

# Chapter 12

## Crown Corporation

### Governance

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# Crown Corporation Governance

## **Background**

### *What is corporate governance?*

**12.1** Corporate governance can be defined as the process and structure used to direct and manage the business and affairs of an organization with the objective of achieving the corporate mandate. Without effective corporate governance, establishing effective accountability is impossible.

### *What are the characteristics of effective governance?*

**12.2** The following is a list of the characteristics of effective governance. Boards must:

- be comprised of people with the necessary knowledge, ability and commitment to fulfill their responsibilities;
- understand their purposes and whose interests they represent;
- understand the objectives and strategies of the organization they govern;
- know and obtain the information they require to exercise their responsibilities;
- once informed, be prepared to act to ensure that the organization's objectives are met and that performance is satisfactory; and
- fulfill their accountability obligations to those whose interests they represent by reporting on their organization's performance.

**12.3** If a board truly exemplifies these characteristics, it will be providing effective governance, thereby promoting accountability.

### *How does effective governance promote accountability?*

**12.4** For accountability to be achieved, three conditions must exist. First, all parties must understand and agree with the mandate, mission, and strategic goals of a corporation. Second, information that adequately communicates the degree of achievement of the mandate, mission and goals of the organization, and compliance with guidelines must be passed upward through the accountability chain. Third, those in authority in the accountability chain must be willing to act within their authority in response to information received. All three of these conditions will be met in an environment of effective governance.

### *Why did we undertake this project?*

**12.5** As we mentioned in last year's Report, it was our intention to perform a detailed governance review of at least one New Brunswick Crown corporation during the 1996-97 audit year. Because an audit project had already been scheduled in the area of governance,

accountability and management control framework pursuant to the joint audit of the Atlantic Lottery Corporation Inc. (ALC) with the Auditor General of Nova Scotia, we chose that corporation. ALC is a Crown corporation under provincial legislation and we felt that any findings from the joint audit project could also be used in completing our own governance review. In effect, then, our work in the governance and accountability area for ALC fulfilled a dual role. It helped us to meet our commitment relating to the joint audit of ALC while at the same time allowing us to do a detailed governance review of a New Brunswick Crown corporation.

***Why is effective governance important for ALC?***

**12.6** ALC has four shareholders, representing four distinct provincial jurisdictions. Therefore, the establishment and maintenance of appropriate accountability relationships is very important. As we discussed above, the board can promote accountability by effectively fulfilling the governance role it has been assigned by the shareholders.

***Why is this important to the Legislative Assembly of the Province of New Brunswick?***

**12.7** It is clear that the main objective of the Atlantic Lottery Corporation is to maximize its profits, thereby maximizing the dollars available for public use in the four shareholder provinces. However, provincial policies sometimes restrict ALC's ability to meet this primary goal. For example, the Province has placed certain restrictions on games in order to try to limit the perceived negative social consequences of gaming. Measurement of the degree of success in achieving ALC's mandate, then, is more complicated than simply looking for growth in the bottom line.

**12.8** If there is effective corporate governance, the board of ALC will be providing the Province with the information it needs to evaluate the degree to which ALC has achieved its mandate. That information can be used as an important Legislative control.

**12.9** On the other hand, if governance and accountability structures are weak, then the Legislative Assembly may lack some of the information it needs to make accurate assessments of ALC's performance.

***The Corporation***

**12.10** The Atlantic Lottery Corporation was incorporated under the Canada Business Corporations Act in 1976 to be a co-operative venture between the four Atlantic provinces in the lottery business. Both revenues and net profits paid to shareholders have shown substantial growth over the past twenty years, coinciding with rapid growth in the lottery business in North America during the same time period. Many new games have been introduced both nationally and regionally. From relatively modest beginnings, the corporation has grown to employ a staff of over four hundred and twenty-five persons, with head offices in Moncton, and regional offices in Nova Scotia and Newfoundland.

**12.11** The environment in which ALC operates has changed rapidly in recent years. While technological advances have led to major

improvements at ALC, they have also created significant risks, particularly in the area of competition. When ALC was incorporated, it had a monopoly in Atlantic Canada over public gaming, with the exception of charity events and harness racing. However, with the rapid growth of the Internet, competition from gaming organizations outside the Atlantic provinces could soon become a very important strategic issue.

### ***Governance at ALC***

**12.12** ALC is an unusual public-sector corporation in that it has not just one government's set of interests to consider, but the interests of four provincial governments. This puts the board of ALC in the unique position of having to ensure all provincial concerns are dealt with, while still attempting to make decisions that are in the best interests of the corporation. The full board of directors of ALC is made up of eight members, two of whom are appointed by each of the four provincial shareholders. The shareholders include the Lotteries Commission of New Brunswick, the Nova Scotia Gaming Corporation, the government of the Province of Newfoundland and Labrador, and the Prince Edward Island Lottery Commission.

### ***Scope***

**12.13** Our objective in carrying out this project was to review the governance, accountability and management control framework for the corporation's activities, including an assessment of the quality of information and reporting available on its plans and performance. However, for purposes of this chapter, we have focussed on findings relating to governance and accountability issues only.

