



Tuesday, April 12, 2005

April 5, 2005

Final Report on CBT Energy Inc. – Review of Conflict of Interest and Other Related Concerns

Overview

The Internal Audit and Advisory Services (IAAS) branch of the Provincial Ministry of Finance has recently completed a review of some specific issues related to CBT Energy, following an inquiry related to potential conflict of interest between parties associated with that organization.

The purpose of the review, prompted by a July 2004 letter to the Ministry of Finance by Chilliwack-Kent MLA Barry Penner, was to look at whether there was any conflict of interest with CBT Energy's CEO and other contractors to CBT Energy. The review also looked at restructuring costs associated with a joint venture with Columbia Power Corporation (CPC).

We are very pleased to report that following its review, IAAS concluded that there was **no actual conflict of interest** and **no attempt by CBT Energy's CEO to further his personal interest over that of CBT Energy**. We are also pleased the report confirms that related actions taken by CBT Energy and its directors and officers, including its CEO met all applicable legal requirements.

Recommendations

IAAS's final report contains recommendations about ways CBT Energy might be able to improve some of its operational policies and practices.

In the spirit and context of ongoing and continuous improvement, CBT Energy will review each of the 20 recommendations, and respond, as appropriate, in a timely manner. Our focus for any improvements is to ensure that CBT Energy continues to have the best people, and the best management and organizational practices, to allow us to continue to effectively deliver benefits to the residents of the Columbia Basin region.

As such, we are pleased to provide a summary of IAAS's report for interested Basin residents to review. A copy of the full report is available upon request by e-mailing us at mmaloney@cbt.org

**Josh Smienk
Acting CEO, CBT
Chairman, CBT and CBT Energy**


[View the report](#)_(downloadable PDF)

Announcements

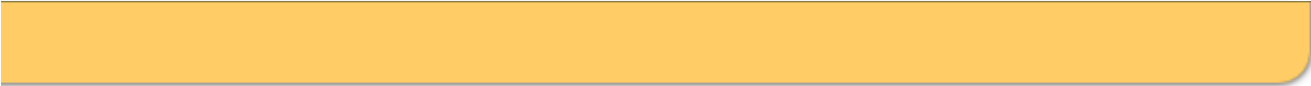
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**Revised Final Report on CBT Energy Inc. – Audit of
Conflict of Interest and Other Related Concerns**

**Internal Audit & Advisory Services
Ministry of Finance**

Date of fieldwork completion: September 2004

Executive Summary

On July 4, 2004, Paul Taylor, former Deputy Minister of Finance, received a letter from Barry Penner, MLA, raising concerns about a potential conflict of interest as a result of the relationship between Mr. Ken Epp, CEO and Director of CBT Energy Inc. (CBTE) and ZE PowerGroup Inc. (ZEPG). Specifically he was concerned about possible "related party transactions" totalling \$2 million during a three-year period from fiscal 2001/02 to 2003/04. These transactions between CBTE and ZEPG had been disclosed as related party transactions in the parent company's (Columbia Basin Trust) 2001/02 and 2002/03 annual reports but not disclosed in 2003/04.

The primary purpose of our audit was to assess: any conflict of interest by Mr. Epp in his capacity as CEO and Director of CBTE as a result of his business relationship with ZEPG; CBTE's contracting practices; and, restructuring costs of a joint venture.

CBTE has three contracts with ZEPG that are still in use today:

- **Consulting Services Agreement** – entered into in 1995 (by the parent company CBT before CBTE existed) for general consulting services related to the energy industry (total paid from April 1996 to June 2004 is \$1.887 million);
- **Market Monitoring Contract** – initiated in 2001 for on-going insight into energy market developments (total paid from October 2001 to June 2004 is \$██████); and
- **Software License Agreement** – ZE Market Analyzer software license purchased in 2001. The contract also allows for on-going maintenance (total paid from October 2001 to June 2004 is \$██████).

CBTE also contracted directly with Mr. Epp for his services as a CEO. The total paid from June 2001 to May 2004 is \$603,000.

Conflict of Interest

There is no indication of an actual conflict of interest by Mr. Epp as we saw no evidence to suggest that he used his position as CEO and Director of CBTE to further his own interests above those of the organization.

However, in our opinion there is both a perceived and potential conflict of interest. The perceived conflict of interest exists between Mr. Epp's role as a consultant to ZEPG and his CEO position at CBTE. There is a risk that he could be seen as benefiting personally

by influencing the award of work to ZEPG. Mr. Epp has a potential conflict of interest because his consulting services contract allows him to consult to CBTE in another capacity as well as to other parties, including ZEPG and CPC, on energy related issues. We have made recommendations where the risk of a conflict of interest would be eliminated or significantly minimized.

Disclosure of
Conflict of
Interest

CBTE has met the limited requirements of the *Business Corporations Act* for the disclosure of business relationships that may give rise to a conflict of interest. We believe, however, Mr. Epp as Director and CEO of CBTE, a public body, should be held to the higher standards that are expected of a person serving the public to avoid and manage the risk of conflict of interest. These standards are not legislated. We have applied these standards in our audit.

