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BOOK REVIEW

Samuel P. King & Randall W. Roth, *BROKEN TRUST: GREED, MISMANAGEMENT, AND POLITICAL MANIPULATION AT AMERICA'S LARGEST CHARITABLE TRUST* (2006)

This book -- which recounts the saga of the eventually successful efforts to forcibly remove the trustees of the Bishop Estate -- is a highly readable though depressing account of the ways in which human greed can interfere with the accomplishment of laudable charitable purposes. The problems with trust governance began to draw public scrutiny in 1995, when the Estate announced that it would eliminate community education outreach programs that benefited more than 10,000 people annually, including young people and parents in outlying areas of the Islands, inhabited mainly by native Hawaiians. The trustees said there were financial constraints leading to the closure of the programs even though the net worth of the endowment had risen to at least \$10 billion and they continued to pay each of the five of themselves annual salaries of more than \$800,000.¹

In addition, the trustees had established a governance system in which each one was "lead trustee" for a particular aspect of the Estate's activities, with no general board oversight. The most disliked of the trustees was the trustee in charge of educational activities, Lokelani Lindsay, who actively interfered in the management of the school and at times tried to intimidate students and faculty members who were trying to express their frustration with her attempts to oust good teachers and administrators in favor of her hand-picked (and not particularly well-qualified) cronies. It was principally her actions that spurred thousands of Kamehameha staff, alumni, and other concerned citizens to march from the royal mausoleum, where Princess Bernice Pauahi Bishop was laid to rest, to Bishop Estate's headquarters on May 15, 1997, to protest trustee mismanagement and abuse.

Then, on August 9, 1997, the Honolulu Star-Bulletin published an essay in its editorial section under the banner headline "Broken Trust." The essay, written by five prominent Hawaiians began: "The community has lost faith in Bishop Estate trustees, in how they are chosen, how much they are paid, how they govern. The time has come to say 'no more.'" One of the authors of the essay, Prof. Randal Roth of the University of Hawaii, William S. Richardson School of Law, went on to co-author, with Senior U.S. District Court judge Samuel King, this book of the same name.²

The Bishop Estate was created in 1884 by the bequest of Princess Bernice Pauahi Bishop, the last direct descendent of King Kamehameha I of the Kingdom of Hawaii. The book recounts in detail Princess Pauahi's desire to advance the education of native Hawaiians, whose population had been decimated as a result of the introduction of foreign influences and diseases. She therefore was determined to set up a school for the education of such individuals, and under her will she

¹ The amount of compensation was based on a formula derived from state law (two percent of the Estate's tax-free revenues plus commissions on some taxable profits plus comparisons with salaries paid to CEO's of multi-billion dollar for-profit companies. The value of such compensation to the trustees is evident from the book's description of the joy expressed by Lokelani Lindsay when she received word of her appointment.

² The book has an extensive website, with many of the legal documents relevant to the two cases (see note 3) and their outcomes. It is available at <http://www.brokentrustbook.com/index.html>, which lists 48 legal issues raised by the Bishop Estate imbroglio.

directed that 434,000 acres of royal lands be set aside for in a charitable trust to be used for the benefit of the Kamehameha School for native Hawaiians.³

For many years the trust operated appropriately, but it began to fall under the influence of powerful politicians and corrupt members of the judiciary. The Supreme Court of Hawaii had assumed the power to select the trustees,⁴ which carried with it the duty to carry out that responsibility with due care and the goal of benefiting the trust. That this did not occur is evident from the many conflicts of interest between the justices and the trustees, including the appointment of the Chief Justice as a trustee! Indeed, a few months after the publication of the Broken Trust essay, the justices stopped naming trustees and the power to do so is now vested in a single probate judge.

Publication of the essay led the governor of Hawaii to order the attorney general to commence an investigation, and she initiated both a civil inquiry and a criminal one. In addition, the Federal Internal Revenue Service (IRS) launched an investigation into the issue of excessive compensation, use of charitable funds for personal purposes, conflicts of interest and self-dealing, and impermissible lobbying. The IRS threatened to revoke the trust's tax exempt status unless the sitting trustees⁵ were removed because it believed the Estate's assets to be at risk.

