



Inquiry report

Inquiry into the West Coast Development Trust

Office of the Auditor-General
Private Box 3928, Wellington 6140

Telephone: (04) 917 1500
Facsimile: (04) 917 1549

Email: reports@oag.govt.nz
www.oag.govt.nz

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This is the report of an inquiry we
carried out under sections 16 and 18
of the Public Audit Act 2001.

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Foreword

I began this inquiry after I was sent information containing a number of specific allegations about individual files and transactions at the West Coast Development Trust. After investigating the detail of those allegations, I have concluded that many of the concerns were unfounded and that others were based on minor administrative or procedural errors, or occasional errors of judgement.

Despite that conclusion, this is a sobering report. In the course of my inquiry, it rapidly became apparent that the main problem is that the Trust is dysfunctional at a governance level. The trustees do not work together effectively. There is an atmosphere of suspicion and distrust, which manifests in hostility and accusations.

The behaviour at the Trust during the past 18 months is not appropriate for a public entity, or for trustees. Much of it continues today.

I have therefore concluded that I am unable to provide Parliament with assurance that the Trust is able to deliver fully on its purpose of generating sustainable employment opportunities and economic benefits for the people of the West Coast region until this situation changes.

The trustees urgently need to find a way to work together so they can take effective collective responsibility for the governance of the Trust. If individual trustees cannot make that change, and remain unable to fulfil their responsibilities, then they should consider stepping down. There is no other mechanism in the Trust deed for achieving change. The solution therefore rests with the individuals sitting around the Trust's board table.



K B Brady
Controller and Auditor-General

30 July 2008

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Summary

The Auditor-General decided in October 2007 to conduct an inquiry into the operations of the West Coast Development Trust (the Trust), after receiving information on the workings of the Trust, including allegations of conflicts of interest. The inquiry considered:

- the management of conflicts of interest by the Trust;
- compliance with procedures and policies for providing funding to Trust applicants;
- use of Trust resources to benefit Trust applicants; and
- roles and responsibilities in the governance and management of Trust operations.

After completing our inquiry, we have one recommendation to make – that the group of trustees urgently find a way to work together so that they can take effective collective responsibility for the governance of the Trust.

All trustees need to focus on the legal and ethical responsibilities they owe, individually and collectively, to the Trust and to the community of the West Coast region. If trustees cannot make that change, and remain unable to fulfil their responsibilities, then they should consider stepping down. Unlike other public entities with elected boards, there is no other ready mechanism for resolving this level of dysfunction.

Until we see evidence that the group of trustees is able to take effective collective responsibility for the governance of the Trust, we are unable to provide assurance that the Trust is able to deliver fully on its purpose of generating sustainable employment opportunities and economic benefits for the people of the West Coast region.

The Trust, which uses the trading name Development West Coast, was established in April 2001 to administer \$92 million of a \$120 million funding package given by the Crown to assist the West Coast economy to adjust to the Government's policies to end logging of indigenous forest. The Trust is a charitable trust to benefit the community of the West Coast region. It was initially governed by 12 trustees (some elected and some appointed by local authorities and other organisations). The number of trustees reduced to six in 2007, and recently increased to seven.

As we noted in May 2006 in our performance audit report *Management of the West Coast Economic Development Funding Package*, the Trust began well. But it has encountered significant difficulties in recent times. Those difficulties have centred on personal and political conflicts mainly at a governance level, and have affected the operation of the Trust in a range of ways. Important relationships

have broken down, and behaviour has emerged that is less than satisfactory in a public entity.

The most important challenges facing the Trust now are questions of governance and management. Our inquiry looked at the overall role of the Trust, its external and internal relationships, its systems for disclosing information and the consequences of unauthorised disclosure, and the different views that have been held about the authority for decision-making. We conclude that, as a result of the cumulative effect of these various issues, the Trust is dysfunctional at a governance level and has been so for some time.

With respect to management of conflicts of interest by the then chairman, Mr Frank Dooley, and the then chief executive, Mr Mike Trousselot, we conclude that:

- the Trust generally has appropriate systems for managing conflicts of interest, and that there is good awareness of the systems and of the general principles;
- there was no evidence of any trustee (including Mr Dooley) taking part in decisions in which they had a conflict of interest – although, in keeping with the legal advice to the Trust, trustees did sometimes present information to a meeting on matters where they had acknowledged a conflict of interest;
- Mr Dooley had a good understanding of conflicts of interest, and in the documents we examined it was generally made clear when he was acting as a professional adviser to an applicant rather than as a trustee;
- there has been one example, in November 2005, when Mr Dooley did not manage a conflict of interest situation properly – although we acknowledge that the situation was complex and that he took advice on how to manage what he regarded as a difficult and urgent ethical issue; and
- it was reasonable for the Trust to appoint the chief executive, Mr Trousselot, as a director of companies in which it was investing, and consideration was given to the terms of engagement and how conflicts of interest should be managed. The arrangements would have been stronger if they had been more carefully and clearly documented and explained, and if staff reporting lines had been formally changed for all issues relating to those companies.

We encourage the Trust to further amend its systems to enable conflicts of interest to be identified before meetings, and the appropriate response to be agreed between the relevant trustee, the chairperson, and the chief executive. It is important that trustees take individual and collective responsibility for managing conflicts of interest in practice, to protect the integrity of the Trust's decision-making systems.

We also investigated a number of other issues raised with us but found no basis for the allegations.

In conclusion, the major challenge facing the Trust is that it is dysfunctional at a governance level. On the specific concerns put to us on the actions of Mr Trousselot, we found a small number of matters that could have been handled more effectively. On the specific concerns about the actions of Mr Dooley, we found only occasional instances of poor judgement. In both cases, however, these conclusions need to be set against seven years of effective administration of the Trust and against a deteriorating governance and operating environment in recent times.

Part 1

Introduction

- 1.1 The West Coast Development Trust (the Trust) is a public entity under the Public Audit Act 2001.¹ The Auditor-General is therefore its auditor, and is also able to carry out performance audits and inquiries into the activities of the Trust.
- 1.2 On 1 August 2007, the Auditor-General received a request for an inquiry into the Trust's operations, which was supported by a range of information about the Trust. On 25 September 2007, the *Greymouth Star* published an article stating that the information given to the Auditor-General had been leaked to the *Greymouth Star*. The newspaper article referred to material from Trust files, including an email and a letter from Mr Frank Dooley, the chairman of the Trust at the time.
- 1.3 Because of the public disclosure of the information and the associated public comment, Mr Dooley contacted the Trust's appointed auditor, and then us, asking that we inquire into the concerns that had been raised and were being reported in the media.
- 1.4 We assessed the material we had received, and the two requests, and decided that there were matters that warranted an inquiry. We released the terms of reference for the inquiry on 30 October 2007. The full terms of reference are attached as an appendix to this report.
- 1.5 We chose not to inquire into how confidential Trust information was provided to us, because it was disclosed to an appropriate authority. It is the general policy of the Auditor-General not to reveal the identity of people who contact us with concerns about public entities, because there is a public benefit in enabling people to raise concerns through this channel. Although information was also leaked to the media, we did not investigate those leaks because they appeared to be too closely linked to the disclosure to us. However, we do comment later in this report on the treatment of confidential Trust information (see paragraphs 2.36-2.39 and 3.22-3.32).

The inquiry process

- 1.6 In carrying out our inquiry, we visited the Trust and met with the six people who were trustees in late 2007 and with senior staff members of the Trust. We also met with the then chairperson, Mr Dooley, and two members of the advisory body.² We extended an invitation to individuals who were trustees before the October 2007 elections, and spoke with those former trustees who expressed an interest in talking with us.

1 The West Coast Development Trust trades as Development West Coast.

2 The advisory body is a group of experts who advise the trustees on applications for funding.

- 1.7 We reviewed relevant information and files from the Trust, including minutes of meetings and various files on applications for funding, as well as other information provided to us. We did not consider it necessary to meet with individuals or entities that had received financial assistance from the Trust.
- 1.8 We prepared a draft report and discussed it with the two most affected parties, Mr Dooley and the Trust's chief executive, Mr Mike Trousselot,³ to check whether our understanding of the facts was accurate and complete, and to meet natural justice requirements. After considering their comments, we gave them a second draft for further comment. We then gave a copy of parts of the draft report to the rest of the trustees and to the chair of the advisory body for comment. We discussed some sections again with Mr Dooley before we finalised and issued this report.
- 1.9 This process, and the length of time it has taken, has provoked some disquiet among interested parties. The process of preparing and consulting on draft documents is an important part of any inquiry, and confidentiality is essential. We have to check that our understanding of the facts is accurate and that our interpretation of events is reasonable. We also have to protect the rights of potentially affected parties to receive natural justice, which cannot be done if the process is not confidential. During the consultation process, additional information is often provided and initial views can change as the issues are explored in more depth. Therefore, the process can be an iterative one. The conclusions we reach at the end of our investigation and consultation are our own.

3 In April 2008, Mr Trousselot resigned as chief executive to take up another position.

Part 2

Background

Establishing the West Coast Development Trust

- 2.1 The Crown established the Trust in April 2001 to administer \$92 million of a \$120 million funding package, given by the Crown to assist the West Coast economy to adjust to the Government's policies to end logging of indigenous forest. The remaining \$28 million was divided equally between each of the four West Coast local authorities¹ to spend as they saw fit.
- 2.2 The Trust is a charitable trust to benefit the community of the present and future inhabitants of the West Coast region. The Trust fund can be used to:
 - promote sustainable employment opportunities in the West Coast region; and
 - generate sustainable economic benefits for the West Coast region; and
 - support projects (other than infrastructure that is normally the responsibility of local authorities or central government), if those projects promote sustainable employment or generate sustainable economic benefits.
- 2.3 The Trust was initially governed by 12 trustees, six of whom were directly elected, four of whom were appointed by the region's local authorities, one who was appointed by Te Rūnanga o Ngāi Tahu, and one appointed jointly by the presidents of the New Zealand Law Society and the New Zealand Institute of Chartered Accountants. The trustees' role is to direct and supervise the conduct of the Trust's business. The number of trustees was reduced to six in 2007, but has recently been increased to seven.
- 2.4 Unlike other public entities with elected boards (such as schools, local authorities, or district health boards), there is no "circuit breaker" mechanism in the Trust deed to enable the elected trustees to be replaced if there is a governance failure.
- 2.5 The trustees appoint an advisory body to act as expert advisers in distributing funds to business and community groups. Applications for more than \$100,000 cannot be approved without a recommendation to do so from the advisory body, and the advisory body can recommend approving the application only if it considers that the application meets the objects, or purpose, of the Trust. A chief executive and staff support the trustees and the advisory body.
- 2.6 Under the Public Audit Act 2001, the Auditor-General is the Trust's auditor, and appoints an auditor to conduct the Trust's annual financial audit on his behalf. The appointed auditor has issued clear audit opinions on the Trust's financial statements since it was established.
- 2.7 The Trust's own systems for measuring its performance, including its stakeholder satisfaction surveys, have also been positive.

