
INFORMATION NOTE

Selected Issues Relating to Declaration of Interests and Avoidance of Conflicts of Interests by Senior Members of Government

1. Introduction

1.1 This note provides information relating to declaration of interests by senior members of government in the United States (US) and the United Kingdom (UK). Specific topics include 1) declaration of interests; 2) procedures to avoid conflicts of interests; 3) operation of blind trusts; and 4) operation of British Virgin Island (BVI) Companies. Senior members of government here refer to Cabinet Secretaries in the US and Cabinet Ministers in the UK.

2. Declaration of Interests

The United States

2.1 Cabinet Secretaries are required by law¹ to file the "Public Financial Disclosure Report" — SF278². SF278 is a public document, and any individual can file a request to see the document.

2.2 The categories of information to be disclosed are prescribed by law to include: assets and income; transactions; gifts, reimbursements, and travel expenses; liabilities; agreements or arrangements; outside positions; and compensation in excess of US\$5,000 paid by one source.

2.3 Examples of reportable property interests or assets include stocks, bonds, other securities, pension interests, tax shelters³, interests in trusts, personal bank accounts, real estate, commercial crops, livestock, accounts or other funds receivable, and collectible items for resale or investment.

¹ 5 C. F. R. part 2634.

² The form is provided in "Declaration of Interests by Senior Civil Servants in some Overseas Countries," Research and Library Services Division, Legislative Council Secretariat, March 2000, Appendix III.

³ A tax shelter usually means any activity which provides a taxpayer with the opportunity to shelter otherwise taxable income from liability to tax. In certain cases, charitable income is a tax shelter. Investment in activities that are considered socially desirable (like forestry or anti-pollution devices) is also sometimes given the status of a tax shelter.

2.4 For real estate, the requirement is to describe its nature and location. There is no requirement to report the specific address or the acreage. If the real estate is held in connection with a business operation, the business name, type and location must be indicated.

2.5 Any person who files a public financial disclosure form (a filer) must report the category of value of the asset at the close of the reporting period. Real estate may be valued by using a tax assessment, recent appraisal, purchase price, or a good fair estimate.

2.6 A filer must disclose assets in which he or she has an ownership interest, whether the assets are held separately or jointly with others. A filer must ordinarily disclose all properties held under a trust arrangement and its income, plus any transactions of the trust's assets.⁴ There is a reduced disclosure for blind or excepted trusts⁵.

2.7 Additionally, a filer is required to report information concerning his or her spouses and dependent children⁶ in the following categories: assets and income; transactions; gifts, reimbursements and travel expenses; and liabilities.

2.8 Before certifying that a nominee for a Cabinet Secretary position is in compliance with the relevant legal requirements, the Office of Government Ethics (OGE) often requires the nominee to sign an ethics agreement that commits the official to take remedial measures to resolve the conflict. These measures include recusal agreements, waivers, qualified trusts and divestitures.⁷

⁴ US Office of Government Ethics, *Public Financial Disclosure: A Reviewer's Reference*, 1996, pp. 7-30.

⁵ An excepted trust has both of the following characteristics: 1) the filer, the filer's spouse or dependent children did not create the trust, and 2) the filer, the filer's spouse or dependent children have no specific knowledge of the trust's holdings or source of income through a report or disclosure, whether intended or inadvertent.

⁶ For a filer, a dependent child means his or her son, daughter, stepson, or stepdaughter if such person is either: (1) unmarried, under age 21, and living in his or her household, or (2) considered dependent by tax code standards (which generally require that a dependent child receives more than half of his or her financial support from the filer).

⁷ For more detailed information, see "Process of Appointment of Senior Members of Government in Selected Countries," Research and Library Services Division, Legislative Council Secretariat, March 2002, pp. 31-2.

The United Kingdom

2.9 On appointment to each new office, a Minister is required by the *Ministerial Code*⁸ to provide his or her Permanent Secretary with a full list in writing of all interests which might give rise to a conflict. The list covers not only the Minister's personal interests, but also "*those of a spouse or partner, of children who are minors, of a trust of which the Minister, or a spouse, or partner is a trustee or beneficiary, or of closely associated persons*".⁹ On receipt of the written list, the Permanent Secretary will arrange a meeting with the Minister to discuss it and to consider what advice is necessary and what further information is needed.

