

June 2000

University of Pennsylvania Conflict of Interest Policy

The University of Pennsylvania has always valued both excellence and integrity in serving the purposes to which the University is dedicated: education, research, and service. In order to promote these values, the University has long aspired to ensure that both actual and perceived conflicts of interest are avoided. On June 19, 1981, the Trustees adopted a Resolution on Conflict of Interest Policy establishing guidelines for dealing with conflicts of interest on the part of the faculty, trustees, associate trustees, officers, and other employees of the University. In June 1986, the Trustees adopted a Resolution amending and restating the Conflict of Interest Policy to clarify that the June 19, 1981 policy was in conformity with the Commonwealth of Pennsylvania Corporation Not-for-profit Code. The Policy was enhanced in 1995 by the Protocol on Trustee Norms, which both stated the Trustees' intention that a higher standard apply and instituted the current system of annual reporting.

Legislation enacted in June 1996 makes it appropriate and timely to review this policy again. The legislation introduced the concept of "intermediate sanctions," *i.e.*, sanctions short of revocation of tax exemption, when charities engage in "excess benefit transactions." Such transactions can arise in many different contexts, including executive compensation in excess of market benchmarks, licensing of technology at a rate less than the market would pay, and entering into a contract with a service provider on terms less favorable than arm's length. Under the new legislation, intermediate sanctions may be imposed when an excess benefit transaction involves a "disqualified person," defined as someone in a position to exercise substantial influence over the charity. A transaction will withstand scrutiny if it can be determined that compensation rates and contract terms were set at levels equal to those that would prevail in arm's length transactions. Such terms will be presumed to have met this market test if they have been approved by a committee of disinterested trustees.

In light of these developments, the Trustees propose to adopt a more comprehensive conflict of interest policy for Trustees, Officers, and members of the Trustees' Investment Board; modify the University's executive compensation review process; and charge a Compensation Committee with responsibility for administration of the executive compensation review process and conflict of interest policy.

Changes from the June 1986 Conflict of Interest Policy will ensure that the University is in compliance with the new intermediate sanctions regulations. To create a more protective policy for the University, the scope of the policy has been broadened to include members of the Trustees' Investment Board, as well as Emeritus and former Trustees for a period of five years subsequent to their election to emeritus status or departure from the Board, respectively. The policy requires that "Covered Persons" immediately notify the University of a proposed transaction between the University and

him or herself or an affiliate. The policy also provides for mandatory physical recusal by Covered Persons from participation in any discussions of “Covered Transactions” with University officials and members of the University-wide community and at meetings of the Trustees or their committees, except to respond to general requests for information about a transaction.

The policy includes the IRS standard for approval of a transaction involving a potential conflict, which is to determine that the transaction results in a payment to the Covered Person that is no more than “fair market value.” In addition, the responsible parties would have to determine that the Covered Transaction did not present an unacceptable appearance of conflict and that it was fair, reasonable, and in the best interests of the University.

RESOLVED, that the June 1986 Resolution on Conflict of Interest Policy as enhanced by the 1995 Protocol on Trustee Norms be amended and restated to read, in its entirety, as follows:

This policy on conflict of interest is divided into three parts, the first dealing with faculty, the second dealing with trustees, officers, and Investment Board members, and the third dealing with other employees of the University.

I. Faculty

Certain categories of potential conflict of interest as to faculty are addressed in existing University policies, including the Conflict of Interest Policy for Faculty Members adopted by the Faculty Senate on November 17, 1982, approved by the Provost on March 1, 1983 and printed in the 1983 Handbook for Faculty and Academic Administrators. University Council also recommended a Policy on Outside Financial Interests on September 24, 1969, which is as follows:

A member of the faculty may have a significant investment or interest, or hold an official position, in an outside firm or organization but has not undertaken to perform continuing work or services for it. Such an economic or official relationship is of concern if 1) the firm or organization is engaged in activities which parallel activities in which the University is currently or prospectively engaged and in which the faculty member plays (or might appropriately play) a role in his or her academic capacity; or 2) the firm or organization has a present or prospective relationship with the University, e.g., as a supplier of goods or services or as a party to a research contract, and the conduct of that relationship may involve the faculty member in his academic capacity. In either of these situations, the faculty member shall be required to report the facts and circumstances to the department chairman and the academic dean or director so that appropriate steps may be taken to avoid a conflict of interest.

