
MEMORIAL FOR THE OPINION OF COUNSEL

for

Shetland Islands Council and the Shetland Charitable Trust

Re: Constitution of the Shetland Charitable Trust

Opinion *intus*

2011

Dundas and Wilson CS LLP

Ref: JW/CB/STE305.0001

Turcan Connell, Solicitors and Asset Managers

Ref: KJP/SAM/S0608.003

MEMORIAL TO COUNSEL

JOINT INSTRUCTIONS FROM SIC AND SCT

1. INTRODUCTION

- 1.1 The Shetland Islands Council ("SIC") and The Shetland Charitable Trust ("SCT") jointly seek the Opinion of Counsel.
- 1.2 SIC was constituted under Section 2 of the Local Government etc (Scotland) Act 1994. It is a major employer in Shetland with around 3,200 employees. The Council consists of 22 elected members serving a population of approximately 22,000.
- 1.3 SCT was established by SIC by Deed of Trust. SCT is a registered Scottish Charity (Scottish Charity Number: SC027025) which currently has 23 trustees.
- 1.4 At a meeting of the Trustees of SCT at Islesburgh Community Centre, Lerwick on 8 September 2010 (Minute enclosed as document 6) the Trustees passed a motion:

"That the SCT ask Mr A Buchan, Chief Executive of Shetland Islands Council, and Ms A Black, General Manager of the SCT, to jointly identify the most relevant senior member of the Scottish legal system to determine if the constitution of the SCT requires to be changed in light of current OSCR opinion and Trust regulations, and to make recommendations as are necessary for the future governance of the Trust."

2. BACKGROUND TO THE SCT

- 2.1 The Charitable Trust was first established as the Shetland Islands Council Charitable Trust in 1976. The reasons for the establishment of the Trust are set out in 4.3.3 of Dundas & Wilson's report, *Shetland's Oil Monies and their Governance*, 7 March 2008 enclosed as document 1.
- 2.2 The present Trust was established by SIC by Deed of Trust on 10 September 1997 to replace the previous trust and was re-named SCT. A copy of the Deed of Trust is enclosed as document 2.
- 2.3 The Deed of Trust provides for the members of SIC, the Headmaster of the Anderson High School and Lord Lieutenant of Shetland being trustees of SCT ex officio.

2.4 There are currently 23 trustees as one member of SIC decided to stand down as a trustee due to a declared conflict of interest.

2.5 Historically the Chief Executive of SIC was also Chief Executive of SCT. However in 2002 the SCT accepted recommendations from the then SIC and SCT Chief Executive to distance the relationship between the two organisations. The SIC Chief Executive no longer maintains the same role for the SCT.

3. CURRENT ROLE OF SCT

- 3.1 SCT is managed and administered by a team of nine directly employed staff. The General Manager's role is to ensure that SCT carries out its activities in furtherance of its purposes, represents value for money, and complements the needs and aspirations of its primary beneficiaries (the Shetland community).
- 3.2 SCT is an independent organisation, free to carry out its charitable activities either alone or in partnership with any other party it so wishes. SCT endeavours to 'top up' public services, in line with the community's needs, which are complementary to those provided by national and local taxation. SCT wishes to ensure that the charitable activities it carries out are appropriate and complementary to those activities carried out by SIC. This is done through dialogue with senior managers in SIC.
- 3.3 SCT seeks advice from the senior managers in the SIC as to what activities it might carry out for the public benefit of the inhabitants of Shetland. These managers are referred to as Service Co-ordinators. This ensures that both SIC and SCT follow the same strategic direction and avoids any duplication of effort in assessing if projects or activities are suitable for funding. The Service Co-ordinators provide professional advice, with the final decision to support a project or activity, lying with the Trustees of SCT.
- 3.4 SCT provides grant assistance to a number of organisations providing a range of social, leisure, cultural, heritage and environmental activities. These include:
- Citizens Advice Bureau;
 - COPE Limited;
 - Disability Shetland;
 - Festivals: Folk Festival;

- Shetland Amenity Trust; and
- Shetland Recreational Trust.

3.5 SCT also supports a range of charitable projects and schemes such as:

- Christmas Grant to Pensioners and Disabled Persons;
- Community Support Grant Aid Scheme; and
- Bus services Elderly and Disabled.

3.6 SCT invests in a range of community facilities and equipment and has in place a planned maintenance programme. This ensures that buildings, equipment and other assets are well maintained and in good condition.

3.7 SCT also makes a number of one-off contributions to individuals and organisations.

3.8 A copy of the draft Report and Accounts to 31st March 2010 is enclosed as document 7.

4. ISSUES

4.1 In recent years, a number of issues have arisen. These can be conveniently considered under various headings:

- (a) Accountability;
- (b) Independence; and
- (c) Charitable status.

4.2 Accountability

4.2.1 There is a desire to ensure accountability of the SCT to the Shetland community.

4.2.2 At inception of the present Trust in 1997, the view was taken that accountability was best achieved by ensuring that all the Councillors were ex-officio Trustees.

4.2.3 Councillors must comply with the obligations imposed on Councillors under the Code of Conduct for Councillors issued by Scottish Ministers under the Ethical Standards in Public Life etc (Scotland) Act 2000¹.

4.2.4 Councillors are elected and answerable to the Shetland community in that capacity.

4.3 Independence

4.3.1 As explained above, while accountability may be best achieved by ensuring that all the Councillors are ex-officio Trustees, on the other hand this does call into question whether there is a lack of independence of the Trustees of SCT from SIC.

4.3.2 In a small community such as Shetland, the number of people with the time, desire and skills to serve on a number of public bodies is limited. There is also a concern that the experience and expertise that is available to the community is not spread too thinly in a desire to ensure independence.

4.4 Charitable status

4.4.1 SCT is regulated by the Office of the Scottish Charity Regulator ("OSCR") under the provisions of the Charities and Trustee Investment (Scotland) Act 2005 ("the Act").

4.4.2 The Act establishes a charity test. The charity test is satisfied if the charity meets one of the charitable purposes² and provides a public benefit. A body does not meet the charity test if its constitution allows it to distribute or otherwise apply any of its property (on being wound up or at any other time) for a purpose which is not a charitable purpose³.

4.4.3 SCT appears to pass these tests and is indeed registered with OSCR.

4.4.4 As the OSCR guidance "Meeting the Charity Test" notes, there is no fixed stipulation in the legislation that charities' constitutions must be independent of any third party other than Scottish Ministers. However, the Act is explicit about the duties of charity trustees and the need to guard against conflicts of

¹ Section 1. The Act draws upon the basic governance principles of: openness; accountability; and transparency. Elected members should comply with the model code of conduct.

² Section 7(2).

³ Section 7(4).

interests. The guidance goes on to say that trustees therefore need to be alert to the issues of effective operational independence although it is not part of the charity test. The trustees are bound by the general duties in section 66 of the Act:

'66 Charity trustees: general duties

- (1) *A charity trustee must, in exercising functions in that capacity, act in the interests of the charity and must, in particular –*
 - (a) *seek, in good faith, to ensure that the charity acts in a manner which is consistent with its purposes,*
 - (b) *act with the care and diligence that it is reasonable to expect of a person who is managing the affairs of another person, and*
 - (c) *in circumstances capable of giving rise to a conflict of interest between the charity and any person responsible for the appointment of the charity trustee –*
 - (i) *put the interests of the charity before those of the other person, or*
 - (ii) *where any other duty prevents the charity trustee from doing so, disclose the conflicting interest to the charity and refrain from participating in any deliberation or decision of the other charity trustees with respect to the matter in question.*
 - (iii) *The charity trustees of a charity must ensure that the charity complies with any direction, requirement, notice or duty imposed on it by virtue of this Act.*
 - (iv) *Subsections (1) and (2) are without prejudice to any other duty imposed by enactment or otherwise on a charity trustee in relation to the exercise of functions in that capacity.*
 - (v) *Any breach of the duty under subsection (1) or (2) is to be treated as being misconduct in the administration of the charity.*
 - (vi) *All charity trustees must take such steps as are reasonably practicable for the purposes of ensuring –*

- (d) *that any breach of a duty under subsection (1) or (2) is corrected by the trustees concerned and not repeated, and*
- (e) *that any trustee who has been in serious or persistent breach of either or both of those duties is removed as a trustee.'*

4.4.5 In the guidance for charity trustees, OSCR makes it clear that charity trustees are expected to put the interests of the charity before their own interests or those of any other person or organisation. In particular, it says that where a charity trustee is faced with a conflict of interest between the interests of the charity and those of a person or organisation responsible for their appointment as a charity trustee, the interests of the charity must come first. The charity trustee must act in the interests of the charity to which they have been appointed, not in the interests of the person or organisation which appointed them, for example, a Local Authority or another charity. The guidance goes on to note that if in relation to a particular issue the conflict of interest is irreconcilable then the charity trustee in question must make this known to the other charity trustees and not take part in any discussion or decision making on the issue.

4.4.6 In summary, the arrangements to manage potential conflicts of interests will require to satisfy OSCR as well as stand scrutiny under Local Authority legislation and guidance.

5. OSCR

5.1 SCT had a meeting with OSCR on 31 October 2008. The Minutes of that Meeting are enclosed (document 4). At paragraph 2.10 it is recorded that

"with the current structure and arrangements, it is difficult to evidence independence and compliance with section 66 of the 2005 Act."