1 West Coast Regional Council, Buller District Council, Grey District Council, and Westland District Council.

Our performance audit of the West Coast Development Trust

- 2.8 We carried out a performance audit in 2006 that considered how the Trust and the four local authorities were administering the funding they had received. Further information on the establishment and structure of the Trust is set out in the report of that performance audit, *Management of the West Coast Economic Development Funding Package*, which we published in May 2006.
- 2.9 Our performance audit looked at the governance arrangements for the Trust and tested that the distribution of Trust funds complied with the Trust deed. The performance audit's findings were generally positive about the Trust's governance arrangements, including:
- governance of the Trust's subsidiary companies;
 - management of conflicts of interest;
 - maintaining confidentiality; and
 - meeting the transparency and accountability requirements of the Trust deed.
- 2.10 We noted in that report that a number of people considered that 12 trustees was too many for effective governance, and were concerned that there were no skill requirements for trustees. We also reported some people's concerns that the Trust was not sufficiently transparent and that perceptions of a "veil of secrecy" could lead to suspicion. Our report emphasised that confidentiality was important for the application process, given the range of personal, financial, and commercially sensitive information involved, but we also encouraged the Trust to continue with its initiatives to more regularly involve the public through meetings and by improving reporting on its performance.
- 2.11 All decisions to provide funding must ultimately be consistent with the objects of the Trust. Our 2006 report commented on the significant debate about aspects of the interpretation of the objects of the Trust, and that this lack of agreement sometimes affected the Trust's operations and decision-making processes. We encouraged the Trust to resolve those debates, including by obtaining further legal advice and using a forthcoming review to clarify some issues.

The Treasury review

- 2.12 The Trust deed required the Trust's settlor² and the trustees to review the operations of the Trust after five years of operation. The Treasury, acting for the Minister of Finance, began this review in June 2006, working closely with the Trust. The review was completed in June 2007.

² This is the person who created the Trust – in this case, the Minister of Finance on behalf of the Government.

- 2.13 Issues considered during the review included the:
- number of trustees and the composition of the Trust;
 - role of trustees appointed by local authorities, and their relationship to their appointing body;
 - changing governance and management needs of the Trust as the organisation moved out of the establishment phase and matured, and the need for a tiered system of clear delegated decision-making authority for the Trust, its subcommittees, and the chief executive;
 - extent of the Trust's role in distributions to community groups, the assessment of those distributions against the objects of the Trust, and the role of the advisory body in those applications;
 - possibility of giving the Trust a power to borrow; and
 - interpretation of the "infrastructure clause" in the Trust deed's description of the objects of the Trust.
- 2.14 Both our performance audit and the Treasury review noted the general agreement among the trustees and stakeholders that the number and mix of trustees was proving a barrier to effective governance. The Treasury review documents noted that stakeholders cited a number of factors that were inhibiting effective governance, the main ones being the Trust's leadership style and the misalignment of local authority incentives with the objects of the Trust. The review noted that the Trust's relationships with its stakeholder local authorities were "at a low ebb", and that work would be required to improve them.
- 2.15 After the Treasury review, the Trust deed was amended to reduce the number of trustees from 12 to six. The Treasury review noted that six trustees would be able to make decisions efficiently and have a strong sense of direction, while still achieving a strong West Coast presence and a link to the local authorities. The change included reducing the number of local authority-appointed trustees from four trustees (appointed by each of the four local authorities in the West Coast) to one trustee appointed by the four local authorities. This change came into effect with the local authority elections in October 2007.
- 2.16 The Treasury review noted that the role of local authority-appointed trustees had been queried during the review. The review clarified that, once appointed, trustees had a fiduciary duty (see paragraph 2.22) under general law and the Trust deed to act in the best interests of the beneficiaries "as a whole" (that is, the West Coast region) rather than any one district. The review also noted that improving the trustees' governance dynamics and external relationships would largely come down to the abilities of trustees and their approach in these areas.

- 2.17 Other findings of the Treasury review included that:
- the Trust had succeeded in getting its operations established and supported by a strong set of policies and processes within a short time frame;
 - the Trust had managed its funds well under its investment strategy;
 - the Trust had been involved in community distributions to a greater extent than envisaged by the settlor, and would review its involvement (particularly in minor distributions with limited economic effect); and
 - as the Trust had grown in size, capability, and operations since it had been formed, the trustees needed more of a governance focus than they had in the establishment phase (that is, a focus on determining the direction and major policy settings of the Trust). The review noted that an intended shift to a more tiered application process, with greater delegation to the advisory body and chief executive, would support this approach.
- 2.18 A number of detailed changes were made to the Trust deed because of this review. It was also agreed that another review would take place in five years.

Emerging difficulties

- 2.19 Our 2006 performance audit described an organisation that had established itself well and was reasonably effective, albeit with areas where further work was needed. The Treasury review also noted much that was positive, but acknowledged some emerging difficulties. The review alluded to problems with the relationship with the local authorities, disagreements about the role and allegiances of trustees, and ongoing debate about the meaning and application of core provisions of the Trust deed.
- 2.20 Our discussions with people during our inquiry, our review of documentation, and our review of the various events and media commentary of the past 18 months confirms that those issues have now become major difficulties. We discuss particular issues in more detail in this report, but it is useful to note some points now as general background.
- 2.21 At least some of the difficulties arise from a question about the core nature of the Trust, and whether it should be regarded as similar to a local authority (given its composition of locally elected and local authority-appointed trustees) or to a commercial investment organisation. This issue links to questions about the appropriate levels of transparency and public accountability, systems for disclosing information, and decision-making roles and responsibilities within the organisation.

- 2.22 In our view, the Trust is a hybrid organisation:
- Three of the seven trustees³ are elected based on local authority boundaries, and another is appointed by the region's local authorities. There is clearly a democratic and therefore political element to the Trust, which is likely to colour its relationship with the community and other locally elected organisations. The Trust is partially representative of the people of the region, and must therefore be in some way responsible to the community that elects it. That element is implicitly recognised in the Trust deed, which includes a general requirement for the Trust to operate with transparency and accountability.
 - At the same time, the organisation is established as a trust. This means that trustees have very specific legal responsibilities under the Trust deed and general law to act in the best interests of the beneficiaries of the Trust. These responsibilities are often referred to as fiduciary duties and impose high standards of conduct, diligence, and probity on trustees.
 - The Trust is also set up to make commercial investment decisions. The nature of its activity means that, in many respects, it is operating similarly to a venture capital fund. It operates in a commercial environment that sometimes involves access to commercially sensitive and confidential material, and a significant measure of risk-taking.
- 2.23 These different aspects of the Trust create a complex working environment, and the lack of a shared view on the way in which those different aspects come together has clearly been behind many of the issues we identify in this report. It is not straightforward in practice to protect commercially sensitive information and meet public transparency and accountability obligations, or to balance the risk-taking required for venture capital investments with traditional trustee duties of prudence or the dictates of political accountability. But the Trust has to agree on a balance and to build that balance into its governance and management systems. It achieved that in the first years of its operations, but more recently has not been able to maintain the necessary level of agreement among trustees on these critical issues.

Relationships between the trustees

- 2.24 Relationships between the trustees have deteriorated significantly since we completed our performance audit of the Trust in mid-2006.
- 2.25 In late 2006, when the Trust and local authorities were involved with the Treasury review, the Westland District Council replaced its appointed trustee. The trustee

3 A seventh trustee was appointed in February 2008. See paragraph 2.35.

appointed by the West Coast Regional Council also resigned at this time. Mr John Clayton and Mr Tony Williams became the appointed trustees for the West Coast Regional Council and the Westland District Council respectively, and attended their first meeting on 6 November 2006.

- 2.26 Mr Clayton has challenged and questioned some Trust policies and processes since being appointed, including Mr Dooley's practices in managing information. Mr Clayton considered that the Trust could be more open with its policies and information. He has a local authority background, and thought the Trust should operate more along the lines of a local authority than a commercial organisation. He has questioned the Trust's confidentiality requirements and how they fit with the requirement in the Trust deed to operate transparently and accountably.⁴
- 2.27 We have reviewed the range of legal advice on the meaning of the requirement in the Trust deed to operate transparently and accountably. We agree with the conclusion in the Trust's advice that this is an overall reporting obligation on the Trust as a whole, not individual trustees, and that it is compatible with a confidentiality policy designed to protect commercial information.
- 2.28 Mr Williams sought to clarify his reporting responsibilities to his appointing local authority, the Westland District Council. In mid-2007, he sought his own legal advice on governance issues, including the interpretation of the clause in the Trust deed about transparency and its relationship to the Trust's requirement that trustees maintain confidentiality. Mr Clayton referred to that legal advice at a meeting of the West Coast Regional Council in June 2007. The legal advice was tabled at a meeting of the Westland District Council in August 2007, which at that stage agreed to pay part of the cost of the advice.
- 2.29 We would have expected an issue of this kind to be discussed first with fellow trustees and Trust staff. The fact that it was not was symptomatic of the relationship difficulties that were emerging among the trustees and between the Trust and the local authorities.
- 2.30 The Trust had sought its own legal advice on corporate governance principles about the same time. The matters of disagreement between the legal advisers were referred back to these advisers for consideration, and there has been extended correspondence between them.
- 2.31 Minutes of Trust meetings in the period from November 2006 to September 2007 record robust debates about governance issues at the meetings, and a deteriorating governance environment.

4 Minutes of Trust meeting, June 2007.

- 2.32 In September 2007, six of the then twelve trustees voted to replace Mr Dooley as chairman with Mr Williams. Six trustees supported Mr Dooley. With six for and six opposed, Mr Dooley remained as chairman.

Outcome of 2007 elections

- 2.33 Trustee elections were held on 13 October 2007. One new trustee was elected by Westland district – Mr Bruce Smith. Mr Dooley was re-elected by Buller district, and Mr Clayton was elected by Grey district. Mr Williams was appointed by a panel made up of representatives of the four local authorities. Mr Mark Lockington and Mr Barry Wilson continued in office representing their appointing bodies (the New Zealand Law Society and the New Zealand Institute of Chartered Accountants, and Te Rūnanga o Ngāi Tahu, respectively).
- 2.34 After the 2007 elections of trustees, the Trust was split into two factions, each of three trustees, and there was a dysfunctional relationship between the two factions. It was widely known on the West Coast that the trustees were unable to work together, and this affected the Trust's effectiveness and the working environment for Trust staff. The trustees could not agree on who should chair the Trust. Minutes of the Trust meetings show heated argument on a wide range of procedural and substantive issues.
- 2.35 The trustees asked the settlor to appoint a seventh trustee to resolve the deadlock on various matters, including the appointment of a chairperson of the Trust. The Trust deed was amended to provide for the appointment of an additional trustee, and the Minister of Finance announced the appointment of a seventh trustee, Mr Brian Roche, on 15 February 2008. Mr Dooley stood down as chairman and the trustees unanimously elected Mr Roche as chairman at their meeting on 14 March 2008.

