

CONFLICT OF INTEREST – HOLDING COMPANY

Case No. 02-10

Facts:

Engineer A, a licensed engineer, is the president and a minority shareholder of an engineering firm, ABC Engineering. ABC Engineering is a majority-owned subsidiary of a holding company. The same holding company also owns a construction company, XYZ Construction. Engineer A is not a shareholder in either the holding company or the construction company. The holding company provides the internal accounting and strategic planning services, but offers no professional or other external services to clients or the public. ABC Engineering and XYZ Construction often do design/build work together.

ABC Engineering also does design/bid/build work, and on occasion, XYZ Construction will choose to pursue construction work on these same projects. In fact, ABC Engineering and XYZ Construction often jointly decide whether to pursue design only, construction only, or both types of work. If the companies pursue both design and construction independently, Engineer A discloses the potential conflict of interest to the client (and secures the client's signature on a disclosure form) and does not take part in the contractor selection or site inspection phase of the work. Engineer A was recently offered shares in the holding company that would compensate Engineer A for XYZ Construction's success.

Questions:

1. Is it ethical for Engineer A's company to pursue design work either jointly with XYZ Construction or independently through ABC Engineering under the facts presented?
2. Is it ethical for Engineer A to accept shares in the holding company that would compensate Engineer A for the XYZ Construction's success?

References:

- Section II.4. - Code of Ethics: Engineers shall act for each employer or client as faithful agents or trustees.
- Section II.4.a. - Code of Ethics: Engineers shall disclose all known or potential conflicts of interest that could influence or appear to influence their judgment or the quality of their services.
- Section II.4.c. - Code of Ethics: Engineers shall not solicit or accept financial or other valuable consideration, directly or indirectly, from outside agents in connection with the work for which they are responsible.
- Section III.5. - Code of Ethics: Engineers shall not be influenced in their professional duties by conflicting interests.
- Section III.5.b. - Code of Ethics: Engineers shall not accept commissions or allowances, directly or indirectly, from contractors or other parties dealing with clients or employers of the Engineer in connection with work for which the Engineer is responsible.

Discussion:

1 Engineers and engineering firms are increasingly engaging in new modes for offering
2 professional services. With the growth of design/build, construction management, limited
3 liability companies, joint ventures, and other project delivery and practice methods, engineers
4 are finding the manner in which they offer their professional services rapidly changing from the
5 traditional sole proprietorship, partnership, and corporation modes. Sometimes these different
6 modes of professional practice raise ethical issues for engineers to consider.

7
8 The NSPE Board of Ethical Review (Board) has considered differing practice modes in the past
9 and the impact such modes would have on ethical issues. For example, in BER Case 86-1, the
10 Board considered two similar fact situations involving an innovative practice mode. Situation 1
11 involved Engineer A who had the opportunity to join a business consortium consisting of his
12 engineering firm, an architectural firm, a construction firm, and a financial firm. The general
13 purpose of the consortium was to improve general marketing and business development. To
14 defray consortium expenses for promotion, publicity, overhead, etc., each firm was required to
15 pay to the consortium an entrance fee plus a percentage of income derived from business
16 successfully generated from referrals by other consortium members. In Situation 2, Engineer B
17 had the opportunity to join a business consortium consisting of his engineering firm, an
18 architectural firm, a construction firm, and a financial firm. The general purpose of the
19 consortium was to improve general marketing and business development. To defray consortium
20 expenses for promotion, publicity, overhead, etc, each firm was required to pay, to the
21 consortium, an entrance fee. In addition, Engineer B was required to pay a referral fee directly
22 to the consortium firm member which “found” the new business client for Engineer B. If
23 Engineer B “found” a new business client for a member of the consortium, Engineer B would
24 receive a finder’s fee. In reviewing the facts, the Board ruled that Engineer A’s participation in
25 the consortium would not be prohibited by the NSPE Code of Ethics while Engineer B’s
26 participation in the consortium would be unethical.

27
28 Turning to the facts in the present case regarding the first issue, as long there is full disclosure to
29 all clients of Engineer A’s relationship to the contractor through the holding company, it is the
30 Board’s view that any potential conflict of interest is being properly addressed by Engineer A.
31 The fact that Engineer A does not participate in contractor selection or site inspection also helps
32 Engineer A avoid a conflict of interest or appearance of impropriety issues. In addition,
33 engineers must also be mindful whether the professional services involve a public client, and that
34 there may be other public conflict of interest laws, regulations, or requirements.

35
36 Regarding the second issue, that of Engineer A being offered shares in the holding company as
37 compensation for XYZ Construction’s success, here an actual conflict of interest would exist
38 when Engineer A and XYZ Construction both accept work on the same project independently.
39 The basis for the conflict is that by virtue of the shares in the holding company, Engineer A’s
40 welfare would be inextricably bound up in XYZ Construction’s welfare. As such, Engineer A
41 would be in the position of being ethically obligated to act as a faithful agent and trustee while
42 representing an Owner’s interests, but at the same time being impacted by the success (or failure)

1 of XYZ Construction who also would be working for the same Owner. Under these
2 circumstances, the conflict of interest could not be absolved by disclosure. Rather, Engineer A
3 must either forego the shares, or not accept work on the same projects as XYZ Construction.
4 Only in this manner can the ethical obligation to act as faithful agent and trustee for the client be
5 met.

6 **Conclusions:**

- 9 1. It would be ethical for Engineer A's company to pursue design work either jointly with
10 XYZ Construction or independently through ABC Engineering under the facts presented.
- 11
12 2. It would be unethical for Engineer A to accept shares in the holding company that would
13 compensate Engineer A for XYZ Construction's success.

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23 NSPE members, other engineers, public officials and members of the public. The BER reviews each case in the context of the NSPE Code and
24 earlier BER opinions. The facts contained in each case do not necessarily represent all of the pertinent facts submitted to or reviewed by the
25 BER.*

26
27 *Each opinion is intended as guidance to individual practicing engineers, students and the public. In regard to the question of application of the
28 NSPE Code to engineering organizations (e.g., corporations, partnerships, sole-proprietorships, government agencies, university engineering
29 departments, etc.), the specific business form or type should not negate nor detract from the conformance of individuals to the NSPE Code. The
30 NSPE Code deals with professional services—which must be performed by real persons. Real persons in turn establish and implement policies
31 within business structures.*

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