5.2 SCT have a conflict of interest policy which is enclosed as document 3 (pages 4-8).

5.3 Following this meeting SCT established a Governance Review Group. After several meetings and a period of public consultation, its findings and recommendations were presented to the Trustees of SCT on 11 February 2010. At that meeting, the Trustees decided to delay a decision on the future governance of SCT until after the next local elections in 2012, but discussions should continue with OSCR and the public of Shetland to come to an acceptable solution.

- 5.4 This outcome was discussed with OSCR at meetings on 23 and 24 June 2010. OCSR wrote to SCT following these meetings, on 9 July 2010 (copy enclosed as document 5). OSCR commented:

"We acknowledge that the policy exists but confirm it is the practical application of the policy that is of particular interest to OSCR, given the current governance arrangements of the charity"

"There is in our view a high systematic risk of irreconcilable conflict where (effectively all) councillors are SCT trustees."

Further:

"It is not solely about the way in which the decision is arrived at, but also about how the decision making process and practice appears to others outwith the trustee body."

OSCR add:

"Given there has been no change to the governance arrangements within SCT, we consider there is a real risk both of systematic and specific conflict which will continue to impact on effective compliance with your own policy and the trustees statutory duties, on so on effective and appropriate governance of the Trust..."

With immediate effect, using our powers under section 28 of the Charities and Trustee Investment (Scotland) Act 2005... OSCR will put the following requirements in place: [listed]...

If, for example, OSCR were to identify practices or actions that are inappropriate, we will consider more substantive action including using our powers under section 31 of the Charities and Trustee Investment (Scotland) Act 2005..."

- 5.5 OSCR conclude that "we continue to encourage you to move forward to adopt different, less high risk and more appropriate governance arrangements."

6. QUESTION

- 6.1 Does the constitution of SCT require to be changed to comply with current law and practice?

- 6.2 If the answer to the first question is yes what changes does senior counsel consider would be necessary to meet the minimum requirements of achieving compliance with current law and practice?

APPENDIX

Documents

1. 'Shetland's Oil Monies and Their Governance', Dundas & Wilson CS LLP, 7 March 2008
2. Deed of Trust by Shetland Islands Council dated 10 September 1997
3. SCT Administrative Regulations adopted by Trustees on 18 March 2010
4. OSCR File Note of meeting with SCT on 31 October 2008
5. Letter from OSCR to Bill Manson dated 9 July 2010
6. Minute of Meeting of SCT of 8 September 2010
7. Draft Report and Accounts to 31st March, 2010

OPINION

Introduction

1. I refer to the Memorial to Counsel sent to me on 7th December 2010 containing joint instructions on behalf of Shetland Islands Council ("the Council") and the Shetland Charitable Trust ("the Trust"). I refer also to the consultations which were held on 16th December 2010, and on 31st January and 24th March 2011.
2. The joint instructions concern the constitution of the Trust and whether it requires to be changed in light of considerations arising from the enactment of the Charities and Trustee Investments (Scotland) Act 2005 ("the 2005 Act"), and if so, what changes ought to be made. At a meeting held on 8th September 2010, the Trust resolved to ask the Chief Executive of the Council and the General Manager of the Trust jointly to seek an opinion on the matters referred to in the joint instructions.
3. In order to give my opinion, I first set out the factual and legal background before addressing the two questions specified in the Memorial.

The Council

4. The Council are a local authority constituted in accordance with the provisions of the Local Government (Scotland) Act 1973 as amended ("the 1973 Act") and of the Local Government etc (Scotland) Act 1994 ("the 1994 Act"). By virtue of each of these Acts, the Council are the statutory successors of previous local

authorities having jurisdiction over the islands of Shetland, in particular the County Council of the County of Zetland ("Zetland County Council").

5. As a local authority, the Council are constituted by their convener and councillors (or "members") in accordance with section 2(1) of the 1994 Act. The Council have a range of statutory powers and duties, including powers and duties many of which relate to the provision of services and facilities to the inhabitants of their area. Examples of these powers and duties which may be said to be relevant for the purposes of this Opinion include:

- (a) The duty as an education authority "to secure that there is made for their area adequate and efficient provision of school education and further education": Education (Scotland) Act 1980, section 1(1);
- (b) The duty to promote social welfare and to provide and secure facilities for the promotion of social welfare, including the provision of residential and other establishments: Social Work (Scotland) Act 1968, sections 1(1) and 4, and Part II in particular.
- (c) The duty to "ensure that there is adequate provision of facilities for the inhabitants of their area for recreational, sporting, cultural and social activities" and the powers to provide, or to incur expense in the provision of, facilities for those purposes: Local Government and Planning (Scotland) Act 1982, section 14(1), 15 and 16.

The first two are examples of underlying powers and duties and in each case they are supplemented by a range of more detailed powers and duties in relation to the functions in question.

6. There are also certain specific powers and duties which may be noted in the context of the activities of the Trust. Section 69 of the 1973 Act, which is entitled "Subsidiary powers of local authorities", provides in part that:

- "(1) Without prejudice to any powers exercisable apart from this section but subject to the provisions of this Act and any other enactment passed before or after this Act, a local authority shall have power to do any thing (whether or not involving the

expenditure, borrowing or lending of money or the acquisition or disposal of any property or rights) which is calculated to facilitate, or is conducive or incidental to, the discharge of any of their functions.

“(2) ...”

Section 74 of the 1973 Act is entitled “Disposal of land” and provides in part that:

- “(1) Subject to... subsection (2) below, a local authority may dispose of land held by them in any manner they wish.
- “(2) Except in accordance with regulations under subsection (2C) below, a local authority shall not dispose of land under subsection (1) above for a consideration less than the best that can reasonably be obtained.

“(2A)”

7. Subsections (2A) and following of section 74 were inserted into the 1973 Act by amendments made by the Local Government in Scotland Act 2003 (“the 2003 Act”). Section 1 of the 2003 Act is entitled “Local authorities’ duty to secure best value” and it provides in part that:

- “(1) It is the duty of a local authority to make arrangements which secure best value.
- “(2) Best value is continuous improvement in the performance of the authority's functions.
- “(3) In securing best value, the local authority shall maintain an appropriate balance among –
 - (a) the quality of its performance of its functions;
 - (b) the cost to the authority of that performance; and
 - (c) the cost to persons of any service provided by it for them on a wholly or partly rechargeable basis.
- “(4) In maintaining that balance, the local authority shall have regard to –
 - (a) efficiency;
 - (b) effectiveness;
 - (c) economy; and
 - (d) the need to meet the equal opportunity requirements.

“(5)”

8. Section 20 of the 2003 Act provides in part that:

- “(1) A local authority has power to do anything which it considers is likely to promote or improve the well-being of –
 - (a) its area and persons within that area; or
 - (b) either of those.
- “(2) The power under subsection (1) above includes power to –
 - (a) incur expenditure,
 - (b) give financial assistance to any person,
 - (c) enter into arrangements or agreements with any person,
 - (d) co-operate with, or facilitate or co-ordinate the activities of, any person,
 - (e) exercise on behalf of any person any functions of that person, and
 - (f) provide staff, goods, materials, facilities, services or property to any person.
- “(3) The power under subsection (1) above may be exercised in relation to, or for the benefit of—
 - (a) the whole or any part of the area of the local authority;
 - (b) all or some of the persons within that area.
- “(4) The power under subsection (1) above includes power to do anything –
 - (a) in relation to, or for the benefit of, any persons or place outwith the area of the local authority; or
 - (b) in any such place,if the authority considers that doing so is likely to achieve the purpose set out in that subsection.

“(5) ...”

9. The powers just referred to are powers granted to every local authority. In the case of the Council, they have additional powers which were granted by the Zetland County Council Act 1974 (“the 1974 Act”) to Zetland County Council, referred to in the 1974 Act as “the Council”. The general duties and powers of the Council are provided in Part II of the 1974 Act which includes section 5(1) and (2) which imposes duties upon the Council in connection with “the provision,

maintenance, operation and improvement of port and harbour services and facilities in... a harbour area", and to take action "for the proper development or operation of the harbour undertaking." The expression "harbour undertaking" is defined in section 3(1) as meaning "the harbour undertaking for the time being of the Council authorised by this Act". Section 67 provides in part that:

"(1) If in respect of any financial year the moneys received by the Council on account of the revenue of the harbour undertaking exceed the moneys expended or applied by the Council in respect thereof, the Council may in respect of that year apply out of the county fund and carry to the credit of a reserve fund in respect of the harbour undertaking such a sum as they consider reasonable not exceeding the amount of such excess.

"(2) ...

"(3) Any reserve fund provided under this section may be applied –
(a) ...
(e) for any other purpose which in the opinion of the Council is solely in the interests of the county or its inhabitants."

10. These provisions demonstrate that there is a range of powers which the Council may exercise to provide services and facilities, to dispose of property and to expend funds for the benefit of their area and the inhabitants of their area. The exercise of any of these powers will involve an exercise of discretion by the members of the Council as well as compliance with the statutory limitations or restrictions which are applicable to the particular exercise of the power in question.

