting services.

HISTORY OF THE CONCEPT OF CONFLICT OF INTEREST

Although conflict of interest has become a ubiquitous and increasingly important moral concept, it did not