Disclosure of Trust information

- 2.36 The minutes of Trust meetings show that, from early 2005, the Trust has had problems with confidential information being discussed with people outside the Trust, and in some cases being reported in the media. In some cases, information has just been leaked. In other cases, the issues have been more complex and have related to:
- the different views about the extent to which local authority-appointed trustees could report back to their appointing local authorities on Trust matters; and
 - a lack of clarity about the boundaries between different roles for local authority-appointed trustees who were also elected members of the appointing local authority.

- 2.37 In September 2006, a Trust subcommittee discussed these issues with a trustee whom some considered responsible for disclosing information outside the Trust. The matter was reported back to the Trust at a meeting on 6 November 2006. The trustee denied any wrongdoing and was asked to confirm his commitment to the Trust's confidentiality requirements. The trustee did so and no further action was taken.
- 2.38 Leaks of confidential Trust information, and/or disclosure of information other than through the formal channels, have continued during the past 18 months. We have seen evidence of leaked material being debated in the community or in the hands of journalists since June 2007. Two recent and specific incidents are the leaking of information to the *Greymouth Star* at the time that information was provided to us, and the leaking of information arising from meetings shortly after the election in 2007. From mid-2007, Trust minutes show an increasing level of concern by the chief executive about leaks of confidential material and the effect on the Trust and Trust staff.
- 2.39 Mr Dooley and Mr Trousselot have told us that they were not concerned about confidential Trust information being sent to us, but were very concerned about such material being made public. With the agreement of some of the trustees before the October 2007 elections, they began legal action against Mr Smith, a candidate for election as a trustee (subsequently elected), asking for the return of leaked Trust information and disclosure of the source of his information. Mr Smith has confirmed that he received confidential Trust information about an application for funding and passed it on to the *Greymouth Star*. Despite Mr Smith becoming a trustee in November 2007, the substantive legal action between the Trust and Mr Smith was not resolved until June 2008.

Effect on Trust staff

- 2.40 The West Coast media has taken a keen interest in the Trust and its governance problems. The deteriorating governance environment, breaches of confidentiality, and negative media reporting about the Trust have adversely affected Trust staff. Mr Trousselot and the Trust's marketing manager reported their concerns about the effect on Trust staff to trustees at Trust meetings in 2007.

Part 3

Governance and management issues

- 3.1 By the time we concluded our investigations, it was clear that the specific issues raised with us were symptomatic of more fundamental governance and management problems, rather than major issues in themselves. In this Part of the report, we discuss those general problems that have occupied the Trust during the past 18 months and during the period of our inquiry. We discuss conflict of interest issues in Part 4.
- 3.2 We accept that the Trust has operated effectively for most of its existence. It has received favourable assurance on its performance in the form of stakeholder satisfaction surveys, unqualified annual audit reports, and favourable reviews by this Office and by the Treasury.
- 3.3 The Trust has put considerable effort into building a set of policies and procedures for matters such as managing confidential information and conflicts of interest, based on legal advice.
- 3.4 During the past 18 months, however, the Trust has consumed significant resources in addressing governance issues, some of which had previously been regarded as settled. We have already detailed the background to these issues – in particular, the deteriorating relationship between trustees and the differing views held on the appropriate relationship for the Trust with local authorities. The time and money spent dealing with these matters are likely to have adversely affected the Trust's effectiveness and reputation, and it is clear that the Trust's ability to operate effectively has been harmed during this period of disputes about basic governance issues.
- 3.5 In this Part, we expand on some of the behaviours by trustees that have concerned us. The most significant issues are:
- different views on the role of the Trust;
 - relationships between trustees, and between trustees and Trust staff;
 - disclosure of information;
 - transparency and accountability; and
 - authority for decision-making.
- 3.6 Some progress was made on basic governance issues at a facilitated meeting between all trustees and their individual legal advisers in February 2008. That such a meeting was needed at all, and that each trustee was separately represented by lawyers, is evidence of the level of dysfunction. Nonetheless, we commend the trustees for the agreements that were reached. A great deal more is needed, however, if the trustees are to restore effective working relationships and to build clear and shared understandings on core governance questions.

The role of the West Coast Development Trust

- 3.7 In Part 2, we noted the different dimensions of the Trust's role and the debates that have taken place in recent years between trustees on the role of the Trust.
- 3.8 One particular aspect of this debate between trustees that has surfaced in the past few months concerns the extent to which trustees must act through the Trust or individually. The Trust got legal advice on corporate governance principles in July 2007.
- 3.9 The advice noted that the Trust is a charitable trust board that must give effect to the objects in the Trust deed, but must also act in a commercial manner to achieve those objects. The advice noted that "the Trust is a commercial entity within a charitable structure. The Trustees must operate as a commercial board, not a political council." The Trust resolved to adopt this and other basic corporate governance principles on 6 August 2007.
- 3.10 In mid-2007, Mr Williams obtained his own legal advice (see paragraph 2.28), which took a different view from the Trust's lawyers on some corporate governance matters – including the extent to which a trustee can act independently of the Trust. Correspondence shows that the debate between the legal advisers (and the trustees) on these issues continued for some time.
- 3.11 There has also been some debate about whether newly elected trustees are bound by resolutions of the Trust made before they were elected. All trustees have now accepted that they are bound by lawfully made formal resolutions of the Trust that have not expired, been varied or rescinded, or been overturned by a court. They have also accepted that the principles of transparency and confidentiality bind the Trust as a whole and each individual trustee.¹
- 3.12 We discussed with some of the trustees their view of the nature and role of the Trust. They were clear about the legal nature of the Trust and their obligation to give effect to the Trust's charitable objects. The Trust is involved in the commercial and community sectors, and clearly needs to act in a commercial manner when investing and when dealing with clients. This does not now appear to be contested.
- 3.13 The trustees may have different views on how they should best give effect to the objects of the Trust, and the level of risk that is acceptable. This is to be expected in a group of people with different experiences and backgrounds, and it is not necessary for the trustees to have a common view on such matters. The trustees are free to debate their views at Trust meetings when considering applications and when setting the Trust's strategic direction.

¹ *Development West Coast – Facilitation Agreement*, 4 February 2008. This document records the consensus reached on these and other matters at a facilitated meeting on 4 and 5 February 2008.

- 3.14 However, it is important for the Trust as a whole to have a shared understanding of the way in which the Trust will operate and organise itself as it blends the different aspects of its context into a practical working organisation. It is also important for trustees to agree on the strategic direction. That is the process for bringing together the different perspectives of individual trustees into a coherent framework that can guide the Trust's day-to-day decision-making on applications. Once the strategic direction and governance and management systems have been agreed, all trustees should work within them. If they have concerns or questions, those should be worked through collectively with their fellow trustees in keeping with the Trust's procedures.
- 3.15 After the 2007 elections, the Trust intended to hold a planning day to work through such matters with the new group of trustees. However, it was not possible to have the planning session at that time, given the state of relationships. It was held in April 2008, and a strategic plan has now been agreed. We are also aware that Trust staff have carried out a significant amount of work to prepare new protocols. We encourage the Trust to hold such meetings and to use them to finalise and adopt the protocols. They are the appropriate forum for debating and resolving different views on the role of the Trust, and for the trustees to collectively agree on the policies and procedures under which they and the organisation will operate.

Relationships within the West Coast Development Trust

- 3.16 The Treasury review in 2006-07 led to a reduction in the number of trustees from 12 to six. This change was a direct response to the governance and relationship problems referred to in paragraph 2.14. The Treasury noted at the time that improving the trustees' governance and stakeholder relationships would largely come down to the trustees' abilities and their approach in these areas.
- 3.17 Unfortunately, the six trustees who have been in office since the 2007 elections have not been able to work together effectively in some respects. They have been clearly and publicly split into two factions, each of three trustees, on many issues. During the inquiry, we have seen some of the email communications between trustees. We have been surprised by the tone of some of the emails and the extent of animosity between some of the trustees. We were told that the trustees agreed to a truce on "inflammatory" emails towards the end of 2007. However, our review of communications and minutes of meetings during 2008 shows a continuing problem of unprofessional behaviour and personal animosity.
- 3.18 The trustees should note that, in a situation with some similarities to this one, the High Court has criticised trustees for "playing games". In that case, a faction of

trustees attempted to remove the chairperson of a charitable trust before a vote on a significant issue on which they disagreed with the chairperson.² The trustees first boycotted a meeting to vote on the issue, leaving the meeting without a quorum. They then sought to call another meeting to remove the chairperson and appoint one of their own in his place. This would have given them the numbers to win the vote on the significant matter. The High Court issued orders prohibiting the dissenting trustees from holding a meeting to remove the chairperson, and directing them to attend a meeting to vote on the proposal. The High Court said that the trustees were attempting to misuse the processes of the trust by using trust powers for an improper purpose.

- 3.19 We refer to this case to show that trustees must be careful not to use Trust processes for improper purposes or with an ulterior motive, and that in extreme cases such behaviour can become a legal issue as well as an ethical one. The trustees must give effect to the objects of the Trust and must not use their powers or trust processes for any other reason. The Trust has spent a significant amount of money in the past few months on legal advice to consider and address differences between trustees. The Trust will be less effective in delivering on its objects if Trust resources continue to be consumed in addressing and resolving disagreements between trustees. People may be less likely to apply to the Trust for funding if they perceive the Trust's focus to be on sorting out its own governance problems rather than conducting its ordinary business of promoting economic development.
- 3.20 The elected trustees have been elected for a three-year period and have a mandate from the people that voted for them to be trustees for that three-year period. The appointed trustees have a mandate from their appointing bodies to hold office as trustees for the term of their appointment. Once they become trustees, their primary duty is to the Trust. There is no mechanism in the Trust deed to enable trustees to be replaced with an appointed commissioner if there is a significant governance failure. The expectation is that the trustees will make it work. Any trustee who is not able to work with other trustees or Trust staff should consider whether they are able to be an effective trustee. The trustees need to put aside any personal animosity towards each other and work together in the interests of fulfilling the objects of the Trust for the period of their election or appointment.
- 3.21 One of the new trustees, Mr Smith, has placed considerable demands on Trust staff in terms of information requests. We understand that, in the past, requests by trustees for information from Trust staff were channelled through the chairperson as a way of managing the interface between the governance and management arms of the organisation. The general code of conduct that is being prepared includes a protocol on communication between trustees and

² *Kyd v Collinge & Ors* (unreported, HC Auckland, CIV 2004-404-5049, 17 September 2004, Winkelmann J).

staff. We encourage the Trust to finalise this protocol, given the need to maintain clear lines of accountability, to maintain the distinction between governance and management, and to manage the potential for such requests to place undue demands on staff. It is important that there is a clear and shared understanding of the trustees' information needs for their governance role, and of the systems that are in place to meet those needs, to avoid all parties becoming frustrated.