The Trust

11. The original charitable trust was established in 1976 as the Shetland Islands Council Charitable Trust. The reasons for the establishment of such a trust arose out of the negotiation of a Disturbance Agreement by Zetland County Council with the oil industry at the time of the passing of the 1974 Act. Payments were to be received as a result of oil related development which were known as "Disturbance Payments". Zetland County Council (or their statutory successor as

local authority in 1976) determined to allocate such funds to the Shetland Islands Council Charitable Trust. The reasons for this were recorded in 1978 as having been concerns at the time about the consequences of such funds being received and held by the Council's predecessor, including the possible consequence of the nationalisation of port facilities which could lead to the loss by the Council's predecessor of the ability to distribute funds from the Reserve Fund held by the Council's predecessor for local purposes using the power given by section 67(3)(e) of the 1974 Act. The Disturbance Agreement ended on 1st September 2000.

12. The Trust was established by a Deed of Trust dated 10th September 1997 ("the Trust Deed") and became known as the Shetland Charitable Trust in 2003. The Trust Deed was granted by the Council in favour of all of the elected members (or councillors) of the Council, the Headmaster of Anderson High School, Lerwick and the Lord Lieutenant of Shetland, all as Trustees *ex officio* (hereinafter the "Trustees"). The Council currently has twenty two elected members, one of whom has resigned as a Trustee, and there are presently twenty three Trustees in total.
13. The sum of one pound was assigned to the Trustees in the Trust Deed and it was stated:

"And we declare that the said sum of One Pound Sterling and any other property heritable or moveable real or personal which may hereafter be made over by us or by others to the Trustees for the purpose of the trust hereby created and the investments and property representing the same from time to time all hereinafter referred to as "the Trust Fund" and shall be held in trust for the purposes hereinafter written..."

Within those purposes, the "Objects of Trust" were stated as follows:

"(SECOND) The Trustees shall hold the Trust Fund at their sole discretion to make grants or loans with or without interest out of the income or capital of the Trust Fund for any purposes which in the opinion of the Trustees are solely in the interests of the area administered by the local or other governmental authority for the time being of the Shetland Islands or of the inhabitants of the said area (hereinafter referred to as "the

community”) and provided that any such grant or loan is for charitable purposes: Declaring that without prejudice to the generality of the foregoing such grants or loans may be made towards all or any of the following purposes:-

- (a) In carrying out developments on or in connection with the said area calculated to promote the welfare of the community;
- (b) In encouraging and assisting the holding of meetings of members of the community for purposes of recreation, instruction or education;
- (c) In improving, maintaining and encouraging the improvement and maintenance of means of communication in the said area, and in particular by (i) building or improving or maintaining ports, harbours, piers, roads, bridges or aerodromes; (ii) hiring or chartering or purchasing and operating any boat, ship, vessel, aeroplane or any kind of land, sea or air vehicle; (iii) ...;
- (d) In promoting directly or indirectly the development of any industry or industries among the community for its benefit in any manner in which the Trustees consider desirable;
- (e) In promoting directly or indirectly the development of agriculture among the community for its benefit;
- (f) In encouraging the education of the community by such means as the Trustees may consider desirable;
- (g) In improving the medical service to the community by such means as the Trustees may consider desirable;
- (h) In the preservation and improvement of the said area in a manner which in the opinion of the Trustees is most conducive to promoting the said area for the benefit of the community and of the Nation;
- (i) In the founding, endowing and equipping of schools, colleges, institutions, laboratories, experimental stations, libraries, sports centres, welfare centres or technical education centres for the community;
- (j) In encouraging the study and practice of any useful branch of human knowledge by the provision of buildings, equipment or otherwise as the Trustees may consider desirable;
- (k) In the doing of all such other things as are incidental to any of the foregoing purposes:...”.

In my opinion, these Objects of Trust demonstrate that the Trust is a public trust although that is not critical for the purposes of the questions before me. The fact that the Objects of Trust may be exercised only for charitable purposes is emphasised by reference to the scope of any Supplementary Deed in purpose (FOURTH) and by the limitation stated there upon the exercise of the specific powers set out in the Schedule of Powers which is annexed to the Trust Deed.

The activities of the Trust

14. The Trust has been administered as a charitable trust. Following the passing of the 2005 Act, the Office of the Scottish Charities Regulator ("OSCR") was established in accordance with section 1(1) of the 2005 Act. The Trust has been registered as a charity by OSCR (with registered number SC027025). OSCR has a duty to keep a public register in accordance with sections 1(5) and 3 of those bodies which meet the "charity test" set out in section 7(2).
15. The funds held by the original Shetland Islands Council Charitable Trust were transferred to the Trust and have been administered as part of the Trust Fund. The Trust also received the Disturbance Payments until that source of income ended in August 2000. The income of the Trust since then has been primarily from investments and rental income. The value of the Trust Fund in March 2008 was of the order of £230m although it has fluctuated upwards and downwards, both before and since, in light of prevailing financial circumstances. In March 2010, the value was £210m.
16. The Trust has its own staff. I am instructed that the Trust "endeavours to 'top up' public services, in line with the community's needs, which are complementary to those provided by national and local taxation." The Trust seeks to ensure that both the Council and the Trust "follow the same strategic direction and avoids any duplication of effort in assessing if projects or activities are suitable for funding." The Trust seeks advice and recommendations from senior managers of the Council on funding issues in order to avoid duplication, for example from social workers of the Council. Grant assistance is provided to organisations providing a range of social, leisure, cultural, heritage and environmental activities. The Trust provides support to charitable projects involving the disabled, community support and bus services. The Trust has invested in and maintains community facilities and equipment.

17. The Trust receives rental income from the leasing of properties which are owned by Shetland Leasing and Property Limited ("SLAP") which is a wholly owned subsidiary of the Trust. There are thirty five leases of property of which one-fifth are leases to the Council. All of the rents are calculated to deliver a commercial return, and of the total rental income the proportion received from the Council is about forty per cent. The principal properties are an airport, an engineering base and two colleges, the latter two of which are tenanted by the Council. SLAP also leases a small aeroplane to the Council.
18. The Trust provides buildings under a partnership agreement with the Council for the delivery of care in rural areas and the care is provided in these buildings by the Council. (Within Lerwick, both the buildings and the delivery of care are provided by the Council.) The Trust supplies heat to about one thousand domestic properties through another wholly owned subsidiary, Shetland Heat Energy and Power Limited.
19. The Trust receives rental income from the lease to the Council of the Sullom Voe oil terminal, which in turn is sub-let to the oil industry. The sale of Sullom Voe by the Council occurred in 1997 and it was sold to the former Shetland Islands Council Charitable Trust.
20. The Council sold to the Trust in 2007 a 90% interest in Viking Energy Limited ("VEL") which company subsequently entered into a partnership agreement with Scottish and Southern Energy to develop a windfarm in central Mainland. The principal reason for the sale by the Council of their interest in VEL to the Trust was the then prohibition on local authorities selling electricity generated by wind power. The shares in VEL were sold at what was considered to be fair value at the time.

21. The Trust and SLAP receive services from the Council under Service Level Agreements for purposes such as banking, payroll management and administration.
22. The Trust has prepared Administrative Regulations which were adopted on 18th March 2010 ("the Administrative Regulations"). These address the constitution, management and conduct of the business of the Trust, as well as the arrangements for the Trustees. Paragraphs 6.1 to 6.5 refer to circumstances which may give rise to a conflict of interest on the part of the Trustees and the steps to be taken in such circumstances.
23. It should be noted that in addition to the circumstances of the Trust, I have also been provided with information concerning other charitable trusts which have been set up by the Council, namely the Shetland Recreational Trust, the Shetland Amenity Trust and the Shetland Arts Development Agency. In each case, these have been registered by OSCR as charitable trusts. Although the Shetland Recreational Trust was established with trustees who were members and officials of the Council, all of the elected members have recently declined to act as trustees and arrangements are being made to identify trustees by a process of application from members of the public. In the case of the other two of these trusts, neither has a substantial number of members of the Council as trustees.

The issue

24. The issue which arises is the result of the fact that almost all of the Trustees are simultaneously councillors of the Council. This issue has three aspects as set out in the Memorial. The first is the accountability of the Trust to the community of Shetland, the second is the independence of the Trustees, and the third is the potential effect on charitable status following the passing of the 2005 Act.
25. OSCR has the function of monitoring charities in accordance with section 1(5)(c) of the 2005 Act, and the Trust requires to satisfy OSCR that it can continue to

meet the charity test, and that the Trustees are able to fulfil the duties of charitable trustees, all as set out in the 2005 Act and in guidance issued by OSCR. There have been meetings between the Trust and OSCR, and in a letter to the Trustees dated 9th July 2010, OSCR stated:

"The charity's conflict of interest policy was the subject of discussion at our meetings... We acknowledge that the policy exists but confirm it is the practical application of the policy that is of particular interest to OSCR, given the current governance arrangements of the charity."

"Given there has been no change to the governance arrangements within [the Trust], we consider there is a real risk both of systemic and specific conflict which will continue to impact on effective compliance with your own policy and the trustees statutory duties, and so on effective and appropriate governance of the Trust."

In the same letter, OSCR imposed immediate requirements using its power under section 28 of the 2005 Act to make a direction following inquiries which related to the sending of agendas and minutes to OSCR and the management of conflicts of interest. OSCR also stated that after monitoring it might use its powers under section 31 "in relation to both the charity trustees individually and the charity as a whole."