These policies are recognized to govern those areas of potential conflict of particular concern to faculty.

A number of other existing University policies pertaining to conflicts of interest apply to faculty members unless they are intended by their terms to apply only to other groups or employees. These policies include, but are not limited to, policies on patent and copyright, purchasing, nepotism, and sexual harassment.

II. Trustees, Officers, and Investment Board Members

The University of Pennsylvania is an institution of higher education that prizes truth, excellence, and integrity. The Trustees, Officers, and members of the Investment Board are chosen to serve the purposes to which the University is dedicated: education, research, and service. These persons have a duty to conduct the affairs of the University in a manner consistent with such purposes and not to advance their personal interests. This conflict of interest policy is intended to permit the University and its Trustees, Officers, and Investment Board members to identify, evaluate, and address any real, potential, or apparent conflicts of interest that might, in fact or in appearance, call into question such persons' duty of undivided loyalty to the University.

A. Covered Persons

This policy applies to the following persons: (1) voting members of the Board of Trustees (including Charter Trustees, Term Trustees, Alumni Trustees, and Commonwealth Trustees); (2) Trustees Emeriti who have served in that capacity for five years or less; (3) other former voting Trustees for a period of five years from the end of their term as such; (4) Officers as defined in the Statutes; and (5) members of the Investment Board. Each Covered Person (except former Board members who are not Trustees Emeriti) shall be required to acknowledge, not less than annually, that he or she has read and is in compliance with this policy adopted by the Board of Trustees on June 16, 2000.

B. Covered Transactions

This policy applies to transactions between the University and a Covered Person, or between the University and another party with which a Covered Person has a significant relationship. A Covered Person is considered to have a significant relationship with another party if:

1. the other party is a family member, including a spouse, parent, sibling, child, stepchild, grandparent, grandchild, in-law, or domestic partner;
2. the other party is an entity in which the Covered Person has a material financial interest. The determination of what constitutes a

- material financial interest includes entities in which the Covered Person and all individuals or entities having significant relationships with the Covered Person own, in the aggregate, more than (a) 1 percent of any class of the outstanding securities of a firm or corporation; (b) 10 percent interest in a partnership or association; or (c) 5 percent of the total direct and beneficial assets or income of the person; or
3. the Covered Person is an officer, director, trustee, or employee of the other party.

A Covered Transaction also includes any other transaction in which a Covered Person believes there may be an actual or perceived conflict of interest, including any transaction in which the interests of a Covered Person may be seen as competing with the interests of the University.

In order to assist the University in identifying proposed Covered Transactions, each Covered Person (except former Board members who are not Trustees Emeriti) annually shall complete a Conflict of Interest Questionnaire provided by the University and shall update such Questionnaire promptly as necessary to reflect changes during the course of the year. Former Board members who are not Trustees Emeriti are encouraged but not required to complete the Questionnaire during the five-year period following completion of their terms. Completed Questionnaires shall be returned to the Office of the Secretary and shall be subject to review by such office and the Office of the General Counsel, as well as by any outside legal counsel and/or auditors who may be appointed to advise the Compensation Committee of the Board of Trustees appointed to oversee this policy. Completed Questionnaires also shall be available for inspection by any Board Member.

C. Disclosure, Refrain from Influence, and Recusal

When a Covered Person becomes aware of a proposed Covered Transaction, he or she shall have a duty to take the following actions:

1. immediately disclose the existence and circumstances of such Covered Transaction to the Compensation Committee and to the Office of the General Counsel;
2. refrain from using his or her personal influence to encourage the University to enter into the Covered Transaction; and
3. physically recuse himself or herself from participation in any discussions regarding the Covered Transaction with officials of the

University, at meetings of the Board of Trustees or the Investment Board, at meetings of committees of either Board, and with other members of the University community, except to respond to requests for information about the Covered Transaction.