Disclosure of information

- 3.22 During the inquiry, we discussed the issue of confidentiality with trustees and Trust staff. Everyone that we talked to raised the issue as a concern. We were told that problems first surfaced when confidential Trust information was leaked from the Trust in 2006 and published in the West Coast media.
- 3.23 More recently, and since the 2007 elections, matters discussed at Trust meetings have been made public and the trustees have argued among themselves about whether statements they have made to the media were authorised.
- 3.24 We have not attempted to investigate the detail of these various incidents. It is unclear whether we would have been able to ascertain who had dealt with information inappropriately. Nor did we consider it necessary for the purposes of this inquiry to try to establish those facts. What is clear, from Trust minutes, media commentary, and our discussions with those involved, is that disclosure of Trust information through unauthorised channels has been a significant factor in the breakdown of effective relationships at the Trust in the past 18 months. We have already noted (see paragraph 2.39) the length of time that it took to resolve the legal issues associated with Mr Smith's role in the disclosure of information to the *Greymouth Star*, even after he was elected as a trustee.
- 3.25 The fact that confidential Trust information on applications for funding and on internal governance debates has been made available to the public through the media, including since the election in October 2007, is likely to have reduced the level of trust that people have in the Trust and to have affected the Trust's effectiveness and reputation. Some people that we spoke to consider that leaks of confidential information about applicants has led to a drop in the number of applications for funding. The fact that other matters discussed at Trust meetings since the election have been made public has not helped public confidence, or the confidence of relevant public sector agencies, in the Trust's effectiveness.
- 3.26 The Trust is not subject to the Official Information Act 1982 or the Local Government Official Information and Meetings Act 1987, which provide a system for determining which information should be released and which should be protected. It is therefore not subject to the statutory principles and rules that

guide most other public entities. It has had to develop its own approach based on the Trust deed.

- 3.27 It would be impossible for the Trust to conduct its operations as a provider of funding to individuals and businesses without protecting the confidentiality of material supplied by applicants. Applicants for Trust funding often include sensitive information in applications, and some seek an undertaking that information will be given to relevant Trust staff and members of the advisory body only, and not given to trustees.
- 3.28 The Trust has legal advice that each trustee is bound by an obligation of confidentiality, and that any failure to maintain confidentiality would be a serious breach of duty. The Trust adopted a series of corporate governance principles in August 2007, including that “each trustee is bound by an obligation of confidentiality”.³ The current trustees agree that material submitted to the Trust by applicants must remain confidential. Five out of the six trustees have signed a standard confidentiality agreement agreeing not to disclose any confidential information while as a trustee and after ceasing to be a trustee, and agreeing to indemnify the Trust for any loss or damage suffered through the trustee’s unauthorised disclosure of confidential information. Mr Smith has signed a modified version. Trust employees are also required by their employment contracts and the staff code of conduct to maintain the confidentiality of sensitive information.
- 3.29 The Trust needs to be clear about the authority for communicating Trust matters to the public,⁴ but there does not appear to be more that the Trust could do to protect confidential information. The system relies on the personal integrity of trustees and employees. The confidentiality agreement between the Trust and trustees makes the requirement very clear and imposes a potential financial liability on trustees for breaching it. The requirement to keep sensitive material confidential is a core obligation on the part of employees and members of governing bodies in the public sector. A trustee who inappropriately discloses confidential information is unlikely to be acting in the interests of the Trust, given the likely resulting damage to the Trust’s reputation and effectiveness. Similarly, any employee who leaks confidential information would be in breach of their employment agreement and face serious employment consequences if found to be responsible.⁵

³ *Policy Manual*, Part 2 Trustees, clause 2, page 1 (adopted 6 August 2007).

⁴ We note that the trustees reached consensus on dissemination of information at the facilitated session on 4 and 5 February 2008. It is not clear whether these protocols are operating effectively yet.

⁵ Our comments here are not intended to apply to employees or office holders who have concerns about serious wrongdoing using the Protected Disclosures Act 2000.

- 3.30 The trustees should consider the nature and extent of the Trust's disclosure of information and reporting to the four local authorities and other appointing bodies as part of the requirement to act transparently and be accountable. This is something the trustees should consider and agree as a group, rather than it being a personal matter for the appointed trustees. The results of that agreement should then be built into the general procedures of the Trust. We understand that work is now well advanced to document appropriate policies and procedures on these issues, and we encourage the Trust to finalise and adopt them. All trustees should then operate in keeping with the agreed systems.
- 3.31 The issue of reporting to appointing local authorities is less significant now than in the past, given the changes to the Trust deed to reduce the number of local authority-appointed trustees from four to one. However, we agree with the views in the Treasury review and the Trust's legal advice that a trustee's primary loyalty is to the Trust. It is unhelpful for an individual trustee to take on reporting obligations to an appointing body, and it is likely to be inconsistent with that person's legal duties as a trustee. The nature and extent of reporting to an appointing body should be agreed and managed by the Trust as a whole.
- 3.32 The Trust needs clear systems for working out what is and what is not confidential, and agreed processes for making information available to the public. The Trust had a system for this that used three categories of information. We are pleased that the trustees have recently confirmed previously established principles for determining confidentiality and making information available to the public.

Transparency and accountability

- 3.33 In our 2006 performance audit, we considered that the Trust had mostly met the accountability requirements in the Trust deed in terms of making certain information available to the public. However, we noted that some people thought that the Trust was not transparent in its operations and should conduct more of its business in public. We said that we considered it appropriate for the trustees to discuss applications for funding in closed session, but encouraged the Trust to continue with recent initiatives to hold public meetings on high-level public interest matters (such as regional economic development).⁶ We also encouraged it to continue to improve its systems for measuring and reporting on its performance to the community it serves.

⁶ Paragraphs 2.75-2.80 of our performance audit report, *Management of the West Coast Economic Development Funding Package* (May 2006).

- 3.34 There has been some debate among the trustees about how they should give effect to the requirement in clause 4.2 of the Trust deed, which states:
- The Trust shall conduct its affairs in a manner that is transparent and accountable to the people of the West Coast Region.*
- 3.35 During our inquiry, we received different views from current trustees about the extent to which the Trust should conduct some of its business with the public present. Some trustees consider that the Trust should be more open in its processes and would favour the local authority model, where Trust meetings would be open to the public unless there is good reason to exclude them (for example, when considering applications for funding).
- 3.36 In our performance audit, we said that it was up to the Trust to determine how to meet the transparency and accountability requirements of the Trust deed. From time to time, the Trust has actively considered how best to do this, and uses a range of ways to communicate with the community, as reflected in its strategic plan.
- 3.37 The issue has been debated by current trustees, and they recently confirmed the policy that certain information, such as material about major regional and district initiatives, will be publicly available without request. The trustees also determined who is responsible for communicating this information and the methods of communication, which include public forums.
- 3.38 The approach adopted appears to us to strike a good balance between the need to be transparent and accountable, and the need to protect confidential information. The trustees are likely to need to consider and review their approach from time to time.

Authority for decision-making

- 3.39 This aspect of our inquiry focused on the extent and clarity of delegations by the Trust in the area of distribution of funding to applicants, and the authority for certain other contentious decisions made in the past few months.
- 3.40 Until recently, the Trust has not delegated decision-making powers on applications for Trust funds to committees or to staff to any great extent. Several people that we spoke to told us that trustees had been very “hands on” in terms of decisions on applications. We noted that the advisory body has occasionally questioned its own role given the trustees’ close involvement in operational decisions. The Treasury review found that the trustees needed to have more of a governance focus than they had in the past. This suggests that the trustees need to devote their efforts more to strategy and governance matters than to operational decisions.

- 3.41 The Trust has previously delegated some decision-making authority on applications to a subcommittee known as the committee of chairs – for example, approving expenditure on expert advisers to assess significant proposals and to approve variations to approved funding arrangements on the recommendation of the advisory body. More recently, the Trust has agreed to give a greater level of authority to the chief executive in the area of distribution of funding to applicants. The delegations are now in place for a system of cascading decision-making. But the then chief executive, Mr Trousselot, advised that he and his staff had not been willing to exercise their delegated authority to any significant extent while the governance environment had been so unstable.
- 3.42 In our review of Trust files, we noted that the then chairman, Mr Dooley, had advised trustees at a meeting in October 2006 that he had authorised two separate payments of funds for a Trust client after having considered the negative effects on the business and the Trust’s image and reputation if funds had not been made available. Not all of the pre-conditions required for the Trust support of the client had been met. Mr Dooley told us that he had no specific delegation to authorise payments but, in the case in question, believed he needed to act to ensure that the Trust’s reputation was maintained and because the Trust’s staff with responsibility for distribution had played a part in the client’s failure to meet all of the pre-conditions.
- 3.43 In another case, discussed in paragraph 5.18, an applicant sought a variation to the terms of a funding arrangement. The variation was not significant to the Trust’s position but was to the financial advantage of the applicant. The advisory body approved the variation but Mr Trousselot did not seek approval from the trustees or committee of chairs at that time. The variation was later ratified by the trustees.
- 3.44 These examples are not overly significant. We acknowledge that the Trust will sometimes be under pressure from applicants or funding recipients to make decisions urgently, that staff will sometimes make errors when there is urgency, and that in some cases general policies need to acknowledge that exceptional circumstances may sometimes require a different process. Nonetheless, it is important that all Trust expenditure is properly authorised. We expect all trustees and senior Trust staff to have a very good understanding of financial delegations and to ensure that all financial decisions are properly authorised. Financial delegations need to be accessible and clear.
- 3.45 Mr Trousselot told us that the governance difficulties in the Trust made it hard for routine business, such as approvals or variations of funding terms, to be conducted while maintaining commercial confidentiality. He also told us that

in some cases he and Mr Dooley had had to act in the best interests of the Trust without having complied with the usual pre-approval processes. He told us that retrospective approval was sought in those situations.

- 3.46 Some of the current trustees were also concerned about whether a decision to take legal action against Mr Smith for releasing confidential Trust information to the media, made shortly before Mr Smith was elected as a trustee, was properly authorised. The decision was made by several trustees and the chief executive, but not all trustees were consulted. This issue was before the courts as part of the legal action between the Trust and Mr Smith while we were carrying out this inquiry, and so we have not formed a view on whether the decision was appropriately made. We note, however, that the prolonged debate about the authority for that decision highlights the importance of clear delegations and decision-making authority.
- 3.47 The Trust needs to be very clear where the authority for decisions involving expenditure of Trust funds resides, and the process for making decisions. The Trust deed authorises the trustees to delegate their functions or powers, but where there is no delegation the decision-making authority remains with the trustees.
- 3.48 The recent changes in the composition of the Trust, and the directions agreed to by the Trust in the Treasury review, provide an opportunity to reconsider and rationalise financial delegations, including in situations where urgency is required. The Trust also needs to decide whether it wishes to delegate any authority to the chairperson for financial decision-making. We encourage the trustees to consider and agree on financial delegations as soon as possible.
- 3.49 We also note that we were not always clear whether the delegations that we saw were current. We encourage the Trust to regularly review all policies, including financial delegations.