26. Section 31 provides in part that:

- "(1) Subsections (4)... apply where it appears to OSCR, as a result of inquiries under section 28 –
 - (a) that there has been misconduct in the administration of –
 - (i) a charity...
- "(2) ...
- "(4) OSCR may, by notice, suspend any person concerned in the management or control of the charity or body who appears to it to–
 - (a) have been responsible for or privy to the misconduct,
 - (b) have contributed to, or facilitated, the misconduct, or
 - (c) be unable or unfit to perform that person's functions in relation to the property of the charity or body.
- "(5) OSCR may direct –
 - (a) the body representing itself as a charity,
 - (b) ...

to stop doing so.

“(6) ...”

OSCR also has the power following inquiries under section 28 to remove a charity from the register in terms of section 30(1)(b).

27. It is therefore apparent that OSCR is giving serious consideration to whether or not the Trust may lawfully continue as a charitable trust. Having said that, the letter from OSCR also stated that “if there were to be positive changes to the governance arrangements, we would review our monitoring.”
28. The result is that the Trust wishes to consider its governance arrangements, in particular the composition of the Trustees. The focus of this consideration is clearly the position which has been stated by OSCR but it appears to me that if that is resolved the aspects of accountability and independence will also be addressed.

The legislation and guidance

29. Section 66 of the 2005 Act, which is entitled “Charity trustees: general duties”, provides in part that:
 - “(1) A charity trustee must, in exercising functions in that capacity, act in the interests of the charity and must, in particular—
 - (a) seek, in good faith, to ensure that the charity acts in a manner which is consistent with its purposes,
 - (b) act with the care and diligence that it is reasonable to expect of a person who is managing the affairs of another person, and
 - (c) in circumstances capable of giving rise to a conflict of interest between the charity and any person responsible for the appointment of the charity trustee —
 - (i) put the interests of the charity before those of the other person, or
 - (ii) where any other duty prevents the charity trustee from doing so, disclose the conflicting interest to the charity and refrain from participating in any deliberation or decision of the other charity trustees with respect to the

matter in question.

- “(2) The charity trustees of a charity must ensure that the charity complies with any direction, requirement, notice or duty imposed on it by virtue of this Act.
- “(3) Subsections (1) and (2) are without prejudice to any other duty imposed by enactment or otherwise on a charity trustee in relation to the exercise of functions in that capacity.
- “(4) Any breach of the duty under subsection (1) or (2) is to be treated as being misconduct in the administration of the charity.
- “(5) All charity trustees must take such steps as are reasonably practicable for the purposes of ensuring—
 - (a) that any breach of a duty under subsection (1) or (2) is corrected by the trustee concerned and not repeated, and
 - (b) that any trustee who has been in serious or persistent breach of either or both of those duties is removed as a trustee.”

30. Aside from the nature of the duties which fall upon the Trustees of the Trust by virtue of subsection (1) of section 66, subsections (2) and (4) mean that each Trustee could be responsible individually in the event of actions which were deemed to be misconduct (as that expression is defined in section 66(4)), although subsection (5) does give each of the Trustees an opportunity to correct any breach by virtue of the duty imposed in subsection (5)(a). The steps which the Trustees are taking to consider the constitution of the Trust are in my opinion at least a first step in the fulfilment of their duties under the 2005 Act.

31. In September 2010, OSCR published a document entitled “Guidance for Charity Trustees” (“the 2010 OSCR Guidance”). Although it is written principally for “the charity trustees of small to medium sized charities”, it is stated that “the guidance should also prove useful to charity trustees of larger charities”: paragraph 1.2. For present purposes, the following passages in the 2010 OSCR Guidance may be said to be relevant. Paragraph 3.3 provides three possible scenarios “which may give rise to conflicts of interest” but emphasises that these “should not be seen as the only areas where conflicts of interest can arise, but are

provided as examples of the most common.” The third possible scenario provides that:

“... there may be the possibility of a conflict of interest between the concerns of two different organisations to which a charity trustee is affiliated. The trustee should declare a conflict of interest to the other charity trustees, and refrain from participating in any discussion or decision-making process about the subject in question. An example might be where a charity trustee is a member of two different organisations which are applying to the same trust for a grant. The conflict of interest should be disclosed... and the charity trustee should not take part in any discussion or decision-making.”

In respect of each of the three scenarios, the 2010 OSCR Guidance provides that:

“It is not only the responsibility of individual charity trustees to act only in the interests of the charity and avoid conflict of interest, but also the duty of their fellow charity trustees to take reasonable steps to ensure that they do so.”

32. In March 2011, OSCR published guidance entitled “Who’s In Charge: Control and Independence in Scottish Charities” (“the 2011 OSCR Guidance”) which includes not only advice to charity trustees by reference to the requirements of the 2005 Act, but also contains a number of case studies which describe the circumstances of identified charitable trusts and action which has been taken by OSCR. These case studies include one relating to the Trust. At page 7, it is stated that:

“This guide will be of particular use to:

- the charity trustees of large and complex charities
- the charity trustees of charities with close connections with local authorities...
- people and bodies advising such charities
- ...
- local authorities... or other bodies which have close links to charities or work in partnership with them.”

The 2011 OSCR Guidance is therefore relevant to the Trustees, to those who are advising the Trustees, and also to the Council.

33. For present purposes, the following particular passages in the 2011 OSCR Guidance may be noted. Chapter 2 is entitled "What to watch out for" and a number of "Key points" are set out throughout the Chapter. In the opening to Chapter 2 on page 10, it is stated that the guidance is looking at "those structures and situations where charity trustees should take particular care to ensure they remain in charge." A number of situations are set out including the following on page 12:

"B. A charity has links to another body

"Many charities have links to other bodies. Sometimes these relationships can be very close and significant to the charity, example where:

- The two bodies share personnel and either:
 - All the charity trustees serve on the Board of the other body
 - The majority of the charity trustees have a duty to the other body as members or employees
- The other body was instrumental in setting up the charity
- ..."

There is then reference to particular risks which OSCR has identified in respect of such charities.

34. At page 14, the 2011 OSCR Guidance states that:

"b. A charity with links to another body must actively manage conflict of interest

"When a charity's trustees are all or mostly members or employees of another body they are likely to face situations where their ability to take independent decisions is called into question.

"Establishing an appropriate structure and governance arrangements for a charity is only the first step. Charity trustees should demonstrate through day-to-day practice that they are acting in the best interests of the charity. They should show publicly that:

- They are aware of, and managing, any conflict of interest and can demonstrate this
- Where there is a conflict, that the decision on the matter was taken in the charity's best interests
- In any situation where a charity trustee is unable to give priority to the charity's interests, he or she should consider withdrawing in

order for the decision to be made by other charity trustees who are not affected by such conflicts

- The charity remains able to carry on its business. The charity should have a governance structure in place which would allow quorate decisions to be made even if a number of trustees had to withdraw.”

35. At this point in the 2011 OSCR Guidance, the “Case study” relating to the Trust is set out. There is a description of the circumstances of the Trust and the concerns which OSCR has expressed in the correspondence referred to above.

36. At page 15, the following are set out:

“Key points for charity trustees and other bodies

- The make-up of the Board, where it is dominated by members from a linked body, can lead to an inherent risk of recurrent conflicts of interest
- Conflict of interest policy should be applied in all situations where there is a conflict or potential conflict
- The charity should consider whether it is advisable to maintain a Board where conflict of interest arises so frequently that charity trustees must withdraw thus preventing effective management of the charity
- Charity trustees should always demonstrate that they are behaving in the best interests of the charity and be conscious of how their actions appear to the public.”

37. At page 17, it is stated:

“Key points for charity trustees and other bodies

- Bodies that set up or forge strong links with a charity should be aware that this does not necessarily give them control over all of the charity’s activities. Where bodies such as local authorities set up bodies which are intended to seek charitable status, the bodies’ structure and the nature of their activities must allow them to pass the charity test and enable their charity trustees to fulfil their duties to the charity
- A majority of charity trustees in a charity established by another body should ideally be independent of that body, that is, the majority should neither be its members nor its employees

- If linked and independent charity trustees are evenly balanced on the Board, it is good practice that the Chair be one of the independent charity trustees
- Contracts and property arrangements between the bodies should be clearly in the interests of the charity whether it is making use of another body's assets, or supplying its assets for use by another body."

38. In Chapter 3 of the 2011 OSCR Guidance, which is entitled "Ensuring independent decision-making – a practical guide", the following statements are relevant. At page 24, in two separate passages it is stated that:

"The appointments process for charity trustees should be designed to identify the best people for the needs of the charity. What the needs of the charity are will depend on its context and activities, and these may make it appropriate to bring in charity trustees who can provide links to stakeholders, whether beneficiaries or other bodies with whom the charity is involved. Such charity trustees must act in the interests of the charity, as must all charity trustees. Where there are links to another body, a transparent arm's length selection process for independent charity trustees, such as an independent nominations committee may be appropriate and help to ensure real and perceived independence...."

"The law does not prevent a linked body from appointing some or all of a charity's trustees, nor prevent the appointment of charity trustees ex-officio (that is, because of another post or role they have). However, a charity trustee, once appointed, must act only in the charity's best interests and cannot act merely as a delegate from another body or group of stakeholders."

