



4 December 2018

Geoff Williams
Chief Executive
Rotorua Lakes Council
Private Bag 3029
Rotorua Mail Centre
Rotorua 3046

Dear Geoff

REQUEST TO INQUIRE INTO MUDTOPIA

In August 2018, the Office of the Auditor General received a request to inquire into the Rotorua Lakes Council's (the Council) financial management, accountability, and governance of the Mudtopia event. Specifically, we were asked to carry out an independent and forensic audit of various transactions relating to Mudtopia. The correspondent also raised concerns about the procurement of some services for Mudtopia, suggesting that Councillor Maxwell might have had a conflict of interest.

We requested information from the Council on 4 September and 23 October 2018 to help us form our views on the matters raised.

After careful consideration, we have decided not to conduct a formal inquiry or forensic audit. Our reasons are detailed in this letter.

We have also set out our understanding of the facts based on information provided by the correspondent and the Council.

Decision to hold a mud festival

On 9 December 2015, the Council's Strategy Policy and Finance Committee¹ (SPF Committee) considered a business case on a proposed mud festival. The following recommendations were made by the SPF Committee:

- a. The Council own the event, with an appropriate structure and appointed directors to be determined by Council with the approval of the Mayor and chief executive.
- b. Upon securing sufficient Government investment, and subject to a robust due diligence process being completed by Council officers, the Committee resolves to approve an underwrite of up to \$500,000 annually to the established entity for the conduct of the mud festival until the event has reached a sustainable level.
- c. The Mayor and CEO be authorised to negotiate the value and term of the underwrite agreement.

These recommendations were adopted by the full Council on 17 December 2015, with the only amendment being that the portfolio lead, alongside the mayor and chief executive, was also authorised to negotiate the underwrite agreement.

¹ The purpose of the Strategy, Policy and Finance committee is to develop all strategic, policy and planning frameworks for approval by Council. Membership comprises the Mayor and all councillors.

Central government funding

Following consultation with stakeholders including the tourism sector, iwi, the Bay of Plenty Regional Council and Council operational staff, a comprehensive business plan was developed. New Zealand Major Events (part of the Ministry of Business, Innovation and Employment – MBIE) then agreed to fund Mudtopia up to \$1.5 million over five years to support its establishment. The Council committed to owning and underwriting the event.

Governance of Mudtopia

Following the Council's 17 December 2015 decision, a specialist event management company was appointed to run the event, and an external advisory board was appointed to provide governance oversight of the event. That board included Council staff, representatives from the event management company, various other stakeholders, and Professor Jeong (founder of the South Korean Boryeong mud festival). The board did not have financial delegations. The Council told us that the establishment of "an advisory board was a requirement of MBIE as its accepted vehicle for event governance."

The Council also told us that it considered using other structures to run Mudtopia, including a limited liability company with not for profit status, charitable trust, and council-controlled organisations. We are not aware of when these options were considered.

Regardless of the structure selected, the practical reality is the Council would probably still have to cover any losses beyond the \$500,000 underwrite.

Decision whether to continue to support Mudtopia

About four months before the event, concerns were raised publicly about whether purchasing South Korean cosmetic mud to use at the event, presented a biosecurity risk, given the country's history with foot and mouth disease. Following this negative publicity, Council staff asked the Council's Operations and Monitoring Committee² at the Committee's 3 August 2017 meeting if it wished to continue supporting the event.

The Committee also discussed the possible risks from this publicity to the event's financial bottom line. At the time, the cost to the Council of pulling out was advised to be around \$900,000 with the commitments made to that date. The pessimistic forecast was that the net loss from Mudtopia, excluding capital expenditure, would be \$575,871. This was less than writing-off all of the expenses incurred to date.

The Committee was also told that "Council committed to what was described as an 'underwrite' of up to \$500,000, though the reality is that this is not technically an underwrite given it is the Council owning the event and any financial risks around it." The Committee confirmed its support for the Mudtopia event.

On 7 August 2017, following a meeting with the advisory board and delivery partners, the decision was made to proceed with Mudtopia without importing cosmetic mud from South Korea. The event was held 1-3 December 2017.

² The purpose of the Operations and Monitoring committee is to ensure consolidated and complete reporting and monitoring of all financial and non-financial information and performance measures against the Annual Plan, Long-term Plan and strategy goal/priorities. Membership comprises the Mayor and all councillors.

Event operated at a loss

Mudtopia operated at a loss of \$570,387. It incurred a further \$170,000 of capital expenses on facility upgrades and the purchase of inflatable event equipment. Therefore, the total cost to the Council was \$740,387.