Financial
Statement
Disclosure

Based on legal advice and advice from their external auditors, CBT determined it was not necessary to disclose CBTE's related party transactions for fiscal 2003/04 in their consolidated financial statements. This was a change in disclosure from prior years. In our opinion, management should again discuss with their external auditor whether or not a related party disclosure is necessary due to the new information contained in our report.

Restructuring
Costs

Direction was given to consider the restructuring of CBTE and CPC. Costs incurred were processed through the Power Project Planning Joint Venture (PPPJV). We conclude that the restructuring costs incurred by CBTE and reimbursed by CPC, the Manager of the PPPJV, are outside the mandate of the PPPJV, and that these costs were paid without an approved budget.

We have recommended that the PPPJV Management Committee allow these costs because a separate budget approval was not initially required and a precedent had been established through paying prior costs. We have made recommendations to improve the financial management of these costs.

Contract
Awarding
Practices

CBTE, as a government corporation and a public body, is expected to comply with the spirit and intent of government's procurement policy. There were many weaknesses in awarding contracts. Controls were not in place to provide assurances of fairness and value for money for the contracts examined and it was difficult to determine whether these contracts were approved. With CBTE's low staffing levels and the perceived conflict of interest of the CEO, it is difficult to effectively manage contracts. We have made recommendations to improve the procurement process and contract management. Our audit did not include joint venture power project contracts.

We also noted, in our audit of contracts, that ZEPG fulfills an important role in CBTE by providing advice to the Board and management on strategic information. We believe by contracting out this service CBTE is vulnerable to a loss of protected information and have recommended that the CBTE Board tender the various assignments awarded to ZEPG or hire staff to fulfill this role.

Interventions

We also assessed whether the Vancouver Island Generation Project and Heritage Contract interventions undertaken by CBTE are within CBTE's mandate. We concluded that they were. These interventions were carried out under the direction of the CBTE Board and were conducted independent from CBTE's joint venture partner. CBTE and CPC should endeavour to reach an agreement when assessing whether to intervene to ensure intervention activities are cost-effective and necessary to meet respective mandates. Further, budgets were not approved by the CBTE Board and cost-benefit analyses were not available.

A full list of our recommendations is attached to this Executive Summary.



We would like to thank the staff and management of CBTE and CPC, and the CBTE Board, for their assistance and co-operation during our audit.

David J. Fairbotham
Executive Director
Internal Audit & Advisory Services

April 4, 2005

CBT Energy Inc. – Audit of Conflict of Interest and Other Related Concerns

Attachment to the Executive Summary – List of Recommendations

Note that the first three recommendations below are provided to help the Board protect itself from perceived and potential conflict of interest concerns. The Board can decide which of these three recommendation(s) to adopt depending upon the level of risk they want to accept.

1. The CBTE Board should consider disallowing the CEO to consult outside of his CEO role.
2. If the above recommendation is not accepted, we recommend that the CBTE Board disallow the CEO from consulting with organizations that consult to CBTE, its parent company or its joint venture partner.
3. If Mr. Epp consults outside the CEO role, then CBTE Board approval should be sought and documented for each contract he accepts outside his CEO role.
4. The Chair of CBTE should inform the PPPJV Management Committee of any potential or perceived conflict of interest and the steps that CBTE has taken to resolve it.
5. CBTE's Conflict of Interest Guidelines should be amended to reflect the standards outlined by the Board Resourcing and Development Office, Office of the Premier.
6. Management should again discuss with their external auditor whether or not a related party disclosure is necessary.
7. The Agreement should be amended to allow for the incurring of costs related to Project Castle. Both CBTE and CPC should agree on the content of these amendments.
8. CBTE management should obtain budget approval for restructuring costs from the CBTE Board and PPPJV Management Committee before undertaking projects on behalf of the PPPJV.
9. CBTE management should collaborate with the Joint Venture Manager to provide them with reasonable and sufficient information to conduct their due diligence on the costs.
10. The PPPJV Management Committee should allow payment of Project Castle costs, subject to completion of their due diligence.

11. Given the lack of resources, the CBTE Board should approve all contracts before they are entered into and this approval should be documented and included in the contract file.
12. CBTE management should review existing contracts to see whether it would be more cost effective to bring services in-house.
13. If, based on a cost benefit analysis, CBTE decides a contract is necessary then contracts should be tendered and competitively awarded depending upon the size of the contract.
14. If contracts meet the government conditions for direct awarding, CBTE staff should document the rationale in the contract file and the intent to contract should be posted on BC Bid.
15. CBTE management should ensure all contracts include clear deliverables.
16. CBTE management should follow the spirit and intent of government's procurement policy.
17. The CBTE Board should tender the various assignments given to ZEPG or hire staff.
18. CBTE and CPC should endeavour to reach agreement on interventions to ensure that intervention activities are cost effective and necessary to meet respective mandates.
19. CBTE management should complete a cost-benefit analysis before entering into an intervention.
20. The CBTE Board should approve a budget for each intervention they authorize and this approval should be documented in the CBTE Board minutes.