39. There are other aspects of the 2011 OSCR Guidance which are relevant to the Trustees, in particular the advice on "How can a charity show it is taking decisions independently?" beginning at page 28. At page 29, an appropriate conflict of interest policy is required of a charity, and it is stated:

"When should a charity trustee consider withdrawing from a meeting?

"The charity's constitution or other governing documents should set out the procedure when there is a conflict of interest such as those detailed above, or state that the procedure will be regulated by a code of conduct or standing orders.

"Where a charity trustee is aware that he or she is subject to a conflict of interest between the interests of the charity of those of another person or body who appointed them, and where they are unable, because of their duty to that other person or body to put the interests of the charity first, then they must withdraw from the discussion or decision concerned. It may also be appropriate for charity trustees to withdraw from discussions in other circumstances of conflict of interest. Where they do not do so, they should be able to demonstrate that they have acted in the interests of the charity..."

At page 30, the following is stated:

"What happens if a charity trustee has to withdraw from decisions frequently?

"A charity trustee will have to consider whether their interests mean that conflicts will be regular and recurring, and, particularly if, in terms of the charity's constitution or code of conduct or of good practice they find themselves frequently having to withdraw from significant charity decisions. Is this preventing them from usefully carrying out their charity trustee duties? In such a situation, it may be appropriate for them to stand down and be replaced by a charity trustee who does not have the same conflicts.

"There is no legal reason why charity trustees may not have an interest in another connected body as long as they are able to give priority to the interests of the charity. It is up to the individual charity trustee then to decide in the light of the circumstances whether the scale of the conflict means they should not join, or remain, on a charity Board."

40. There can be no doubt that the particular passages quoted, as well as the 2011 OSCR Guidance generally, are relevant to the situation of the Trustees and the governance of the Trust. In summary, they suggest that where a charitable trust has a link to a local authority, such as where the trust was set up by the local authority, the particular governance considerations arise. Such a charity requires to have a governance structure which allows decisions to be made even where a number of trustees have to withdraw because of a conflict of interest. Where withdrawal of trustees because of a conflict of interest is regular, the trust ought to reconsider its board structure and the individual trustees in question should consider whether they should remain as trustees. Where a trust has been

established by a local authority, the majority of the trustees should be independent and the trustee occupying the chair should be an independent trustee. Although there is no prohibition as a matter of law upon a local authority appointing some (or even all) of the trustees of a charitable trust, if that were to mean that the trustees so appointed had a conflict of interest such that the working of the trust became impossible, the practical result would be that a sufficient number of independently appointed trustees would have to be appointed in addition to the local authority appointed trustees.

The first question:

Does the constitution of the Trust require to be changed to comply with current law and practice?

41. Having regard to all of the matters referred to above, it is my opinion that the constitution of the Trust as presently established, or at least the way in which it requires to function, may not in all circumstances be able to satisfy current law and practice. As a result, it would be advisable to alter the arrangements for the appointment of Trustees in order to address that concern.
42. The critical matter is the fact that almost all of the Trustees are members of the Council, and as a result the Trustees may not in every situation be able to comply with the duties imposed by section 66(1) of the 2005 Act, and the common law duties preserved by section 66(3), at least without making the functioning of the Trust unworkable.
43. The fact that a person who is a trustee of a charitable trust may have interests in connection with another organisation, which interests can result in a conflict of interest arising in relation to the person's duties as a trustee of the charitable trust, does not mean that that person is automatically disqualified from being a charitable trustee, nor that the charitable trust in question is acting unlawfully if such a person remains as a trustee. This is confirmed by the 2011 OSCR Guidance. In such a situation, the remedy is for the trustee in question to declare

a conflict of interest and thereby to comply with the duty imposed by section 66(1), and to take no further part in the discussion or decision-making on the matter in question and, in the case of the Trust, thereby to comply with section 6 of the Administrative Guidance, which in turn is required by what is said at page 14 of the 2011 OSCR Guidance (as well as being consistent with paragraph 3.3 of the 2010 OSCR Guidance).

44. The problem in the case of the Trust is that the requirement that a Trustee who is also a member of the Council has to consider and act upon a conflict of interest where the Council is concerned applies to almost all of the Trustees. If each of these Trustees were required to act in the manner described, then the Trust would be incapable of making a decision on the matter in question. This is because if all of the Trustees who were councillors were required to retire from a meeting where a relevant decision was to be taken, the business in question could not be transacted because the quorum of a meeting of the Trustees is twelve by reference to paragraph 10.5 of the Administrative Guidance.
45. Although it is not related to the issue of whether or not the Trustees can comply with their duties under the 2005 Act in a way which permits the Trust to function as a charitable trust, the same considerations will apply to the same individuals in their positions as members of the Council. As noted in paragraph 4.2.3 of the Memorial, members of the Council require to comply with the obligations set out in the Code of Conduct for Councillors which has been issued by the Scottish Ministers in accordance with section 1(1) of the Ethical Standards in Public Life etc (Scotland) Act 2000. If each of the (presently) twenty one out of twenty two members of the Council were to have to declare a conflict of interest in a situation where they had potentially conflicting duties as Trustees of the Trust, the Council would be likely to be unable to function in relation to a particular topic where a decision had to be made by the members. This conclusion may depend upon the standing orders of the Council which have not been before me for consideration

but it appears to be a logical consequence of the fact that the vast majority of both the Trustees and the members of the Council are the same individuals.

46. From the point of view of the Trust, the critical question is whether there will exist a conflict of interest where a Trustee who is a member of the Council is considering a decision which might be said to impact sufficiently on the interests of the Council. This question arises in three parts: first, what is the legal concept of such a conflict of interest; secondly, what are the practical circumstances in which the Trustees are required to make decisions in accordance with the Trust Deed; and thirdly, would the making of decisions in these circumstances give rise to a conflict of interest?

The concept of a conflict of interest

47. The obligation of trustees in a situation which may give rise to a conflict of interest was explained in the case of *Aberdeen Railway Company v Blaikie Brothers* (1854) 1 Macq 461 which was a decision of the House of Lords. The circumstances were that Blaikie Brothers, a firm of iron founders, were seeking to enforce the performance of a contract for the delivery of a consignment of iron chairs to the appellants who were a railway company. The principal defence for the railway company was that at the time of the contract, the managing director of Blaikie Brothers was simultaneously a director and the Chairman of the railway company. For the purposes of my Opinion, it is worth quoting the Opinion of the Lord Chancellor (Lord Cranworth) at some length. In two passages at pages 471 to 474, he said the following:

“This, therefore, brings us to the general question, whether a Director of a Railway Company is or is not precluded from dealing on behalf of the Company with himself, or with a firm in which he is a partner.

“The Directors are a body to whom is delegated the duty of managing the general affairs of the Company.

“A corporate body can only act by agents, and it is of course the duty of those agents so to act as best to promote the interests of the corporation whose affairs they are conducting. Such agents have duties to discharge of a fiduciary nature towards their principal. And it is a rule of universal application, that no one, having such duties to discharge, shall be allowed

to enter into engagements in which he has, or can have, a personal interest - conflicting, or which possibly may conflict, with the interests of those whom he is bound to protect.

"So strictly is this principle adhered to, that no question is allowed to be raised as to the fairness or unfairness of a contract so entered into.

"It obviously is, or may be, impossible to demonstrate how far in any particular case the terms of such a contract have been the best for the interest of the... trust, which it was possible to obtain.

"It may sometimes happen that the terms of which a trustee has dealt or attempted to deal with the estate or interests of those for whom he is a trustee, have been so good as could have been obtained from any other person, - they may even at the time have been better.

"But still so inflexible is the rule that no inquiry on that subject is permitted. The English authorities on this head are numerous and uniform."

"...

"Was then Mr Blaikie so acting in the case now before us? - if he was, did he while so acting contract on behalf of those for whom he was acting with himself?

"Both these questions must obviously be answered in the affirmative. Mr Blaikie was not only a Director, but (if that was necessary) the Chairman of the Directors. In that character it was his bounden duty to make the best bargains he could for the benefit of the Company.

"While he filled that character... he entered into a contract on behalf of the Company with his own firm, for the purchase of a large quantity of iron chairs at a certain stipulated price. His duty to the Company imposed on him the obligation of obtaining these chairs at the lowest possible price.

"His personal interest would lead him in an entirely opposite direction, would induce him to fix the price as high as possible. This is the very evil against which the rule in question is directed, and I see nothing whatever to prevent its application.

"I observe that Lord Fullerton [in the Inner House of the Court of Session: see (1851) 14 D 66, at page 72] seemed to doubt whether the rule would apply where the party whose act or contract is called in question is only one of a body of Directors, not the sole trustee or manager.

"But, with all due deference, this appears to me to make no difference. It was Mr Blaikie's duty to give to his co-Directors, and through them to the Company, the full benefit of all the knowledge and skill which he could bring to bear on the subject. He was bound to assist them in getting the articles contracted for at the cheapest possible rate. As far as related to the advice he should give them, he put his interest in conflict with his duty, and whether he was the sole Director or only one of many, can make no difference in principle.

"The same observation applies to the fact that he was not the sole person contracting with the Company; he was one of the firm of Blaikie,

Brothers, with whom the contract was made, and so interested in driving as hard a bargain with the Company as he could induce them to make.
"It cannot be contended that the rule which I have referred is one confined to the English law, and that it does not apply to Scotland."