### ***Objective***

### ***Criteria***

**12.14** For purposes of our governance review, we have used the first six criteria developed for use in the joint audit project. Because these criteria were developed in consultation with the Auditor General of Nova Scotia, they are not identical to the governance criteria we developed last year and reported in our 1996 Auditor General's Report. However, we do not feel the differences to be significant. These criteria are presented in the "findings" section of this chapter.

### ***Procedures***

**12.15** Our examination procedures for this project included surveying and interviewing all seven of the ALC directors who were on the board at the time of our examination. Additionally, we interviewed the President of ALC, along with several members of senior management. We reviewed minutes of the Board of Directors, the Audit Committee, and the Senior Management Committee. We also reviewed pertinent reports and documents at ALC. General governance and accountability literature was also referred to in completing our work.

### ***Results in brief***

**12.16** Many of the findings from the joint audit of ALC relating to governance and accountability are included in this chapter. We would like to note that we have expanded upon certain items in the Shareholder's Audit Report issued by the Auditor General of Nova Scotia. A summary of our observations and key suggestions / recommendations relating to this project is presented in the "findings" section. Some highlights follow.

**12.17** There is a defined governance structure for ALC.

**12.18** At the time of our audit, there was no code of conduct in force setting standards of behaviour for board members, management, and staff.

**12.19** The corporate mission statement and high-level strategic objectives for the corporation were developed by management as part of their strategic planning exercise. The strategic plan was approved by the board of directors. At the time of our audit, it had not been formally approved by the shareholders.

**12.20** Under the current governance structure, the “directing minds” of ALC are the four Ministers responsible for the four provincial shareholders, not the board of directors.

**12.21** The roles, responsibilities and accountabilities of the board of directors have not been documented.

**12.22** The division of responsibilities between management and the board of directors has not been documented.

**12.23** Board members have traditionally been senior public servants from the four shareholder provinces.

**12.24** Current directors cannot meet the standard of performance relating to independence as required in the Canada Business Corporations Act.

**12.25** The two New Brunswick board members are in a conflict-of-interest situation because they also serve on the board of ALC’s regulator in the province, the New Brunswick Lotteries Commission.

**12.26** The board has not developed a high-level policy framework that provides guidance to management in areas of concern to the board.

**12.27** Current reporting by management to the board does not address the degree of achievement of non-financial strategic objectives.

**12.28** ALC’s annual report does not provide performance reporting information that would allow the reader to assess the degree to which the corporation has met its corporate strategic goals, and therefore its mission.

**12.29** It is important to note that while we make a number of observations and suggestions for improvement relating to governance practices at ALC in this chapter, nothing was identified during our work

which would directly impact on or cause a loss of integrity or credibility related to the quality of the gaming products that are being delivered by the Corporation on behalf of its shareholders.

Exhibit 12.1  
Atlantic Lottery Corporation  
Findings

<b>Criteria</b>	<b>Criteria Assessments</b>	<b>Observations</b>	<b>Key Suggestions / Recommendations</b>
<p>There should be a governance structure and process in place and operational for the Corporation, complete with guiding principles/values and a dispute resolution mechanism.</p>	<p>Criterion met</p>	<ol style="list-style-type: none"> <li>1. There is a governance structure and process in place.</li> <li>2. A list of corporate guiding principles exists.</li> <li>3. There is no code of conduct in force setting standards of behaviour for board members, management, and staff.</li> <li>4. Basic dispute resolution mechanisms have been established in the corporate bylaws.</li> </ol>	<ol style="list-style-type: none"> <li>1. The board should ensure that appropriate comprehensive standards governing board, management, and staff behaviour are adopted for ALC. (See R10 in the shareholder's audit report)</li> </ol>
<p>The Corporation's mandate, mission, goals and objectives should be clearly and concisely defined, properly approved and reflected in its strategic priorities and operational activities.</p>	<p>Criterion met</p>	<ol style="list-style-type: none"> <li>1. The corporate mandate for ALC is defined in the shareholders' agreement and reads as follows. <i>"The Atlantic Lottery Corporation, a body corporate incorporated under the Canada Business Corporations Act, is designated as and hereby becomes an agency of Her Majesty in right of the province of New Brunswick, ... for the purpose of conducting and managing lottery schemes in each of those Provinces and other Provinces."</i></li> <li>2. The corporate mission statement and high-level strategic objectives for ALC were developed by management and reviewed and approved by the board. We feel that it would be more appropriate for the board to take a leadership role in developing the corporate mission and high-level strategic objectives for ALC. They should also ensure that all four shareholders agree with the corporate mission and strategic goals. In an environment of performance reporting, the board has a vested interest in ensuring that strategic objectives are complete, measurable and therefore useful in evaluating the degree to which ALC has achieved its mission.</li> </ol>	<ol style="list-style-type: none"> <li>1. The board should assume responsibility for the development and regular review of the corporate mission statement and high-level strategic objectives for ALC.</li> <li>2. The board should seek formal shareholder approval of future mission statements and high-level strategic objectives developed for ALC. (See R5 in shareholder's audit report.)</li> </ol>