Overall comments

- 3.50 The operations of the Trust have been hindered recently by the dysfunctional relationship and, at times, animosity between the trustees, and by the inability of the trustees to reach an agreed position on some fundamental issues (for example, concerning leadership of the Trust). This, along with concerns that confidential Trust information has been released into the public arena, has the potential to cause significant damage to the reputation and viability of the Trust. It has certainly stopped it functioning effectively in recent months.

- 3.51 We are pleased to note that the trustees have reached agreement on some initial governance issues and that further work is under way, although it is not clear that these initial agreements are operating effectively yet. On some of these matters, it is essentially a question of the trustees together understanding and accepting the legal advice on the nature of the Trust and on their core obligations as trustees. On other matters, there are questions of direction and procedure for trustees to decide, supported by Trust staff and advisers as necessary.
- 3.52 The work that has already been done to implement the changes agreed as a result of the Treasury review also needs to be consolidated, so that the trustees have more of a governance focus. Strengthening the governance in practice would allow Trust staff to work effectively with the stronger system of delegated decision-making for operational matters.
- 3.53 We urge the trustees to continue to find ways to work together effectively in the interests of achieving the objects of the Trust. The most important change that is needed to alter the governance environment is for the trustees as a group to be able to work together and take collective responsibility for the governance of the Trust. The focus should be on the individual and collective legal and ethical duties they owe to the beneficiaries of the Trust rather than on personal or political differences.

Part 4

Management of conflicts of interest

- 4.1 Some of the specific concerns raised with us at the start of this inquiry involved matters of conflicts of interest. We considered how the Trust managed conflicts of interest where a trustee or staff member had a professional or personal interest in, or connection to, an applicant for funding from the Trust.

Managing conflicts of interest in the public sector

- 4.2 In the public sector there is a conflict of interest when a member's or official's duties or responsibilities to a public entity could be affected by some other interest or duty that the person may have. That other interest or duty might exist because of the person's financial affairs, a relationship or role, or something the person has said or done.
- 4.3 There are two aspects to dealing with conflicts of interest:
- identifying and disclosing the conflict of interest (primarily the responsibility of the person concerned); and
 - deciding what action, if any, is necessary to best avoid or mitigate any effects of the conflict of interest (primarily the responsibility of the public entity).
- 4.4 The assessment of a conflict of interest focuses on:
- the directness and significance of the conflict of interest;
 - the nature or extent of the conflicted person's current or intended involvement in the public entity's decision or activity; and
 - the risks that the public entity's capacity to make decisions lawfully and fairly may be compromised and its reputation damaged if the person participates.
- 4.5 In making this assessment, the entity needs to consider how the situation may reasonably appear to an outside observer. Usually, mitigation means that the person with the conflict of interest withdraws from, or is excluded from being involved in, the public entity's work on the particular matter. Sometimes this is required by statute.
- 4.6 This general public sector approach is stricter than that required of private sector company directors under the Companies Act 1993. Under that Act, directors are required to declare and record a conflict of interest, but the default position is that they are then able to participate in the discussion and decision.
- 4.7 Managing conflicts of interest requires careful judgement, and involves a balance. An approach that is too relaxed has legal and reputation risks, and can undermine public confidence in the entity. Equally, an approach that is too cautious and restrictive could frustrate the entity, its members, and its staff from operating

effectively. General guidance on managing conflicts of interest in the public sector is available from the Auditor-General's guidance publication.¹

- 4.8 Impartiality and transparency in administration are essential to maintaining the integrity of the public sector. Where activities are paid for by public funds or are carried out in the public interest, members of Parliament, the media, and the public will have high expectations. They expect people in the public sector to act impartially, without any possibility that they could be influenced by favouritism or improper personal motives, or that public resources could be misused for private benefit.
- 4.9 The existence of a conflict of interest does not mean that someone has done something wrong, and it need not cause problems. In small New Zealand communities, including the West Coast, conflicts of interest regularly arise and have to be managed. However, they must be managed carefully. Proper management of conflicts of interest benefits and protects both the individual and the public entity.

The requirements of the West Coast Development Trust deed

- 4.10 The Trust deed contains rules for managing conflicts of interests of trustees. It states that a conflict of interest occurs for a trustee when:
- the trustee is associated with another entity, such as a company or another trust, that the Trust is dealing with;
 - the interests or duty of the trustee in any particular matter conflicts with their duty to the Trust; or
 - the trustee is dealing with himself or herself in another capacity.
- 4.11 Clause 19 of the Trust deed states that:
- where a trustee has a conflict or potential conflict of interest, the onus is on the trustee to declare the nature of the conflict at a meeting of trustees;
 - a trustee with a conflict of interest is not able to take part in any deliberations or proceedings, including voting or other decision-making, on the matter in which the conflict exists; and
 - the chairperson may require a trustee with a conflict of interest to leave the meeting, and if the trustee does not leave the chairperson may adjourn the meeting until the trustee leaves.

¹ *Managing conflicts of interest: Guidance for public entities* (June 2007) – available at <http://www.oag.govt.nz>.

- 4.12 Following the Treasury review in 2006-07, the Trust deed was amended in September 2007 to strengthen conflict of interest practices. These changes were intended to codify new practices that the Trust had put in place, and involved:
- having a deputy chairperson, to step into the role of the chairperson if the chairperson has a conflict of interest;
 - applying the same conflict of interest rules to the advisory body that apply to trustees; and
 - stating that a trustee with a conflict of interest is not eligible to participate in a meeting of the advisory body in their capacity as a trustee² about a matter in which they have a conflict of interest, and vice versa.
- 4.13 On various occasions, the Trust has sought legal advice on the meaning or application of clause 19 of the Trust deed. This advice is contained in the Trust's *Policy Manual* and is available to all trustees.

Declaring conflicts of interest

- 4.14 Our review showed that trustees generally declared conflicts of interests at Trust meetings when they arose. There was no suggestion that conflicts of interest were not declared at meetings.
- 4.15 The Trust keeps a register of declarations of conflicts of interest made at meetings. The register records the name of the individual, the matter in which the conflict was declared, the nature of the meeting, and in some cases the nature of the conflict in brief terms.
- 4.16 The register that we reviewed covers the period July 2001 to September 2007. It records 205 declarations of interest during this period. Many of the trustees have declared conflicts of interests at meetings.

Managing conflicts of interest

- 4.17 We did not consider it necessary to review the minutes of all meetings at which conflicts of interest had been declared to check how the Trust had managed them. The matters we did consider were:
- the role of the chairperson in managing conflicts of interest;
 - whether a trustee with a conflict of interest can address the meeting after the conflict of interest has been declared; and
 - managing conflicts of interest outside meetings.

² Meetings of the advisory body are not open to applicants for funding or their financial advisers, so it would be difficult for a trustee who is a financial adviser to participate in that capacity.

The role of the chairperson in managing conflicts of interest

- 4.18 If a trustee declares a conflict of interest, the Trust deed provides that the chairperson may require that trustee to leave the meeting, and may adjourn the meeting until the trustee leaves.
- 4.19 It was suggested to us that Mr Dooley had previously overstepped the chairperson's role under the Trust deed. Minutes from a meeting in August 2007 show Mr Clayton expressing concern that Mr Dooley ruled that another trustee had a conflict of interest while that trustee was out of the room. Mr Dooley commented that he had legal advice confirming that it is the chairperson's responsibility to rule on potential conflicts.
- 4.20 The Trust had previously discussed the treatment of conflicts of interest with its legal advisers, who had attended a trustee meeting in October 2005. The minutes record the advice received was that "Trustees should declare associations in regard to agenda items to allow the chairman to rule whether a conflict situation exists." We have also seen other legal advice obtained by the Trust which says that trustees should not judge for themselves whether they have a disqualifying conflict of interest, and that it is the chairperson who has the responsibility for deciding whether in any given case a trustee faces a conflict of interest that should disqualify the trustee from taking part in decision-making.
- 4.21 In an instance discussed with us, Mr Dooley raised a conflict of interest that he was aware of with Mr Williams, and told Mr Williams that he could not participate in voting on the matter. Mr Williams told us that he had not been aware of the matter and, when advised of it, did not think that it was significant.
- 4.22 Mr Dooley's actions were in keeping with the specific legal advice that the Trust had obtained to clarify the role of the chairperson in conflicts of interest. He cannot be criticised for acting on that advice in keeping with the Trust's documented procedures.
- 4.23 We note, however, that in practice it is often preferable for individual trustees to have an opportunity to identify whether they may have a conflict of interest, and to discuss this if necessary with the chairperson or the other trustees. Even if the chairperson has the formal power to rule on conflicts of interest, it is usually better if such issues are dealt with through discussion and agreement beforehand, so that all those concerned can agree on what action is appropriate. This would assist the transparency and probity of the Trust, and also promote individual and collective responsibility for the integrity of the decision-making processes of the Trust.

- 4.24 It will usually be helpful for a trustee who intends to declare a conflict of interest to discuss the matter with the chairperson before the meeting. The chairperson and the trustee can then discuss mitigation options, given the nature of the conflict and the nature or significance of the matter that the Trust is to discuss. Legal advice could also be obtained if necessary.
- 4.25 If a conflict of interest is not brought up by a trustee, it would be reasonable for other trustees or the chairperson to raise a potential conflict of interest that they are concerned about.
- 4.26 The chairperson then has a role in deciding whether a trustee with a conflict of interest may remain in the room while the matter is discussed.

Addressing the meeting after a conflict is declared

- 4.27 Some people we spoke with raised a concern about whether a trustee with a conflict of interest could address the meeting about the matter in which they have a conflict before refraining from voting or leaving the meeting, and whether the Trust had taken a consistent approach to this. The minutes of some meetings record that a trustee has declared an interest, addressed the meeting, and then left the meeting.
- 4.28 In the minutes of trustee meetings that we reviewed, there were several instances of Mr Dooley declaring an interest and then sharing some information with the other trustees before leaving the meeting.³ Minutes from an April 2007 meeting record that some trustees expressed their concerns about the appropriateness of trustees with a conflict of interest making comment, and the acting chairperson for this section of the meeting undertook to discuss with Mr Dooley his method of sharing information. The minutes note that not all conflicts are clear cut and that often it may be appropriate for a trustee with a conflict of interest to comment.
- 4.29 Minutes from a meeting in August 2007 record Mr Dooley declaring an interest in an application, and being invited by the trustees to provide information relevant to the matter before leaving the meeting. In another example, Mr Williams declared a conflict of interest for a funding proposal and was invited by the chairperson to remain in the meeting and contribute to the discussion.
- 4.30 The Trust deed states that a trustee with a conflict of interest may not take part in any deliberations or proceedings, including voting or other decision-making, on the matter in which the conflict exists. The trustee may remain in the meeting unless required by the chairperson to leave.

³ Minutes of meetings on 7 November 2005, 3 April 2006, 12 June 2006, 1 April 2007, 6 August 2007, and 10 December 2007.