The state investigations found the following:

1. repeated payment of excessive compensation;
2. concentration of huge sums in an international investment portfolio instead of spending the money to improve the school, add campuses, etc.;
3. trustee conflicts of interest including personal investments made in investments held by the Estate and use of nearly \$1 million of Estate assets to lobby against legislation that would have limited the trustees compensation;⁶
4. use of Estate employees to do personal work; and
5. micromanagement of the educational aspects of the Estate.

One particularly egregious conflict of interest uncovered was when a trustee "recused" himself as a Bishop Estate trustee just long enough to negotiate on behalf of a buyer for the purchase of Bishop Estate land. The state proceedings were settled in 2000, when the Estate agreed to pay

³ There was a dispute about whether a stipulation that native Hawaiians will be given preference in admissions is lawful. The terms of Princess Pauahi's will do not require that only native Hawaiians be admitted to the school, but the school had limited admissions to such persons. See *Doe v. Kamehameha Schools*, [http://www.ca9.uscourts.gov/ca9/newopinions.nsf/A294DE38BC83F75B88257051005488B8/\\$file/0415044.pdf?openelement](http://www.ca9.uscourts.gov/ca9/newopinions.nsf/A294DE38BC83F75B88257051005488B8/$file/0415044.pdf?openelement). The lawsuit was settled in May 2007. See Kamehameha Schools website press release, available at www.ksbe.edu.

⁴ According to Randall Roth, when the will was written justices of the Supreme Court of the Kingdom of Hawaii had original jurisdiction over probate matters. "When Hawaii became first a republic, then a territory, and then a state, the Supreme Court ceased to have original jurisdiction over probate matters, but the justices continued to select Bishop Estate trustees, now in an unofficial 'individual capacity.'"

⁵ It should be noted that one of the trustees, Oz Stender, whom King and Roth call the "accidental" trustee (he was appointed as a compromise candidate), tried valiantly to persuade the other trustees to act more appropriately. Unlike the others, Stender had actual experience as a trustee of a charitable trust, and the book recounts in detail his inability to change things due to the intransigence of the others.

⁶ This was the Federal Intermediate Sanctions legislation, which eventually became § 4958 of the Internal Revenue Code.

\$25 million to the State of Hawaii. But even then the trustees did not suffer, for this was all covered by insurance.⁷

The Federal investigation, which had threatened the Estate with loss of tax exempt status as a charity, was also settled. The Estate agreed to pay \$9 million, again covered by insurance.⁸ Under the closing agreement, which is available on the website of the School (www.ksbe.edu), there was a restructuring of the institution and its oversight. For example, it was agreed that the management of the School be placed in the hands of a Chief Executive Officer⁹ and that the trustees exercise only normal policy making and other duties typical of such bodies. Various other conditions were specified, including that business meetings must be documented in writing, that a comprehensive business and investment strategy be developed, and that annual reports be prepared and filed in a timely fashion, with the attorney general as well as the IRS.

The book received three awards in 2007 from the Hawaii Book Publishers Association, including "Book of the Year." It is a valuable book for all who are interested in the ways in which charitable intentions of donors can be perverted by corruption and mismanagement by those who owe fiduciary duties to the beneficiaries. The familiar refrain of the book – that courts charged with oversight of the largest charitable trusts can fail in performing their duties -- is also one that needs to be borne in mind by all who seek to develop a better regulatory framework for the not-for-profit sector. Randall Roth has suggested, for example, that the Bishop Estate should be transformed into a charitable corporation, which would allow for greater oversight by the attorney general. Nevertheless, there are many stories of bad board oversight of such entities as well. Perhaps there is no panacea – just a need for continuing vigilance and the willingness of concerned community members to speak out when wrongdoing is unearthed, as they did in Hawaii.

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⁷ See Stephen C. Greene, Insurer to Pay \$ 25 Million to Settle Dispute in Hawaii, Chron. Philanthropy, Oct. 5, 2000, at 42.

⁸ See Stephen C. Greene, Bishop Estate to Pay IR \$9 Million but Retain its Tax-Exempt Status. Cron. Philanthropy, Jan. 13, 2000, at 50. The insurance policy, paid for by the Estate, also reimbursed the trustees for their legal expenses in defending their wrongdoing – some \$4 million!

⁹ This was also mandated by the Hawaii Probate Court.