The financial information publicly released by the Council shows:

	<i>Business plan 2015</i>	<i>Revised Budget 2017</i>	<i>Actual 2017</i>
Revenue			
Funding partners including New Zealand Major Events and NZ Community Trust	\$1,288,500	\$1,050,000	\$800,000
Sponsorship revenue	\$540,000	\$240,000	\$35,000
Ticketing and food and beverage revenue	\$530,977	\$581,477	\$73,900
Total festival revenue	\$2,359,477	\$1,871,477	\$908,900
Expenses			
Festival management	\$626,000	\$501,000	\$523,491
Other expenses	\$1,608,898	\$1,177,273	\$955,796
Contingency 5%	\$111,745	\$83,914	-
Total operating expenditure	\$2,346,643	\$1,762,187	\$1,430,790
Net profit/loss	\$12,834	\$109,290	-\$570,387
Capital expenditure	?	?	-\$170,000
Total cost to the Council	?	?	-\$740,387

Future of Mudtopia

In May 2018, the Council met and agreed not to own or run Mudtopia in the future, or provide direct financial assistance to the event.

Our conclusions

Governance arrangements

Although the resolution passed at the 17 December 2015 Council meeting was broad, the meeting minutes indicate that:

- the Council intended for an entity other than the Council to run Mudtopia; and
- the structure of that entity, and who would govern it, would be referred back to the full Council for decision.

We have not seen evidence that the entity proposed to run the event, and governance arrangements, was referred back to the Council for a decision.

From the documents we were provided with, it appears that the Council was more involved with running the event than originally intended. The Council's oversight was provided by an advisory board established by the Council's Chief Operating Officer, with an event management company called Event Engine contracted to run the event. The Chief Operating Officer was responsible for appointing board members. This board provided guidance and support on the delivery of the event. The board reported to the Chief Operating Officer, and the Chief Executive or his representative, attended the board's meetings.

The fact that the company had been appointed, and that an advisory board had been created and members appointed, was reported to the Council's Operations and Monitoring Committee in 2016.

Expenditure

It is clear from the 17 December 2015 resolution that the Council intended to cap its overall financial exposure on Mudtopia at a maximum of \$500,000. When we contacted the Council about this matter, Council staff confirmed that no formal resolution was passed that authorised the additional financial exposure. Instead, the Council advised us that its Operations and Monitoring Committee was told at its 3 August 2017 meeting about a higher level of financial risk associated with Mudtopia and, more specifically, a level of uncertainty about the likely revenue level. The Operations and Monitoring Committee resolved to proceed with the event on that basis.

Councillor Maxwell - alleged conflict of interest

The correspondent also alleges a financial conflict of interest on the part of Councillor Maxwell, and has requested a forensic audit into the matter. The allegation is made on the basis that Councillor Maxwell's children own two companies that carried out work for the Mudtopia event, and that he did not excuse himself from discussions and decisions about Mudtopia.

Section 6 of the Local Authorities' (Members' Interests) Act 1968 (the Act) provides that members of a local authority are not allowed to participate in discussion or voting on any matter before the local authority in which they have a direct or indirect pecuniary (financial) interest, other than an interest in common with the public. An indirect financial interest can arise where a councillor and/or their partner has a shareholding in a company which has a financial interest in a matter.

The Act does not define a financial interest. The test the Office uses is:

...whether, if the matter were dealt with in a particular way, discussing or voting on that matter could reasonably give rise to an expectation of a gain or loss of money for the member concerned.

Our search of the Companies Office website shows that Councillor Maxwell is not a shareholder in either company. From the information provided by the Council, it does not appear that Councillor Maxwell, or a partner of Councillor Maxwell, had a financial interest in matters relating to the Mudtopia festival. On this basis, it does not appear that Councillor Maxwell had a financial interest in matters related to Mudtopia.

Conclusion

After examining documents provided by the correspondent and Council, and talking to Council staff, we will not be carrying out a formal inquiry or forensic audit into the matters raised.

The expenses incurred by the Council from the Mudtopia event are already in the public arena for scrutiny. The public has the ability to question the Council about individual expenses and hold the Council accountable for those.

While we accept that the Operations and Monitoring Committee agreed in August 2017 to continue supporting the event, even with an increased financial risk profile, on balance we are of the view that as Council (and not a committee of Council) had capped the financial exposure to \$500,000 that there should have been another Council resolution expressly permitting the Council to accept the additional financial exposure.

Similarly, we believe that the decision on the final form of governance arrangements should have been approved by Council, although we acknowledge that the December 2015 resolution on this matter was ambiguously worded.

Our expectation is that public entities need full and proper records of their work that show what decisions were made, how they made them, and the basis on which they were made.

I have provided a copy of this letter to the correspondent.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'K Aitken'.

Kristin Aitken
Sector Manager, Local Government Group