- 4.31 According to the Trust's *Policy Manual*,⁴ the Trust adopted the following policy on 7 August 2006:
- Where trustees have a conflict of interest, they will not address other trustees but vacate the room immediately before the item in question is discussed.*
- 4.32 The Trust had received legal advice that, if a trustee has a possible conflict of interest but also has information that may be relevant to the meeting, that trustee should declare their possible conflict, pass on the information, and then leave the meeting should this be required.
- 4.33 It is reasonable for the Trust to follow the legal advice that it obtained. However, it should have a consistent approach to this issue, and it should document its approach in the *Policy Manual*. The concerns that were raised with us show that not all trustees were comfortable with, or understood the basis for, the approach being adopted.
- 4.34 In our experience with conflicts of interest in the public sector, we generally expect that a board member with a conflict of interest will not address the meeting about the matter in which the conflict exists. Permitting a trustee to do so at the meeting may raise concerns that the trustee has not sufficiently stepped aside from the matter, and may create a perception that the conflict is not being sufficiently or appropriately managed.
- 4.35 We discussed this matter with the Trust's legal advisers. They draw the distinction between an individual providing information and taking part in deliberations. We understand that distinction, and accept that it is a possible interpretation of the Trust deed. It strikes a balance between the public and private sector approaches discussed earlier (see paragraphs 4.2-4.6).
- 4.36 The legal advisers also thought it would not be in breach of the Trust deed if the conflicted trustee addressed the meeting in another capacity, such as that of financial adviser for the application being discussed. In our view, this could create its own risks of perceived unfairness. The Trust would need to ensure that other advisers to applicants had equal access and were able to address meetings of the trustees. Without such a system (and we have not seen evidence of one), we consider that this approach runs the risk of creating an actual or perceived advantage for the adviser who is also a trustee.
- 4.37 In our view, the approach taken by the Trust, based on legal advice, is a possible interpretation of the Trust deed and may be a practical approach given its circumstances. However, it is a less stringent approach than other public entities operate. We encourage the Trust to consider whether it would be possible for trustees with a conflict of interest to advise the chairperson or the chief executive

4 *Policy Manual*, Part 2 Trustees, clause 14, page 11 – Conflicts of interest (adopted 7 August 2006).

of the Trust of any information that they consider necessary before the meeting. It would also protect the trustee and the Trust if that advice was documented, along with the conflict of interest and the reasons the information was nonetheless being provided.

- 4.38 All of the instances discussed in this Part are of trustees with conflicts of interest providing information to meetings. We did not come across any examples of trustees with conflicts of interest being involved in decisions on matters in which they had declared a conflict of interest.

Supporting administrative systems for managing conflicts

- 4.39 We considered whether the Trust's administrative systems were able to support the management of conflicts of interest. Adequate systems exist, but some improvements could be made.
- 4.40 For example, a trustee who has a conflict of interest with an application should not be provided with information on that application. The Trust staff responsible for sending out papers for trustee meetings should take steps to ensure that trustees with a conflict of interest do not receive information about matters in which they have that conflict of interest. The Trust takes this approach, but there have been instances of trustees receiving papers or correspondence they should not have. It was acknowledged at a meeting in April 2007 that there were some inconsistencies in the use of this process and that it needed some attention. Trust staff explained to us that Trust papers are often assembled and distributed to trustees urgently.
- 4.41 Although meeting papers might be distributed before any conflicts of interest have been declared at a trustee meeting, there is a process that should identify potential conflicts of interest in advance. At each monthly trustee meeting, the business enquiries register is provided and discussed. It contains the enquiries that the Trust has received about funding and that may result in formal applications. It gives the trustees an opportunity to declare at the outset any conflicts of interest that might arise if an application is made.
- 4.42 We understand that, if a member of the advisory body receives papers on an application in which they have a conflict of interest, the practice is to destroy the papers unread and to advise that they have done so. The trustees should consider adopting this practice.

The advisory body

- 4.43 We understand that the approach taken by the advisory body to conflicts of interest at its meetings is to permit the conflicted member to participate in the

discussion and voting if they have only a minor involvement with the matter. The advisory body should reconsider this approach because the Trust deed does not permit partial participation based on the nature of the conflict.

Overall comments on managing conflicts of interest

- 4.44 The Trust deed contains clear rules and requirements for declaring and managing conflicts of interest. Trustees and Trust staff are aware of these rules. The Trust has considered how it should manage conflicts of interest, and has received advice from its lawyers. However, more effort is needed to improve the administrative processes that support the management of conflicts of interest.
- 4.45 While individual trustees are responsible for declaring any conflicts of interest, the chairperson also has general and specific responsibilities to protect the integrity of the Trust's decision-making processes. We expect the chairperson to work with trustees in managing conflict issues, with assistance from Trust staff and legal advice as necessary.
- 4.46 Managing conflicts of interest requires integrity and good judgement by the trustees, careful leadership and management by the chairperson, and advice from the chief executive and legal advisers as necessary. The Trust needs to work towards an environment where conflicts are declared and managed without controversy, in the interests of protecting the individual with the conflict of interest and the Trust. This may require the trustees to act with more goodwill towards each other than was evident during our inquiry, where the focus of some trustees after the 2007 elections was on alleging conflicts on the part of other trustees rather than taking individual and collective responsibility for managing them to protect the integrity of the Trust's decision-making processes.

The former chairperson's management of conflicts of interest

- 4.47 We considered how Mr Dooley, the chairman until he stood down in March 2008, dealt with instances when his clients applied for funding from the Trust.
- 4.48 Mr Dooley is a chartered accountant with a business practice in Westport. He has been a trustee since the Trust was established in 2001 and is the longest serving trustee. His accountancy practice has submitted funding applications to the Trust on behalf of three clients, and has also been the accountant for a further three applicants. These six applications amount to about 5% of all the applications considered by the Trust since 2001.

- 4.49 Our review of the files for applicants where Mr Dooley had a professional connection showed that he declared his conflicts of interest at meetings of the Trust. The minutes of relevant meetings record this declaration and whether he left the meeting or remained present after declaring his interest.
- 4.50 Mr Dooley has a good understanding of conflicts of interest and knew that he should not be involved as a trustee in matters where he has a conflict of interest. However, we are aware of one instance where Mr Dooley's conflict of interest was not properly managed by him or by Trust staff. We emphasise that it is only one instance, that the circumstances were complex, and that we do not consider that Mr Dooley intended to act improperly.
- 4.51 It concerned an application that the Trust received from Mr Dooley in his capacity as financial adviser to a client in October 2005. At the applicant's request, it was considered by the advisory body on an urgent basis. It was declined. The minutes of the advisory body meeting list the various aspects of the application that concerned them, and note that any future application would need to address these issues.
- 4.52 Mr Dooley received a copy of the advisory body's recommendation and associated executive summary report in his role as a trustee, which was mistakenly provided to him by Trust staff. The Trust was due to discuss the matter at a meeting two days later. Mr Dooley disagreed with the manner in which the application was presented by Trust staff to the advisory body, and felt that the information before him showed that the Trust staff had not met appropriate standards in their work. Because of the many errors in the executive summary report, he regarded it as fundamentally flawed as a basis for decision-making. Mr Trousselot, the Trust's chief executive at the time, confirmed that the quality of the report was poor and that he disciplined the relevant staff member as a result.
- 4.53 Mr Dooley told us that he sought advice from another accountant about what he regarded as a difficult ethical issue. That advice confirmed that he had a duty as a professional accountant and as a trustee to draw the errors to the attention of those who would be making the decision. He also considered that his actions were in keeping with legal advice previously given to the Trust that trustees had a duty to disclose relevant information. He wrote an urgent letter to his fellow trustees setting out his comments on the matter and attaching a full copy of the application and an independent adviser's report.
- 4.54 The letter was printed on Mr Dooley's professional letterhead and contained comments from his perspective as financial adviser to the applicants, from his experience in the relevant sector, and in his capacity as a trustee. The letter included a number of angry and at times personal comments. In our view, the

tone of the letter was not appropriate. Mr Dooley asked the trustees not to adopt the recommendation of the advisory body and to refer the application back to the advisory body for further analysis and consideration.

- 4.55 The minutes of the meeting to discuss the advisory body's recommendation record that Mr Dooley had declared a conflict of interest in the application. Before leaving the meeting, Mr Dooley discussed the letter he had written and circulated a further one-page summary of facts about the performance of the applicant.
- 4.56 After Mr Dooley left the meeting, the trustees resolved to remove the letter from the application information. In the discussion about the application, Mr Trousselot commented that his staff had not had enough time to assess the application, and that he believed that a true analysis of the application would have resulted in a favourable outcome. The trustees decided to refer the matter back to the advisory body with additional information and analysis for further consideration, and resolved that an independent consultant be used to assess the information if required. The advisory body later recommended supporting the application in principle, subject to various requirements including a report from an external consultant.
- 4.57 Mr Dooley was placed in a difficult position after receiving the advisory body recommendation and executive summary report. We acknowledge his concerns with the information provided to the advisory body and the resulting decision, and that he considered he had a professional duty to correct this information. However, a perception could be drawn from the events that followed that Mr Dooley was using information obtained as a trustee to advocate for, and obtain special treatment for, his client.
- 4.58 In our view, his concerns could have been handled better. Writing a letter to the chief executive would have been more appropriate. The letter should have begun with a clear acknowledgement of the conflict of interest and the steps being taken to manage it, as well as the reasons he was taking the unusual step of intervening in the decision-making process despite that conflict. The letter should also have made clear that on this matter he acted as an adviser and not as a trustee. He could not write in both capacities. The letter should then have set out in dispassionate terms the information that he thought needed to be known by the Trust.
- 4.59 Mr Dooley should then have relied on the chief executive and the Trust's organisational systems to deal with the matter appropriately, and should not have participated at all in the Trust discussion. This approach would have enabled the conflict of interest and the associated ethical dilemma and factual concerns to be clearly recorded, along with the actions being taken to manage them. Mr Dooley

would have been able to provide the information that he thought was important for the Trust to have, while visibly remaining at arm's length from the decision-making.