2.10 The interests to be declared cover financial instruments and partnerships, financial interests such as unincorporated businesses and real estate, as well as relevant non-financial private interests such as links with outside organizations and previous relevant employment. Ministers must resign any directorships they hold when they take up office. This requirement applies whether the directorship is in a public or private company and whether it carries remuneration or is honorary.

2.11 The personal information which Ministers disclose is treated in complete confidence and may not be disclosed without their permission. According to paragraph 118 of the *Ministerial Code*, "[I]f an allegation is made that a particular Minister has a conflict of interest it must be for that Minister to explain their position and justify what has been done. In doing so, they may wish to make public the list of their private interests and the steps taken to avoid an actual or perceived conflict."

2.12 Both the House of Commons and the House of Lords maintain a Register of Members' Interests. Ministers who are members of either House have to file their returns.

2.13 In order to avoid conflicts of interests, Ministers are guided by the general principle that they should either dispose of any financial interest giving rise to the actual or potential conflict, or take alternative steps to prevent it. These steps include:

- (a) placing all investments into a blind trust;
- (b) accepting an obligation to refrain from dealing in the relevant shareholdings; and
- (c) setting up a process to prohibit access to certain papers and ensure that a relevant Minister is not involved in certain decisions and discussions.

⁸ The *Ministerial Code: a Code Conduct and Guidance on Procedures for Ministers*, available at <http://www.cabinet-office.gov.uk/central/2001/mcode/contents.htm>.

⁹ Paragraph 115 of the *Ministerial Code*. The term 'closely associated persons' is not defined in the *Ministerial Code*. According to information provided by the UK Cabinet Office, they expect a Minister to make a declaration if the Minister's child is a trustee or beneficiary and there is a potential conflict of interests.

3. Procedures to Avoid Conflicts of Interests

The United States

3.1 In the US, there is a criminal conflict of interests law, *18 USC 208*, which prohibits a public officer from working on government matters that will have an effect on his or her personal financial interests.

3.2 In addition, senior officials such as Cabinet Secretaries are subject to restrictions on outside earned income. Under Section 102 of the *Executive Order 12674*, a Presidential appointee to a full-time non-career position is prohibited from receiving any earned income for outside employment or for any other activity during that Presidential appointment. Cabinet Secretaries fall into this category of employee.

3.3 OGE oversees the administration of the public and confidential financial disclosure systems for the executive branch. It administers the blind trust programmes. It also administers the certificate of divestiture programmes in the executive branch. OGE, under the *1989 Ethics Reform Act*, is empowered to issue certificates permitting federal officials to defer paying capital gains taxes on assets they must sell to comply with ethics programme requirements. The certificate of divestiture must be obtained from OGE.

3.4 Generally speaking, a Cabinet Secretary cannot participate personally and substantially in matters in which he or she has a financial interest. According to information provided by OGE, if a Cabinet Secretary does not have advance notice that issues come up at a meeting which would create a conflict of interests, simply revealing the interest to the other attendees at the meeting and then not speaking during the meeting may not be sufficient to eliminate the appearance of participation in the meeting. The safest course of action is for him or her to leave.

The United Kingdom

3.5 In the UK, major principles of ministerial conduct are regulated through the *Ministerial Code*. Section 9 of the *Ministerial Code* specifically deals with Ministers' private interests, and contains rules to ensure that no conflict arises between Minister's public duties and their private financial interests.

3.6 In the UK, there is no specific office dealing with the investigation of allegations of ministerial misconduct. Ministers are personally responsible for deciding how to act and conduct themselves in the light of the *Ministerial Code* and for justifying their actions and conduct in Parliament. Ministers only remain in office for so long as they retain the confidence of the Prime Minister. The Prime Minister is the ultimate judge of the standards of behaviour expected of a Minister and the appropriate consequences of a breach of those standards.

3.7 Where it is proper for a Minister to retain a private interest, he or she should declare that interest to Ministerial colleagues if they have to discuss public business which in any ways affects the interest. The Minister should also remain entirely detached from the consideration of that business. Similar steps would be necessary if a matter under consideration in a department relates in some way to a Minister's previous or existing private interests such that there is or may be thought to be a conflict of interests.¹⁰

4. Blind Trust

4.1 In Hong Kong, section 5.7(d) of the *Code for Principal Officials Under The Accountability System (Code)* makes clear that a blind trust is an acceptable way for Principal Officials to avoid conflicts of interests. However, there is no definition of the term "blind trust" in the *Code*, nor in relevant local legislation such as the *Trustee Ordinance*.