D. Standard for Approval of Covered Transactions

The University may enter into a Covered Transaction where it is determined by the parties responsible for approving such transaction on behalf of the University, acting without the participation or influence of the Covered Person, that such transaction is fair, reasonable, in the best interests of the University, and consistent with the University's status as a Pennsylvania nonprofit corporation and a Section 501(c)(3) organization. The University official seeking to enter into a Covered Transaction on behalf of the University shall make a record of such proposed transaction, including the basis for determining that it meets the above-described standard. Before entering into a Covered Transaction, such party shall notify the Compensation Committee, which shall review the adequacy of such determination and shall approve or disapprove the Covered Transaction on that basis.

E. Compensation Committee

This policy shall be administered by the Compensation Committee of the Board of Trustees. The Committee's responsibilities shall include the following:

1. reviewing reports from the Office of the Secretary and/or the Office of the General Counsel regarding the Conflict of Interest Questionnaires;
2. receiving disclosures of proposed Covered Transactions;
3. reviewing proposed Covered Transactions and any preexisting Covered Transactions to determine whether they meet the above-described standard;
4. maintaining minutes and such other documentation as may be necessary and appropriate to document its review of Covered Transactions;
5. adopting guidelines for its operations, including guidelines for the Committee's review of Covered Transactions and for delegation of authority to the Office of the General Counsel to review Covered Transactions that have an insubstantial value;

6. reviewing the operation of this policy and making recommendations to the Board of Trustees regarding changes to the policy; and
7. reporting regularly to the Board of Trustees regarding the work of the Committee.

F. Responsibilities of the Office of the General Counsel

The Office of the General Counsel shall provide advice and assistance to the Compensation Committee in carrying out its responsibilities under this policy. The General Counsel shall attend all meetings of the Compensation Committee, and shall assist in preparing the minutes of Committee meetings.

III. University Employees other than Faculty and Officers ("Employees")

Employees of the University shall avoid any conflict between their personal interests and the interests of the University; furthermore, they shall avoid any situation where it would be reasonable for an objective observer to believe that the person's judgment or loyalty might be adversely affected. For purposes of Paragraphs III (a) and (b) below, reference to the University is intended to include also reference to all entities controlled or owned in substantial part by the University.

(a) If an employee has any power or influence to approve or disapprove a transaction proposed to be entered into between the University and that person or between the University and any entity or individual having a significant relationship to that person, he or she has a potential conflict of interest and may not participate in the process leading to the approval or disapproval of the transaction unless the underlying facts giving rise to the potential conflict of interest are disclosed and approval for participation is obtained pursuant to the procedures described below in paragraph (e).

(b) An employee also has a potential conflict of interest if that person, or any entity or individual having a significant relationship to that person may benefit from information considered by the University to be confidential and learned in his or her capacity as an employee of the University.

(c) A significant relationship exists as to an entity if a person is director, trustee, officer, or employee of, a partner or member in, or has a material financial interest in, the entity in question.

(i) An entity is a corporation, partnership, unincorporated association, or any similar group.

(ii) Determination of a material financial interest is a matter of personal judgement but, at a minimum, would be required for an aggregate

interest for the person and for all entities or individuals having material relationships with the person of more than

- 1 percent of any class of the outstanding securities of a firm or corporation, or
- 10 percent interest in a partnership or association, or
- 5 percent of the total direct and beneficial assets or income of the person.

(d) A significant relationship exists as to an individual if that individual is in the immediate family of a person subject to this policy. The immediate family includes parents, siblings, spouse, and offspring.

(e) An employee who has a potential conflict of interest covered by this policy shall immediately disclose the potential conflict in writing to a superior who in turn should inform the Secretary. The employee may continue participation in the transaction only on terms approved by the Secretary.

(f) A number of other University policies pertaining to conflict of interest remain in effect and may, depending on their terms, apply to employees of the University. These policies include, but are not limited to, policies on extramural consulting by administrative staff, purchasing, sponsoring research, patent and copyright, nepotism, and sexual harassment.