The Lord Chancellor thereafter referred to authority in support of the proposition that the laws of Scotland and England were the same on this matter, a view confirmed in the opinion of Lord Brougham at page 478 *et seq.*

48. The decision in *Aberdeen Railway Company* has been referred to and relied upon in many subsequent cases. For example, in *Regal (Hastings) Limited v Gulliver*, decided in 1942, and reported in a Note at [1967] 2 AC 134, reference was made in the speech of Viscount Sankey at page 138 to the opinion of the Lord Chancellor in *Aberdeen Railway Company* where he said that: "A corporate body can only act by agents, and it is of course the duty of those agents so to act as best to promote the interests of the corporation whose affairs they are conducting". At pages 144 and 145, Lord Russell of Killowen said:

"The rule of equity which insists on those, who by use of a fiduciary position make a profit, being liable to account for that profit, in no way depends on fraud, or absence of bona fides; or upon such questions or considerations as whether the profit would or should otherwise have gone to the plaintiff, or whether the profiteer was under a duty to obtain the source of the profits for the plaintiff, or whether he took a risk or acted as he did the benefit of the plaintiff, or whether the plaintiff has in fact been damaged or benefited by his action. The liability arises from the mere fact of a profit having, in the stated circumstances, been made. The profiteer, however honest and well-intentioned, cannot escape the risk of being called upon to account."

In *Boardman v Phipps* [1967] 2 AC 46, at page 105, Lord Hodson said that:

"The proposition of law involved in this case is that no person standing in a fiduciary position, when a demand is made upon him by the person to whom he stands in a fiduciary relationship to account for profits acquired by him by reason of his fiduciary position and by reason of the opportunity and the knowledge, or either, resulting from it, is entitled to defeat the claim upon any ground save that he made profits with the knowledge and assent of the other person."

In *Inglis v Inglis* 1983 SC 8, at page 15, the Lord Justice Clerk (Wheatley), having referred to *Aberdeen Railway Company* and *Boardman*, said:

“Put in its widest form the doctrine means that the trustee may not place himself in a position where his interests *may* conflict” (emphasis in the original).

Finally, a recent example in Scotland of reference to the principles in *Aberdeen Railway Company* is the case of *Earl of Cawdor, Petitioner* 2006 SLT 1070.

49. These and other cases subsequent to *Aberdeen Railway Company* have involved their own particular facts but for the purposes of the matters considered in this Opinion, I regard the principles set out above from the opinion of the Lord Chancellor as giving the necessary guidance for a consideration of the position of the Trust and the Trustees.
50. In my opinion, the following are the principles which may be identified having regard to the present circumstances. First, a trustee cannot make a lawful decision which may be of benefit to him in his personal circumstances however much it may be shown that he acted with the best of intentions and in good faith. Secondly, it does not matter if he is acting in either capacity as only one of a number of trustees because it is the interests of the body of which he is a trustee which are relevant rather than his direct personal interest. Thirdly, the precise capacity in which the person is acting is not critical, whether that might be as a trustee proper, as a director of a limited company, or in some other fiduciary capacity, as long as it may be said that in the capacity in question the person owes fiduciary duties to his principal. Lastly, the only way in which a particular transaction which has taken place in circumstances contrary to these principles may be allowed to stand, is if the person against whose interest the trustee has acted has consented.
51. I do not regard that last principle as having any application in a situation where one is considering a prospective conflict of interest, rather than an existing

concluded contract which has been challenged. In any event, it is difficult to envisage a situation where either a local authority or a trust having public purposes could properly consent to something which had occurred in a situation of a conflict of interest, not least where the fundamental problem was the fact that it was the position of the individual decision-makers in each case which had brought about the conflict in the first place.

52. I therefore turn to consider the application of the remaining principles identified above to the circumstances of the Trust.

The practical circumstances in which the Trustees are required to make decisions

53. The Trustees are entitled by virtue of purpose (SECOND) of the Trust Deed to expend the Trust Fund to make grants or loans "for any purposes which in the opinion of the Trustees are solely in the interests of the area administered by the local or other governmental authority for the time being of the Shetland Islands or of the inhabitants of the said area (hereinafter referred to as "the community") and provided that any such grant or loan is for charitable purposes." By reference to the specific purposes identified in purpose (SECOND), the following may be noted: the promotion of the welfare of the community in specific purpose (a); the promotion of meetings for purposes of recreation, instruction or education in specific purpose (b); the maintenance of means of communication, in particular the provision of ports and harbours, in specific purpose (c); the encouragement of education in specific purpose (f); and the endowing and equipping of schools and colleges in specific purpose (i). The other specified purposes, and the overall objects of purpose (SECOND), are to the effect that the Trustees may expend the Trust Fund for the benefit of the community.
54. It is my opinion that the nature and scope of these purposes are comparable with, and may impact upon, the functions which the Council may perform, and in certain cases are required to perform, out of the funds available to the Council as a local authority. Obvious examples in the case of the Council are the provision of

education and facilities for education under the Education (Scotland) Act 1980, provision for social welfare under the Social Work (Scotland) Act 1968, provision for recreation, sporting, cultural and social facilities under the Local Government and Planning (Scotland) Act 1982, and the particular provision which the Council may make for ports and harbours under the 1974 Act. I do not repeat the specific statutory provisions which are referred to above. In addition, the entitlement of the Trustees to expend the Trust Fund generally for the benefit of the community may result in their making provision for services and facilities which might otherwise be provided by the Council under section 69 of the 1973 Act, section 20 of the 2003 Act, or otherwise. In all such cases, and by definition in accordance with purpose (SECOND) of the Trust Deed, the Trustees are entitled to expend the Trust Fund within the local government area which applies to the Council and for the benefit of the inhabitants of the area served by the Council.

55. These are some, although not necessarily all, of the general examples of where the Trustees may expend the Trust Fund for the provision of services and facilities in a manner which may affect the necessity for the Council to provide equivalent services and facilities. In paragraphs 16 to 21 above, I provided a description of the actual services and facilities which the Trustees have provided. It appears to be the case that the provision of certain of those by the Trust will have rendered it unnecessary for the Council to consider the provision of equivalent services and facilities which they might otherwise have felt obliged to provide in the interests of the inhabitants of the area served by the Council and in the fulfilment of their statutory functions, powers and duties as a local authority.
56. In situations where a contractual relationship has come about between the Trustees and the Council, the interests of the Trust and the interests of the Council may be said to be directly opposed in the manner described by the Lord Chancellor in *Aberdeen Railway Company*. In the case of decisions on the part of the Trust through SLAP to lease premises to the Council, it would have been in the interests of the Trust to obtain the maximum rent whereas the interests of the

Council would have been the direct opposite. The same would have been the case in relation to the sale by the Council to the Trust of the shares in VEL. In the arrangements for Service Level Agreements, the Trustees will have a duty to obtain these services at the minimum reasonable cost to the Trust, whereas the Council will have duty to obtain the best return for these services.

57. It is also conceivable that were the Trust to acquire an interest in land from the Council, the primary duty of the Council would be to obtain the best consideration in fulfilment of section 74(2) of the 1973 Act. This may not at present be an issue which arises but it could occur in the future. It may have been an issue when the Council sold the Sullom Voe oil terminal although it must be recognised that that was not a transaction with the Trust because it was carried out with its predecessor, Shetland Islands Council Charitable Trust, as well as being entered into before the enactment of both the 2003 Act and the 2005 Act.
58. These are just the obvious examples which are apparent to me of where the interests of the Trust and the interests of the Council could be said to conflict.
59. I understand that it may be said that the Trust cannot fund the Council's statutory functions and I assume that this is because the purposes of the Trust are restricted to the making of grants of loans "for charitable purposes" as set out in purpose (SECOND). Whilst this is the case, it does not in my opinion prevent the providing of a service or facility by the Trust from being of potential advantage to the Council. The Trust will not be fulfilling a statutory function of the Council in any direct sense but the result may be that the Council has less reason to provide an equivalent service or facility using its statutory powers. This is not a feature unique to the activities of the Trust because similar consequences may exist in relation to other charitable trusts. For example, many providers of independent education and independent social welfare services are registered as charities and their provision of services may relieve the relevant local authority of the need to provide the same services to the same extent. There may therefore be an overlap

in the provision of facilities and services, both generally and in the case of the Trust and the Council, but that does not mean that a charitable trust is performing the functions of a local authority. It is this potential overlap which gives rise to a potential conflict of interest on the part of the Trustees who are councillors.

Does the making of decisions in these circumstances give rise to a conflict of interest?

60. I am in no doubt that the answer in the circumstances before me is in the affirmative.
61. In my opinion, the potential for a conflict of interest between the interests of the Trust and those of the Council may arise in both a direct and an indirect sense. In a direct sense, the Council have a duty in performing their functions to obtain best value by reference to section 1(1) of the 2003 Act and to minimise their expenditure in the public interest. The Council have particular duties to obtain the best consideration, for example when disposing of land or an interest in land by reference to section 74(2) of the 1973 Act. The duties of the Trustees are in effect the same. The Trustees each have a fiduciary duty to conserve and maximise the value of the Trust Fund and to expend it only to the minimum extent necessary to meet a particular purpose which they have identified. This duty exists both at common law and in accordance with section 66(1) of the 2005 Act.
62. In these respects, the duties of those who are councillors of the Council and of those who are Trustees of the Trust in a situation where something is to be provided directly by the Trust to the Council, or in the case of the services to be provided by the Council to the Trust, are potentially in conflict.
63. Indirectly, the situation is the same. The Council has the general power under section 69 of the 1973 Act to pursue purposes which are in the interest of their area. Under section 20 of the 2003 Act, they are entitled to consider steps to be taken for the well-being of their community. Under section 67(3)(e) of the 1974

Act, the Council as the successors of Zetland County Council have a particular entitlement to expend funds for the benefit of the community.