4.2 In both the US and the UK, setting up a blind trust is a legitimate way for senior members of government to avoid potential conflicts of interests. A blind trust is a trust in which the beneficiaries do not have knowledge of the trust's specific assets, and a fiduciary third party has complete management discretion. Its purpose is to avoid allegations that senior members of government abuse their inside information for their own ends while in office.

The United States

4.3 In the US, there is no requirement that a Cabinet Secretary must utilize a blind trust to resolve potential conflicts of interests. However, there are detailed legal procedures that need to be followed if a Cabinet Secretary chooses to set up a blind trust. Relevant legal provisions are stipulated in the *Ethics in Government Act 1978* outlined below. The blind trust so constructed is known as a qualified blind trust and OGE is responsible for administering the blind trust arrangements.

Creation of a Blind Trust

4.4 A qualified blind trust must conform to prescribed standards, with a model blind trust agreement being issued by OGE. The trust document will have to be approved by OGE. The trust must also have an approved independent trustee, and be certified by OGE before it is executed.

¹⁰ Paragraph 117, *the Ministerial Code*.

Appointment of Independent Trustee in a Blind Trust

4.5 The trustee appointed must be independent from any interested party¹¹. The independence requirements are extended to those administering the trust and managing the trust assets.¹²

4.6 The eligibility of the trustee is limited to a financial institution, not more than 10 percent of which is owned or controlled by a single individual.

4.7 The trustee needs to be approved by OGE. Any client relationship between the proposed trustee and any interested party should be disclosed, and it may be subject to discontinuance as a condition of approval.

Management of a Blind Trust

4.8 The trustee will be conferred the sole responsibility of administering the trust and managing trust assets without the participation or knowledge of any interested party, including the disposal of the original assets¹³ placed in the trust.

4.9 On a regular basis, the trustee is required to provide reports¹⁴ to the Cabinet Secretary without identifying specifically any asset or holding in the trust.

4.10 The trustee must file an annual fiduciary tax return for the trust, the records of which shall be maintained and made available for inspection by OGE, together with the trust's books of account.

Assets Held in the Blind Trust

4.11 When a blind trust is first set up, it consists of initial assets transferred by the Cabinet Secretary. To avoid conflicts of interests, the blind trust should not contain any assets that are prohibited by the Cabinet Secretary's job nature. Additionally, the trustee should not acquire any holding from any interested party without the prior written approval of OGE.

¹¹ Interested party means the Cabinet Secretary, his spouse, any minor or dependent child, and their representatives in any case in which the Cabinet Secretary, his spouse, or child has a beneficial interest in the principal or income of the blind trust.

¹² For details, please refer to 5 C.F.R. Part 2634. Subpart D.

¹³ These assets have no restriction for sale except for those requiring prior approval of OGE to dispose.

¹⁴ The reports will specify aggregate value of the assets, net income or loss of the trust, etc.

Communication between Trustee and Interested Party

4.12 To maintain "blindness", there should be no direct or indirect communication between the trustee and any interested party unless it is in writing with prior written approval of OGE, and only if it relates to specific issues.¹⁵

4.13 Unless permitted by laws and regulations, the trustee should not disclose publicly any information which might identify trust assets, and should not solicit advice from any interested party with respect to the trust. In addition, he or she should not consult or notify any interested party when exercising his or her authority to manage the assets.

4.14 Interested parties should not receive any information regarding trust holdings, sources of trust income, and the trust unless permitted by laws and regulations.

Termination of a Blind Trust

4.15 There are several occasions where a qualified blind trust will come to an end.¹⁶ The blind trust will terminate following termination of the Cabinet Secretary's official position. The trustee will make full and proper accounting and turn over to the Cabinet Secretary all assets held by the trust.

Blind Trust in Transition

4.16 For the purpose of the *Ethics in Government Act 1978*, a trust is considered to be 'blind' only with regard to those trust assets that the interested parties have no knowledge. Assets that they have knowledge, such as the initial assets placed in the trust, may represent potential conflicts of interests hence are still regarded as "financial interests¹⁷" of the Cabinet Secretary.

4.17 Until these "financial interests" are disposed of or their value is reduced to US\$1,000 or below, the Cabinet Secretary may be prohibited to work on certain assignments unless special arrangements such as exemptions are made.

¹⁵ Specified issues relate to request for a distribution, general financial interest and needs of the interested party, instruction to the trustee to sell initial assets due to a conflict of interests, or notification to the trustee that certain assets are prohibited from being held in the trust.