- 4.60 Clear documentation is the simplest way to manage such risks, and would have better protected both Mr Dooley and the Trust. It is also important in such circumstances to set out the relevant facts calmly and clearly, and to avoid letting emotion cloud the issues. The risk of a perception of inappropriate influence was exacerbated by the letter not clearly separating out Mr Dooley's roles and perspectives, and by its tone.
- 4.61 Mr Dooley is committed to economic development in the West Coast and spends a lot of time on Trust business, such as attending advisory body meetings to take part in discussion on applications. Mr Dooley's access to Trust staff and the advisory body, and his knowledge of the Trust's approach to applications, could easily be seen as advantageous to his clients. Mr Dooley told us that he decided in August 2006 not to act as financial adviser for new applications to the Trust. He has not done so since then.
- 4.62 It was generally clear from the files we reviewed when Mr Dooley was liaising with Trust staff in his professional capacity. It is the usual approach of the Trust for the Trust staff to liaise with applicants and the applicants' advisers when preparing an application.
- 4.63 However, we consider that the two capacities held by Mr Dooley could create confusion or difficulties for Trust staff in dealing with Mr Dooley. We saw one instance when a staff member asked Mr Dooley, as chairman of the Trust, to approve expenditure on a consultant to help the advisory body with an application where Mr Dooley was the applicant's accountant. Mr Dooley's association with the applicant would have been evident from the application form. He did not give the approval sought, but referred the matter to the chief executive.⁵
- 4.64 It was suggested to us that applications from the Buller district, where Mr Dooley resides, had been preferred. We did not consider it necessary to review this in any detail because information about Trust distributions is publicly available in the Trust's annual reports. It does not show any undue favour to the Buller region.

The chief executive's management of conflicts of interest

- 4.65 We considered the position of Mr Trousselot, as the chief executive of the Trust, when he was appointed as director of companies receiving funding from the Trust.

⁵ We note that Mr Dooley responded to the staff member immediately and angrily when he received this request. The language in which he responded was inappropriate and unprofessional.

- 4.66 It is sometimes a condition of receiving funding from the Trust that the Trust is able to nominate or appoint an individual to the board of directors of the company. This gives the Trust direct involvement with the governance and performance of the company, and can be useful in providing assistance to the company in a specific skill-set. The Trust usually arranges for an external person with the appropriate expertise to be appointed to the board on its behalf.
- 4.67 The *Policy Manual* provides for Trust staff being appointed as directors, but only where the company is a wholly-owned subsidiary. The Trust had received legal advice in 2002 that recommended that Trust employees should not be appointed to company directorships, because there was a significant risk of actual or potential conflicts of interest arising. The individual would have obligations to the Trust as an employee and to the company as a director.
- 4.68 The Trust's practice evolved as its understanding of its role developed. It later received legal advice suggesting this previous advice may not be appropriate to the nature of the Trust. The Trust was advised that equivalent organisations in the private sector (in the field of venture capital) do sometimes appoint employees as directors to companies in which they have made a significant investment, to help protect their interests.
- 4.69 In 2006, Mr Trousselot was appointed as a director on the board of three companies receiving financial assistance from the Trust.⁶
- 4.70 The roles of chief executive and director have different responsibilities, and may give rise to conflicts of interest because the interests of the Trust and the company will not always be the same. Directors are required to act in good faith and in what they believe to be the best interests of the company,⁷ while the role of chief executive is to provide objective advice and guidance to the governing body. The role of chief executive of the Trust includes making sure that there are enough checks and balances within the Trust's systems to ensure that funding decisions are implemented appropriately. We therefore considered how the Trust managed this issue.
- 4.71 In guidance we produced for the local government sector,⁸ we expressed the view that chief executives should not be put in a position of conflict between their roles as advisers to the local authority and their obligations as company directors

6 One directorship was an appointment by the Trust; the other two directorships concerned related companies where the chief executive was nominated by the Trust and appointed by the shareholders. The chief executive resigned from the Trust-appointed position in October 2007, and from the two other positions in April 2008 when he resigned as chief executive of the Trust to take up another position.

7 Companies Act 1993, section 131(1). There are some modifications to this duty for subsidiary companies, where a director may be permitted by the company's constitution to act in the best interest of that company's parent company. If the company is not a wholly-owned subsidiary, the prior agreement of all the shareholders is required.

8 *Local Authority Governance of Subsidiary Entities* (2001); *Governance of Local Authority Trading Activities* (1994).

because this arrangement exposes the local authority to possible allegations of bias and impropriety, regardless of the integrity of the chief executive. For many public sector organisations, the same considerations will apply.

- 4.72 The balance may be different in some organisations. For example, more commercial entities, such as State-owned enterprises, will often establish subsidiary companies and joint venture arrangements. They may build in structural links across the group of companies by appointing the chief executive or other board or staff members to the boards of those companies. This model can be appropriate in a closely held group of companies where there is synergy in the activities of the group, and the chief executive can be seen as having a high degree of responsibility for the group as a whole rather than just the parent entity.
- 4.73 The Trust is not a local authority, nor is it a purely commercial organisation. It is a trust with a commercial function. The relationship between the Trust and the companies it provides funding to is an investment and commercial relationship rather than an ownership or company group interest. It is appropriate for the Trust to have considered the range of ways in which it can manage its investment risk and to have sought legal advice on that question. We agree that the practice of private venture capital businesses is an appropriate model for the Trust to emulate.
- 4.74 The trustees agreed to the appointment of Mr Trousselot as a director to help protect the Trust's investments and to give the Trust access to more detailed information and knowledge about the applicant companies.
- 4.75 In the case of the Trust's nomination of Mr Trousselot to the two related companies, the minutes of the meeting where Mr Trousselot was nominated as director do not record any discussion of the potential for a conflict of interest. Questions were raised by some trustees about Mr Trousselot's workload, the directors' fees, and what benefits would be achieved by the arrangement, but the potential for a conflict was not discussed.
- 4.76 Mr Trousselot told us that thought was given to the management of the inherent conflicts of interest with his three directorships:
- The Trust's relationship manager⁹ was to liaise directly with the applicant companies and report independently on the status of the funding conditions and key performance indicators to the Trust. Reports were also provided to trustee meetings by Mr Trousselot as director.
 - Mr Trousselot was to liaise with the Trust's relationship manager regularly to discuss any areas of difficulty. He acknowledged that there could be potential for tension, and suggested that any issues could be referred by the relationship

⁹ The role of the relationship managers (who are Trust employees) is to monitor the Trust's investment with each successful applicant, including ensuring compliance with funding conditions and requirements, and report back to the Trust.

manager to the Trust's chief financial officer, auditors, advisory body, or the chairperson.

- Mr Trousselot was to act in the best interests of the Trust, and advise the company of this if any conflicts of interest arose in doing so.

4.77 In April 2007, some time after the appointments were made, a paper outlining proposed Trust structures and board compositions, prepared for discussion by the Trust, contained a section about terms of engagement for board members as directors. It stated that there should be a deed of engagement for all board representatives or director appointments that would clearly specify any reporting requirements and the channels for this. It also commented that:

- where directors were appointed to companies receiving Trust funding, confusion had arisen about the flow of information from directors to the client relationship manager;
- it was important to ensure that the relationship manager was able to monitor the covenants and ensure that financial reporting requirements were adequately fulfilled – it therefore proposed that the relationship manager should continue to deal directly with clients to manage the funding; and
- any reporting requirements of a director should be to the parent organisation (Trust or holding company) and on more general aspects of the client, rather than around the management of the funds.

4.78 In our view, it was reasonable for the Trust to appoint Mr Trousselot as a director, and consideration had been given to the terms of engagement, how conflicts of interest should be managed, and how reporting lines should be adjusted. The understandings that underpinned the appointments may well have been enough if the Trust's operating environment had not deteriorated in the way it did. Once that happened, however, it affected both trustees and staff. We have already noted the effect on general levels of trust and co-operation, and the increasing tendency to level allegations at one another that emerged. That concerns were raised with us shows that the arrangements were not robust enough for the changed environment. Some people developed the perception that the conflicts of interest were not being properly managed.

4.79 As with all conflicts of interest, there will often be perception issues to manage. It is possible for relatively simple procedural matters to take on a life of their own when conflicts of interest are not managed very clearly and openly, with careful attention to detail. This is particularly so when operating in an environment of distrust. One such matter raised with us was about a letter on behalf of the Trust to the bank of one of the companies of which Mr Trousselot was a director. Mr Trousselot had finalised the letter, using Mr Dooley's electronic signature. It was

suggested to us that Mr Trousselot was under pressure from the company to present an option to the bank that would be more favourable to the company's future financial situation than Mr Dooley and advisory body members were prepared to agree to before any Trust decision on the matter.

- 4.80 During our inquiry, Mr Trousselot told us that he would have sent the same letter regardless of his directorship with the company. Mr Dooley also assured us that he had no concerns about the use of the signature or the content of the letter. It is clear from the documentation at the time the letter was sent to the bank, however, that he had had some initial concerns.
- 4.81 We do not regard this incident as significant. Given the conflict of interest, it would have been preferable for Mr Trousselot not to have been involved with this matter, but we acknowledge the practical difficulties that can arise in an entity with a small number of staff members working under time pressures.
- 4.82 We accept the Trust's view that the directorship appointments provided the Trust with an enhanced level of information about its investments. However, this should not be a substitute for a formal monitoring relationship, carried out independently of the person appointed as a director. We note that some difficulties arose out of this arrangement, in part because of a deteriorating working relationship between Mr Trousselot and the relationship manager. Mr Trousselot had concerns about the monitoring and reporting against the Trust's conditions that was carried out by the relationship manager. Given these issues, it would have been preferable for a formal arrangement to have been adopted where the relationship manager had a separate reporting line (not to Mr Trousselot) for the purposes of these companies.
- 4.83 A deed of engagement was entered into for two of Mr Trousselot's three appointments as director. The deed provides for various matters, including the release of information by the directors to the Trust, but does not alter the duties of directors to act in the best interests of the companies.
- 4.84 The Trust's approach for independent directors appointed by the Trust to a subsidiary company is for a deed of engagement to be entered into between the director, the subsidiary, and the Trust's holding company requiring the company's constitution to be altered to allow the director to act in the best interests of the holding company.
- 4.85 The Trust should also clarify and document the treatment of directors' fees and expenses incurred in fulfilling the director roles (such as costs incurred in attending board meetings). We were told that the Trust permits directors'

fees to be retained by the individual but that any expenses incurred should be reimbursed by the company to the Trust. At the time we carried out our fieldwork, Mr Trousselot had asked Trust staff to keep a record of his expenses but the Trust staff had not yet sought reimbursement for the Trust. We understand this has since been done.

- 4.86 As we noted in paragraph 4.78, it was reasonable for the Trust to appoint Mr Trousselot as a director, but the arrangements for managing this would have been stronger if they had been more carefully and clearly documented and explained to Trust staff and other interested parties. On the question of reporting lines for staff within the Trust who were managing relationships with companies where the chief executive was a director, it would have been better if the reporting lines were formally changed for all issues relating to those companies. To keep the usual reporting lines until trouble emerged was not a robust enough approach.