64. The Trust has Objects of Trust which are in effect the same or similar. The Trustees may decide to expend the Trust Fund in the interests of members of the same community which is served by the Council. The Trustees may expend those funds to provide community facilities of a type similar to those which might be provided by the Council. The result is that in considering both the duties of the Council as the local authority, and the purposes of the Trust, the councillors and the Trustees respectively will be looking potentially to providing the same or similar benefits to the same community.
65. In this indirect sense, I regard it as foreseeable that a Trustee in deciding that the Trust should provide a particular community facility or service might have in his mind the fact that such provision would save the necessity for the Council to consider the provision of the same facility or service. This situation is equally easy to envisage in reverse because the provision of a service or facility by the Council might allow the Trust to save part of the Trust Fund which could then be used for other purposes.
66. The Trustees are required to exercise their discretion and judgement in the dispensing of the funds of the Trust and in making other arrangements with the assets of the Trust. In doing so, the Trustees owe duties as custodians of the Trust Fund and to the community and inhabitants of Shetland to dispense the Trust Fund for the objects set out in purpose (SECOND) of the Trust Deed.
67. At the same time, an overwhelming majority of the Trustees are required separately to exercise the duties of members of the local authority which exercises the functions of a local authority over the same geographical area and in respect of the same community and inhabitants. In their capacity as councillors, those who are also Trustees of the Trust will have to make decisions about how to

allocate the resources of the Council for the same or similar purposes as they are considering for the dispensation of the funds of the Trust.

68. I am therefore satisfied that the constitution of the Trust requires to be changed. This is because in a situation where the interests of the Trust and the interests of the Council may be said either to be in potential conflict, or where the provision of a facility or service by one may be to the potential advantage to the other, the Trustees who are councillors will have a conflict of interest which they require to declare and act upon as Trustees in order to comply with the duty provided by section 66(1)(c)(ii) of the 2005 Act. In that situation, the problem is a practical one because of the fact that there are so many Trustees who are councillors with the result that in that situation no decision can be made by the Trustees. This means that I agree with what has been said by OSCR in the first paragraph of the letter quoted at paragraph 25 above: the problem is the practical application of the conflict of interest policy given the current governance arrangements of the Trust.

69. For all of these reasons, I answer the first question in the affirmative.

The second question:

If the answer to the first question is yes what changes does senior counsel consider would be necessary to meet the minimum requirements of achieving compliance with current law and procedure?

70. Each of the Trustees is a "charity trustee" for the purposes of section 66 of the 2005 Act. As such, each Trustee has a duty in circumstances capable of giving rise to a conflict of interest between the charity and any other person, to declare that conflict of interest and to take no part in the decision in question. In the situations described above, each Trustee who is at the same time a councillor of the Council is subject to a conflict of interest which means that he ought not to participate in any decision on the matter in question in order to comply with the requirements of both section 66(1) and the 2011 OSCR Guidance.

71. Given that that virtually all of the Trustees fall into that category because they are simultaneously members of the Council, this means in my opinion that the inevitable consequence is that in order to allow it to function, the constitution of the Trust must be altered so that it be composed of Trustees who in the main are not subject to that conflict of interest.
72. There are two aspects to the identification of an appropriate level of Trustees who are not likely to be subject to that conflict of interest. The first is the need for the Trust to be able to make proper decisions on all matters without the existence of conflicts of interest on the part of a number of Trustees at a level which makes that decision-making impossible. The second is the need for the Trust to satisfy the requirements of OSCR in accordance with the 2005 Act in order that it may remain as a charitable trust. These aspects do not necessarily lead to the same result, but they are certainly not incompatible. Likewise, the satisfaction of these aspects will bring about a situation in which both the accountability of the Trust to the inhabitants of Shetland and the independence of the Trustees as referred to in paragraphs 4.1 to 4.3 of the Memorial are addressed.
73. By reference to previous examples, it appears that in the case of a charitable trust which is serving purposes which may be of benefit to a local authority, there is no reason why a substantial number of the trustees of such a trust may not be elected members of the local authority in question. This is confirmed by the 2011 OSCR Guidance. Within the papers provided to me, there are the details of two charitable bodies, namely "Culture and Sport Glasgow" and "Fife Sports and Leisure Trust Limited" which are companies limited by guarantee set up by the respective local authorities for the areas in question. In the case of Culture and Sport Glasgow, there are three categories of directors, one of which is "Partner Directors" who are elected members of Glasgow City Council. The maximum number of directors is eleven, of whom no more than six may be Partner Directors. The quorum is six.

74. In the case of Fife Sports and Leisure Trust Limited, there are also "Partner Directors" who are elected members of Fife Council, and of whom there may not be more than six. The maximum number of directors is thirteen. The quorum is four unless another number is fixed. This company was the subject of a case study at pages 16 and 17 of the 2011 OSCR Guidance. This narrates that the constitution of the company allowed the local authority to be its sole member and:

"As such, the council would be able to change the governing rules of the company and appoint or dismiss all of its directors. Best practice would have been for a majority of directors to be selected independently of the council, perhaps through an impartial nominations committee....".

Nevertheless, OSCR decided that the company should be granted charitable status "on balance" because:

"the existing arrangements did not necessarily prevent its charity trustees from acting independently, given other factors in its governance."

These factors included the fact that there was a majority of non-councillor directors, that the Chairperson was one of the independent directors and that the company had clear conflict of interest provisions.

75. There are also details of "Enjoy East Lothian Limited". It does not appear to have prescribed numbers of directors in different categories but it does envisage that directors may be "representatives of the district of East Lothian".
76. It appears that each of these organisations has been set up by the respective local authority and is presently registered as a charity by OSCR, which registration in the case of Fife Sports and Leisure Trust Limited at least has been confirmed after investigation. That suggests that even where a significant number of trustees of a trust or body are elected members of the local authority having responsibilities within the same area, OSCR will not regard the trust or body in question as being unsuitable for charitable status. Having said that, it is clear that in the case of these trusts, their primary or sole source of income is derived from the local authority in question and that is a situation which is different from that of the Trust.

77. That OSCR does not regard the fact that some trustees of a trust having charitable status may be local authority councillors as depriving the trust of its character as a charitable trust appears to me to be entirely appropriate. I have not identified any reason why either an equivalent charitable trust, or the Trust in this case, should not be permitted to have, as at least some of its trustees, persons who are elected members of the local authority for the same area.
78. By reference to the Administrative Regulations at paragraph 10.5, it is presently the case that a decision at a meeting of the Trustees requires a quorum of twelve. This means that with a total potential component of twenty four Trustees, an appropriate quorum is regarded as one half of that number. This seems to me to be reasonable in the interests of the proper accountability of the Trustees to the community for their decisions and the size and nature of the Trust Fund which they are required to administer.
79. At the meeting of the Trust which took place on 8th September 2010, it appears to have been agreed that an appropriate number of Trustees of the Trust in the future would be fifteen: see the Minute of the meeting at page 8. I do not regard that number of Trustees as critical, and it might be more or fewer, but I proceed upon the prospect of fifteen Trustees as the desirable total. In that situation, and in order to reflect the existing approach to an appropriate quorum, the result would be a quorum of eight Trustees.
80. In my opinion, the issue then becomes one of the ability of the Trust to function adequately in relation to all of the decisions which it will require to take including those which may affect the interests of the Council. The Trust comprises a Trust Fund which does not depend upon income from the Council, other than commercial income from rents and the like. Although I have no precise details of this, the capital of the Trust Fund appears to have come in substantial part from the Disturbance Payments and from payments made by the Council under the

unique power which the Council have by virtue of section 67(3)(e) of the 1974 Act. The Trust is therefore unlike the other trusts established by local authorities which are referred to above. The Trust has a more separate and independent existence than those other trusts and in my opinion it is important that this is demonstrated potentially beyond what might be required by OSCR.

81. In order to comply with section 66 of the 2005 Act, with the 2011 OSCR Guidance, and with the principles of law discussed above, I have already said that it is my opinion that any of the Trustees who are members of the Council will have to consider declaring a conflict of interest and withdraw from decision-making where a decision of the Trustees may have an effect on the interests of the Council and for which those same Trustees will have a responsibility as members of the Council.
82. Taking all of these considerations into account, it is my opinion that with a total number of Trustees of fifteen, and a quorum of eight, no more than four Trustees should be members of the Council. This would allow a decision in which the councillor Trustees had declared an interest still to be made by a substantial body of the Trustees and beyond the minimum number required by the quorum. It would demonstrate the functional independence of the Trust from the Council, both in relation to individual decision-making and also in the interests of the community who should thereby be assured that it was the best interests of the Trust in serving the purposes of the Trust which were bringing about the decisions which were being made.
83. Whilst the number of councillor Trustees will be a matter of debate, and I note that at the meeting of the Trust referred to above, seven councillor Trustees were proposed, I have reached the conclusion taking into account the independence of the Trust from the Council, the need for the Trust to be accountable for the decisions which are made, and the desirability for such decisions to be seen as having been made free from the actual or perceived influence of the Council, that

simply to have a bare minority of councillor Trustees would not by itself be sufficient to achieve these objectives.