¹⁶ Other occasions include death of the employee, for example.

¹⁷ See 5 C.F.R. Part 2634.401 and 18 USC Sec. 208.

Public Access to Information of a Blind Trust

4.18 Trust documents at the time of its establishment are available for public inspection, including the qualified blind trust agreement and the list of initial assets.

4.19 When a qualified blind trust is established, certain information, including the identity of the trust, date of creation and category of total cash value, is required to be disclosed to the public via filing the public financial disclosure report.

The United Kingdom

4.20 In the UK, the *Ministerial Code* makes clear that a blind trust is an acceptable way of avoiding potential conflicts of interests.¹⁸ Unlike the situation in the US, there is no specific legislation on the regulation of the setting up and operation of a ministerial blind trust in the UK.¹⁹

4.21 A Minister involving in a serious conflict of interests will normally be advised to dispose of the relevant financial interests or the ministerial duties will be reallocated to another Minister within the same department. A blind trust could be an option when the Minister does not wish to dispose of a particular interest.

4.22 Paragraph 127 of the *Ministerial Code* lays down some basic requirements of a ministerial blind trust, in that a blind trust is "*one in which the Minister is not informed of changes in investments or of the state of the portfolio, but is still fully entitled to both the capital and income generated.*"

4.23 According to Paragraph 127 of the *Ministerial Code*, a blind trust "*is only blind in the case of a widely-spread portfolio of interests, managed by external advisers. Once a blind trust has been established the Minister should not be involved or advised of decisions on acquisition or disposal relating to the portfolio.*"

4.24 The arrangements (including blind trust arrangements) that Ministers enter into regarding the handling of their private financial interests are confidential. Nevertheless, Ministers may need to make public the list of their financial interests if a serious allegation has been made.²⁰ Paragraph 127 of the *Ministerial Code* makes it clear that Part VI of the *Companies Act 1985* allows companies to require information as to the true owners of its shares, which could result in a Minister's interests becoming public knowledge despite the existence of a trust.

¹⁸ Paragraph 127 of the *Ministerial Code*.

¹⁹ Information provided by the UK Cabinet Office.

²⁰ Paragraph 118 of the *Ministerial Code*.

4.25 It is the responsibility of Ministers individually to order their own private lives in such a way as to avoid criticism, and the final decision about what action to take to achieve this objective is theirs. As mentioned in paragraph 2.9, there is a meeting between a Minister and his or her Permanent Secretary to consider what advice is necessary for the Minister's declaration. The Permanent Secretary's role is to ensure that advice is available when it is needed, by drawing on precedent or by securing professional advice from insiders or outside the government through the help of the Cabinet Office as necessary. Meanwhile, ministerial blind trusts do not need to be cleared by the Cabinet Office although the Office is normally consulted about the processes to be followed. There is no model blind trust agreement in the UK.²¹

5. British Virgin Islands Companies

5.1 British Virgin Islands (BVI) is a popular place of incorporation with more than 53 000 International Business Companies²² (BVI Companies) established per year recently.²³ The major advantages attached to BVI Companies are exemption from all BVI taxes and stamp duty, relatively simple company registration and administration requirements as well as confidentiality to the identity of shareholders and directors.

5.2 In the UK, there is no restriction on Ministers using BVI Companies to hold assets. However, according to the UK Cabinet Office, it is likely that any Minister using BVI Companies to hold assets would be reminded by their departmental Permanent Secretary of the potential allegations of criticism on the grounds of tax avoidance. If the Minister is, for example, a Treasury Minister, he or she would be advised to surrender such assets so as to avoid conflicts of interests. In the US, there is no absolute prohibition against an official to use a foreign company to hold assets. However, if a Cabinet Secretary uses a foreign company to hold assets, he or she is required to report the ownership on the Public Financial Disclosure Report (SF 278).

Operation of a BVI Company

Setting up a BVI Company

5.3 The requirements for setting up a BVI Company are relatively few. A BVI Company requires only one shareholder and one director, both of whom can be the investor himself. A registered office in BVI must be provided and a local registered agent must be appointed for submission of application.

²¹ Information provided by the UK Cabinet Office.

²² These companies must be formed under BVI's *International Business Companies Act 1984*.