Part 5

Other issues

- 5.1 During our inquiry, other issues were raised. Generally, these issues were about compliance with policies and procedures for financial assistance to applicants, and whether Trust resources (staff or money) had been used to benefit certain applicants.
- 5.2 Specific issues raised with us were that:
- Trust staff had assisted an applicant associated with Mr Dooley in preparing an application for funding from the Trust, at the direction of Mr Dooley and/or Mr Trousselot;
 - Trust staff had assisted with a business plan for an applicant company of which Mr Trousselot was a director;
 - Mr Trousselot had not sought necessary approvals for a change in the terms of the Trust's funding to a company for which he had been appointed a director; and
 - Mr Trousselot had departed from parameters set by the advisory body when negotiating a proposed funding arrangement with an applicant; and
 - Mr Dooley had lent money to an applicant to enable the applicant to meet a minimum capital requirement for the funding obtained, in breach of Trust policy.
- 5.3 We reviewed the Trust files for applicants where Mr Dooley was an adviser and where Mr Trousselot had been appointed a director, considered relevant Trust policies, and discussed the matter with Trust staff, Mr Trousselot, and Mr Dooley.
- 5.4 We investigated these allegations and did not find anything that caused us concern. We found that Mr Dooley and Mr Trousselot had acted with due regard to Trust policies and procedures for financial assistance to applicants. We briefly explain what we found and our conclusions in the rest of this Part.

Compliance with policies and procedures

- 5.5 The Trust has a *Policy Manual* setting out its standard policies and procedures. It outlines the process that applications should follow, and sets out financial limits and approaches. The *Policy Manual* is regularly reviewed by the Trust, and was being updated when we visited the Trust.
- 5.6 All commercial applications for funding are considered by the advisory body, which makes a recommendation to the trustees. For significant applications, Trust staff are closely involved with applicants during phases such as due diligence and negotiation of terms, both before and after the advisory body considers the application. Applications may be considered by the advisory body several times before a recommendation is made to trustees.

- 5.7 The terms and conditions of funding for an applicant are set out in the advisory body's recommendation to trustees. The trustees can vary these terms and conditions with the agreement of the advisory body. Although the chief executive has delegated authority to approve expenditure on some distributions, final decisions on all applications have, to date, been made by the trustees.
- 5.8 A number of concerns were raised with us about what Trust policies required in one situation, involving a relatively small Trust loan. This particular matter has been at the centre of much of the concern and debate over the last year, and so we deal with it in some detail.
- 5.9 Mr Dooley was the applicant's accountant, became its financial adviser, and later also loaned the applicant money to assist with the project being funded from the Trust. The questions raised with us related to:
- whether a trustee should lend money to an applicant;
 - the management of the conflict of interest; and
 - whether there was a problem in relation to the Trust's policy of lending a maximum of 90% of the cost of any proposal from an applicant.
- 5.10 There is no Trust policy prohibiting a trustee from lending money to, or investing money with, an applicant. If trustees did so, they would need to declare a conflict of interest and step aside from decisions on that application.
- 5.11 Mr Dooley declared a conflict of interest and removed himself from the decision-making each time this application or file came before the trustees for a decision. The declarations did not separately identify the potential and later actual financial relationship. In some meetings he stayed in the room to provide background information to the meeting, but did not participate in the decision-making. Mr Dooley therefore managed the conflict of interest in accordance with the Trust's normal practices.¹
- 5.12 The last question, about the interaction with the Trust's policy of lending a maximum of 90% of the cost of any proposal, was more complex. Trust policy does not prevent an applicant borrowing elsewhere to meet the remaining 10% of the cost. Information on the source of that 10% contribution may be relevant to the assessment of the application and consideration of risk, particularly in bigger loans. On this application, the papers that Trust staff prepared for the advisory body and the Trust did not focus on how the applicant could fund the required 10% contribution or that it might be funded by way of a loan, and there was no apparent focus on this aspect when risks were considered through the Trust's

¹ We comment on those practices in part 4.

processes. In our view, it might have been useful for that information to have been specified, but we note again that this was a relatively small loan and that the applicant's financial position was reasonably obvious from other documentation.

- 5.13 With the benefit of hindsight, we think it was unfortunate that the fact of the potential and later actual loan was not apparent from the Trust's records from the outset, either through the working papers on the application or from Mr Dooley's conflict of interest declarations. While in both cases reasonable judgements may have been made about relevance or materiality, the combination of those separate judgements meant that the information was not on the record anywhere. Given the atmosphere of distrust prevailing in the Trust, that gap meant that questions were able to be raised later when the fact of the loan did come to light. Fuller disclosure through either route might have helped avoid some of those concerns arising.

Use of Trust resources to assist applicants

- 5.14 The *Policy Manual* provides that a thorough and complete evaluation of applications is to be carried out by management. This can involve a lot of early interaction between Trust staff, the applicant, and the applicant's advisers to present a comprehensive appraisal to the advisory body.
- 5.15 We did not find that an inappropriate or unusual level of assistance had been provided to some applicants, based on any degree of connection with staff or trustees. Further, we did not find any evidence in our file review or interviews of inappropriate involvement or direction by Mr Dooley or Mr Trousselot to Trust staff involved in certain applications.

Variations to funding arrangements

- 5.16 The chief executive is often involved in negotiating the terms of funding arrangements with applicants. This can take some time, and the advisory body may discuss an application several times before making a recommendation to the trustees. It is expected that Trust staff will use their commercial judgement in these matters.
- 5.17 From the files we reviewed, Mr Trousselot had acted appropriately in this process. We would expect any significant changes to negotiation parameters previously agreed by the advisory body to be reported back to the advisory body.

- 5.18 In one instance discussed with us, the basis for funding one of the companies of which Mr Trousselot was a director had been changed without being referred back to the trustees. The change was relevant to the company's tax position and was not significant to the Trust's position. The change was agreed to by the advisory body but not referred back to the trustees for approval. This oversight was noticed by our appointed auditor, and retrospective approval was later obtained. It appears that the committee of chairs had the delegated authority to approve the variation, so the matter did not need to go back to the trustees. We do not regard this issue as significant.

Part 6

Our conclusions

- 6.1 The Trust has a significant responsibility to the community of the West Coast region. As the Government's policies to end logging would have a significant effect on the region, the Trust was established to help the region's economy adjust. It was entrusted with \$92 million to help create sustainable economic growth and new jobs in the region through careful and strategic investments. Creating the organisation as a trust placed particular responsibilities on the trustees to act solely in the best interests of the people of the region.
- 6.2 We carried out our performance audit of the Trust in 2006 because we considered it important to provide some assurance over the way in which such an important local fund was being managed. As already noted, our audit showed an organisation that was developing well. There were some emerging issues that required attention, but the overall report was positive.
- 6.3 We are disappointed that, only two years later, we have needed to inquire into the Trust.
- 6.4 We have investigated the various incidents that were raised with us. We have detailed the particular incidents and our conclusions on them in this report because we consider it important to explain to the public what the facts are, and to "set the record straight" on issues that have been covered in the media, rather than because we consider that the incidents are particularly significant. We have identified minor administrative errors that could have been handled better, some processes that could be improved, and occasional instances of poor judgement on the part of Mr Dooley. We have seen nothing to suggest bad faith on the part of Mr Trousselot or Mr Dooley. Those few errors and instances of poor judgement have to be set against the record of effective and appropriate administration during the Trust's first seven years of operation. They must also be set against the increasingly difficult operating environment of the past 18 months, which has meant that the ordinary systems supporting the Trust's decision-making have at times failed or been effectively unavailable.
- 6.5 The relationships between trustees, and the inability to resolve basic questions of governance and management so that the Trust could start to operate effectively again, have been of much more concern to us. The Trust is dysfunctional. The behaviour that we have seen there during the past 18 months is not appropriate for a public entity, or for trustees.
- 6.6 The trustees have been unable to work effectively together since late 2006. Personal opinions and local politics appear to have prevailed over the basic fiduciary duties of the trustees to work together in the best interests of the Trust's

beneficiaries. The inability to agree on the core role of the Trust, how it should operate, how information should be treated, and the many other issues covered in this report have all contributed to an atmosphere of suspicion and distrust. That atmosphere has manifested itself in hostility and accusations.

- 6.7 We make only one formal recommendation. It is that the group of trustees urgently find a way to work together so they can take effective collective responsibility for the governance of the Trust.
- 6.8 All trustees need to focus on the legal and ethical responsibilities they owe, individually and collectively, to the Trust and to the community of the West Coast region. If trustees cannot make that change, and remain unable to fulfil their responsibilities, then they should consider stepping down.
- 6.9 Until we see evidence that the group of trustees is able to take effective collective responsibility for the governance of the Trust, we are unable to provide assurance that the Trust is able to deliver fully on its purpose of generating sustainable employment opportunities and economic benefits for the people of the West Coast region.

Appendix

Terms of reference

Auditor-General's inquiry into Development West Coast

30 October 2007

The inquiry

The Auditor-General has decided to carry out an inquiry into aspects of the operations of the West Coast Development Trust (the Trust) now operating as Development West Coast.

These terms of reference set out the full nature and scope of our inquiry into this matter.

The inquiry will consider certain matters in relation to:

- the management of conflicts of interest by the Trust;
- compliance with procedures and policies for financial assistance to Trust applicants;
- use of Trust resources to benefit Trust applicants; and
- roles and responsibilities in the governance and management of Trust operations.

The inquiry will also consider such other matters arising out of the inquiry that the Auditor-General considers it desirable to report on.

Our mandate

The Trust is a public entity within the Auditor-General's mandate.

The inquiry will be conducted under sections 16(1) and 18(1) of the Public Audit Act 2001. Those sections provide as follows:

Section 16 – Performance audit

(1) *The Auditor-General may at any time examine—*

- the extent to which a public entity is carrying out its activities effectively and efficiently;*
- a public entity's compliance with its statutory obligations;*
- any act or omission of a public entity, in order to determine whether waste has resulted or may have resulted or may result;*
- any act or omission showing or appearing to show a lack of probity or financial prudence by a public entity or 1 or more of its members, office holders, and employees.*

Section 18 – Inquiries by Auditor-General

(1) The Auditor-General may inquire, either on request or on the Auditor-General's own initiative, into any matter concerning a public entity's use of its resources.

Reporting

Section 20 of the Public Audit Act permits the Auditor-General to report on any matter arising out of the performance and exercise of his functions, duties, and powers as he considers it desirable to report on. The Auditor-General will decide on the appropriate manner in which to report his findings on these terms of reference once the inquiry has been completed.

Publications by the Auditor-General

Other publications issued by the Auditor-General recently have been:

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- Reporting the progress of defence acquisition projects
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- Local government: Results of the 2006/07 audits – B.29[08b]
- Procurement guidance for public entities
- Public sector purchases, grants, and gifts: Managing funding arrangements with external parties
- The Accident Compensation Corporation's leadership in the implementation of the national falls prevention strategy
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- Guardians of New Zealand Superannuation: Governance and management of the New Zealand Superannuation Fund
- Annual Plan 2008/09 – B.28AP(08)
- Central government: Results of the 2006/07 audits – B.29[08a]
- The Auditor-General's Auditing Standards – B.28(AS)
- Responses to the Coroner's recommendations on the June 2003 Air Adventures crash
- Inland Revenue Department: Effectiveness of the Industry Partnership programme
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Office of the Auditor-General
Private Box 3928, Wellington 6140

Telephone: (04) 917 1500
Facsimile: (04) 917 1549

Email: reports@oag.govt.nz
www.oag.govt.nz