84. A maximum of four councillor Trustees, when taken along with a quorum of eight, would mean that in no circumstances could the Trustees make a decision without the support of at least one of the non-councillor Trustees, even in a situation where the potential interests of the Council were not an issue. In my opinion, this would be an important factor in affirming and demonstrating the independence of the Trust from the Council in all circumstances and of the fact that its decisions were being made entirely in the interests of the Trust and not because of the particular interests of those Trustees who were members of the Council.
85. Having said that, I am conscious of a desire on the part of the Trustees that because there are seven wards within the Council area, there should be seven councillor Trustees. If that were to be the situation, it is my opinion that the principles and appearance of independence in the making of all decisions by the Trustees could be achieved in other ways. With seven councillor Trustees, one solution would be to increase the total number of Trustees to twenty nine with a quorum of fifteen. This would obviously be cumbersome and undesirable and I can well understand why the Trustees would not wish it, not least because of the desire which they have already stated to reduce the existing number of Trustees.
86. In that situation, there may be other ways of addressing the same principles and appearance of independence. If, for example, the proposed quorum were to be increased to say nine or ten, and the Administrative Regulations were to be amended to require that no decision could be taken unless at least a minimum number of non-councillor Trustees had voted in favour of the decision, then it would be seen that in no situation could a decision be taken by the councillor Trustees alone. Such an arrangement would require that the total number of Trustees be increased from fifteen to eighteen so that in a situation where all of

the councillor Trustees had declared an interest, there would still be sufficient non-councillor Trustees to form a quorum.

87. This is simply one way in which it appears to me that a desire for seven councillor Trustees could be accommodated without departing from what I regard as necessary both to satisfy OSCR and to address the wish for independence and accountability. The fact that OSCR will look at the individual governance arrangements of a charitable trust and make a decision based upon all of the circumstances is demonstrated by what is said in the 2011 OSCR Guidance in the case study of Fife Sports and Leisure Trust Limited. My suggested arrangement should therefore not be seen as prescriptive and it may be that the Trustees can devise other arrangements which would produce the same result in terms of independence and appearance of independence. Ultimately, what will be appropriate will be what is acceptable to OSCR at least for the purpose of preserving the status of the Trust as a charitable trust.
88. I have been provided with a copy of a paper prepared in 1988 for the purpose of nomination of the two *ex officio* trustees. This is clearly of historical interest only, but to the extent that it indicated potential constituencies of the local community from whom non-councillor Trustees might come, the categories suggested appear to me to be reasonable. Having said that, the purpose of this Opinion is to consider the categories of Trustees who might be subject to a conflict of interest rather than who new Trustees might be, and I do not offer any definitive advice on how a new body of Trustees might be constituted.
89. I have noted that it is generally considered to be a good thing that the Trustees who are councillors have a mandate to act as Trustees by virtue of their election as members of the Council. Whilst this is a reasonable view, the problem is that upon becoming Trustees, all of the Trustees owe their fiduciary obligations in accordance with the Trust Deed to the Trust both in accordance with section 66(1) of the 2005 Act and at common law. This is confirmed on page 24 of the 2011

OSCR Guidance. Those who are simultaneously members of the Council owe separate fiduciary duties to the Council as a statutory body having statutory powers and duties. It is the potential conflict between those duties which is critical and the fact that those who become Trustees may be said to have received an electoral mandate through being elected as councillors does not matter.

90. In my opinion, an arrangement such as suggested above would serve the three aspects set out in the Memorial. It would demonstrate that the Trust was accountable as an individual institution to the community of Shetland and was separate from the local authority serving the same area. It would demonstrate that the Trustees who made all decisions were independent of the actual or perceived interests of the Council and thereby demonstrate the independence of the Trust itself. It should allow the question with OSCR regarding the governance of the Trust to be resolved in a way which secures the continued registration of the Trust as a charitable trust under the 2005 Act.
91. As far as the procedure which would be necessary to bring about the desired changes in the constitution of the Trust, it appears that an alteration to the constitution to the Trust which would result in there being fewer trustees who were members of the Council and more Trustees who were not, would satisfy the "reorganisation conditions" set out in section 42(2)(b) and (c) of the 2005 Act. In this situation, the Trust may make an application for approval of "a reorganisation scheme" in terms of section 42(3)(a), and OSCR may approve such an application in accordance with section 39(1), or OSCR (or indeed the Trustees in their own right) may apply to the Court of Session who may approve the application in accordance with section 40(2).
92. It should be noted that the agents for the Trust provided to me a copy of an interlocutor in a Petition by *The Cowane's Hospital Trust* which was pronounced in the Outer House of the Court of Session on 27th January 2011. Although that interlocutor approves a Scheme for the administration of the trust in question, the

application to the Court was for the approval of a cy près scheme rather than an application made under the 2005 Act. If it were thought to be desirable, such an application could be made by the Trust as apposed to an application under the 2005 Act because the right to do so is preserved by section 42(4).

Concluding observations

93. I have reached the views expressed above having regard to how the body of Trustees should be structured in the future following a consideration of the Trust and its purposes and administration, the requirements of the 2005 Act and the 2011 OSCR Guidance, and the relationship between these and the functions, powers and duties of the Council. Having said that, a situation where a majority of the Trustees should always be able to be quorate and to be able to make a decision even if all of the Trustees who are also members of the Council declare a conflict of interest, is similar to the circumstances in the case of *Maidment and Ryan v The Charity Commission for England and Wales* [2009] UKFTT 377 (GRC), a decision of the First-Tier Tribunal (Charity) given on 16th November 2009.
94. The practical circumstances in that case concerned a Scheme for a charitable trust relating to the management of an area of land which was used as a public park (referred to as “the legacy land”) and where the local authority, Dartford Borough Council (“DBC”), were the trustee. In the Reasons for the Tribunal’s Decision, it was stated that:
- “5.28 The Tribunal heard that DBC had proposed to the Respondent [the Charity Commission] that it should appoint “up to three” individuals onto its “Deed, Trust and Obligations Committee” which manages the legacy land. It was proposed that these persons should be nominated by the party political leaders in the Council and by Groundwork Kent and Meadway [*sic*], as they would have relevant horticultural experience. It had, perhaps surprisingly, not been suggested that they should be residents of Dartford...
- “5.29 The Tribunal has considered this issue very carefully. On balance it sees no reason to disturb the present trustee arrangements provided that the arrangements for managing future conflicts of interest are robust. The

Tribunal notes that the Committee of DBC which administers this charity will need for the future to manage situations in which a conflict of interest inevitably arises. The Tribunal takes the view that all members of the Committee who are elected members of the local authority (ie not just members of the ward in which the legacy land is situated) or who are otherwise connected to DBC, would have to declare their interest and not vote on any issue where such a conflict arose. If (as is apparently being suggested) the Committee should be constituted so that its non-conflicted members could not form a quorum, then DBC would in future need to approach the Respondent to authorise all future transactions affected by the conflict of interest. This is clearly undesirable."

The Tribunal then addressed specific circumstances which had arisen and continued:

"5.31 Other situations in which a conflict of interest would inevitably arise would be decisions concerning the future use or development of the legacy land and/or adjoining land; the payment of legal costs by the charity in relation to proceedings arising from DBC's breach of trust; or the granting of a lease or easement over the legacy land to DBC. In the circumstances, the Tribunal is concerned to see governance arrangements put in place which will provide for the Committee of the Council which administers the charity to be able to make quorate decisions in the absence of those affected by a conflict of interest... It therefore seems to the Tribunal that the important issue for the Respondent to provide for in amending the Scheme is the number of independent (ie non-conflicted) persons who are able to form a quorum of the Committee under its standing orders, rather than merely the number of independent persons who are appointed to that Committee, but unable to form a quorum. The Tribunal concludes that this issue should be addressed in providing a machinery of governance for the charity and these appeals therefore succeed in relation to this issue...."

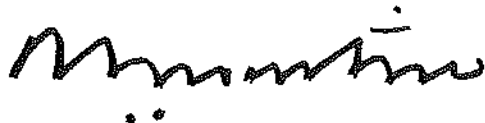
The Tribunal then set out a procedure as to how the Scheme in question should be altered and stated at paragraph 6.1(iii):

"so that the Committee of DBC which administers the charity is required to be constituted so as to provide for a quorum of individuals who do not suffer from a conflict of interest in relation to DBC and its dealings with the charity."

I regard the reasoning and result in *Maidment* as confirming the approach and the outcome which I have described in the circumstances relating to the Trust. It looked at how the trust in question was actually administered and the need for that administration to be, and be seen to be, independent of the local authority in

question. It would, in my opinion, provide useful support for an alteration to the constitution of the Trust in the manner which I have suggested.

THE OPINION OF

A handwritten signature in black ink, appearing to read 'Roy L. Martin', with a small dot above the 'i' and two dots below the signature.

Roy L Martin QC,
Terra Firma Chambers,
Parliament House,
Edinburgh,
25th March 2011.