²³ Web site of the British Virgin Islands Financial Services at <http://www.bvi.org/financial/company.shtml>

Disclosure of Information

5.4 There is no legal requirement for a BVI Company to disclose to local authorities any organizational or accountancy information except the Memorandum and Articles of Association.²⁴ Inspection of the share register is available only by order of the BVI Court.²⁵

BVI Companies in the Hong Kong Context

Public Access to Information

5.5 When a BVI Company establishes a place of business²⁶ in Hong Kong, it is required to register with the Companies Registry²⁷ and the Business Registration Office in Hong Kong.²⁸ Unlike companies incorporated in Hong Kong, a BVI Company can conceal identities of its shareholders as this information is not available to the public and only the BVI Court can order inspection of the share register.

Tax Implications

5.6 When a BVI Company engages in trading activities in Hong Kong and the profits are sourced in Hong Kong, it will be subject to Hong Kong taxation at the same rate as companies incorporated in Hong Kong. If all of the BVI Company's trading activities are sourced outside of Hong Kong, it will not be subject to Hong Kong taxation. When in doubt, it is up to the Inland Revenue Department to determine the source of profits and to demand payment of taxes.

²⁴ In this document, only the registered agent and registered office in BVI are disclosed.

²⁵ Registered shareholders also have the right to access shareholders' information.

²⁶ For definition of "place of business", please refer to section 341 of the *Companies Ordinance*.

²⁷ Registered information includes authorized representatives in Hong Kong, place of business in Hong Kong, list of directors, memorandum and articles of association, etc.

²⁸ For details, please refer to *Business Registration Ordinance*.

6. A Comparison of Various Attributes of Selected Issues

	US	UK
<i>1. Declaration of Interests</i>		
Regulatory framework	by law	by the <i>Ministerial Code</i>
Interests/Investments to be declared	1) assets and income; 2) transactions; 3) gifts; 4) reimbursements, and travel expenses; 5) liabilities; 6) agreements or arrangements; 7) outside positions; and 8) compensation in excess of \$5,000 paid by one source.	1) financial instruments and partnerships; 2) financial interests such as unincorporated businesses and real estate; and 3) relevant non-financial private interests such as links with outside organizations and previous relevant employment.
Family interests/investments to be declared	Spouses and dependent children's financial interests on: 1) assets and income; 2) transactions; 3) gifts; 4) reimbursements and travel expenses; and 5) liabilities.	Included interests of a spouse or partner, of children who are minors, of a trust of which a Minister, or a spouse, or partner is a trustee or beneficiary, or closely associated persons.
<i>2. Procedures to Avoid Conflicts of Interests</i>		
Regulatory framework	by law and the Executive Order	by the <i>Ministerial Code</i>
Conflicts of interests during meetings	<p>A Cabinet Secretary cannot participate personally and substantially in matters in which he or she has a financial interest.</p> <p>If a Cabinet Secretary does not have advance notice that issues come up at a meeting which would create a conflict of interests, simply revealing the interest to the other attendees at the meeting and then not speaking during the meeting may not be sufficient to eliminate the appearance of participation in the meeting.</p> <p>The safest course of action is for him or her to leave the meeting.</p>	<p>A Minister should declare related interests to Ministerial colleagues if they have to discuss public business which in any ways affects the interests.</p> <p>The Minister should also remain entirely detached from the consideration of that business.</p> <p>Similar steps would be necessary if a matter under consideration in a department relates in some way to a Minister's previous or existing private interests such that there is or may be thought to be a conflict of interests.</p>

	US	UK
3. Blind Trust		
Regulatory framework	by law	by the <i>Ministerial Code</i>
Specific arrangement	<p>There are detailed legal procedures that need to be followed if a Cabinet Secretary chooses to set up a blind trust.</p> <p>There is a model blind trust agreement, which is issued and administered by the Office of Government Ethics.</p>	<p>Ministerial blind trusts do not need to be cleared by the Cabinet Office although the Office is normally consulted about the processes to be followed.</p> <p>There is no model blind trust agreement.</p>
4. British Virgin Islands Companies		
Regulatory framework	<p>No absolute prohibition against an official to use a foreign company to hold assets.</p> <p>If a Cabinet Secretary uses a foreign company to hold assets, he or she is required to report the ownership on the Public Financial Disclosure Report .</p>	<p>No restriction on Ministers using BVI Companies to hold assets.</p> <p>It is likely that any Minister using BVI Companies to hold assets would be reminded by their departmental Permanent Secretary of the potential allegations of criticism on the grounds of tax avoidance.</p> <p>If the Minister is, for example, a Treasury Minister, he or she would be advised to surrender such assets so as to avoid conflicts of interests.</p>

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