Exhibit 12.1 - cont.  
Atlantic Lottery Corporation  
Findings

<i>Criteria</i>	<i>Criteria Assessments</i>	<i>Observations</i>	<i>Key Suggestions / Recommendations</i>
<p>The roles, responsibilities and authority requirements or limits of the Board of Directors and management should be defined, understood and adhered to.</p>	<p>Criterion partially met</p>	<ol style="list-style-type: none"> <li>1. The “<i>directing mind</i>” of a corporation is the individual or group who has the power to set key policies for the corporation and is ultimately accountable for achievement of the corporate mandate. The “directing minds” of ALC are therefore the four Ministers responsible for the four provincial shareholders.</li> <li>2. The board of ALC is an administrative management board with some governing responsibilities, particularly in administrative areas. They are not a governing board because they are not the “directing minds” of the corporation.</li> <li>3. Corporate bylaws define the specific powers assigned to the board of directors by the shareholders of ALC.</li> <li>4. Various documents explain the day-to-day responsibilities of management.</li> <li>5. There is no documentary evidence of the four Ministers’ expectations of the board’s roles, responsibilities and accountabilities. Also, the board has made no attempt to document, in consultation with the “directing minds” of the corporation, its own roles and responsibilities. The board appears to act as another layer of management rather than an integral part of the governance structure of ALC.</li> <li>6. The lack of clearly documented roles and responsibilities for the board in turn creates difficulty in establishing the boundary between board and management roles. The board has made no attempt to document the division of responsibilities between the board and management, which leaves ambiguity in the relationship between the board and management.</li> </ol>	<ol style="list-style-type: none"> <li>1. The board members should, in consultation with the four provincial Ministers responsible for ALC, clarify their roles and responsibilities as directors and document them. As a minimum, the board should include the following items when defining its roles and responsibilities. <ul style="list-style-type: none"> <li>• The board should be the communications link between the corporation and the shareholders.</li> <li>• The board should be responsible for developing a high-level policy framework within which management may run the corporation.</li> <li>• The board should monitor and evaluate organizational performance and communicate their evaluation of that performance to the shareholder governments. The board should also take corrective action to improve performance where they deem it necessary.</li> </ul> </li> <li>2. The board should, in consultation with management, clearly document the division of responsibilities between itself and management and ensure that all parties understand and respect the division.</li> </ol>



Exhibit 12.1 - cont.  
Atlantic Lottery Corporation  
Findings

<i>Criteria</i>	<i>Criteria Assessments</i>	<i>Observations</i>	<i>Key Suggestions / Recommendations</i>
<p>The Board of Directors should be comprised of people with the necessary knowledge, ability, commitment, and independence to fulfil their responsibilities.</p>	<p>Criterion partially met</p>	<ol style="list-style-type: none"> <li>1. Board members have traditionally been senior public servants and that continues to be the case. Five of seven directors at the time of our audit were either deputy ministers or working at an equivalent level within government, including both of the New Brunswick representatives.</li> <li>2. The board of directors is comprised of people with the necessary knowledge, ability, and commitment to fulfil their responsibilities as board members.</li> <li>3. The Canada Business Corporations Act (CBCA), under which ALC is incorporated, sets standards of performance based on the assumption that directors have the ability to act independently in the best interests of the corporation. ALC directors are not able to act independently in all cases because they are not the “directing minds” of ALC. They must defer to the wishes of the responsible Minister in their jurisdiction where required. Therefore, current directors of ALC cannot meet the standard of performance in the CBCA.</li> <li>4. Two New Brunswick board members of ALC are also on the board of the Lotteries Commission of New Brunswick (LCNB), the provincial shareholder. As LCNB is charged with regulating gaming activity within New Brunswick, it appears that these directors are in a conflict-of-interest situation.</li> </ol>	<ol style="list-style-type: none"> <li>1. The conflict between the standard to which the board is held under the Canada Business Corporations Act and their ability to act independently due to the current governance structure should be resolved.</li> <li>2. The apparent conflict-of-interest of New Brunswick representatives on the ALC board of directors should be resolved.</li> </ol>

*xhibit 12.1 - cont.*  
*Atlantic Lottery Corporation*  
*Findings*

<i>Criteria</i>	<i>Criteria Assessments</i>	<i>Observations</i>	<i>Key Suggestions / Recommendations</i>
<p>Policies and procedures should exist and be operational for key areas or aspects of the Corporation's management and other activities.</p>	<p>Criterion partially met</p>	<ol style="list-style-type: none"> <li>1. The board has not developed a high-level policy framework, in consultation with the shareholders where necessary, that provides guidance to management in areas of concern to the board. Corporate policy is currently developed at the initiative of management.</li> <li>2. Management-level policies seem to address day-to-day operations on a reasonable basis.</li> </ol>	<ol style="list-style-type: none"> <li>1. The board should adopt a policy-based approach to governance, wherein the board develops a high-level policy framework that provides guidance to management in areas of concern to the board. Such a policy framework should cover the following areas. <ul style="list-style-type: none"> <li>• A list of high-level corporate strategic goals, along with an indication of the information that management must provide to the board. This information should allow the board to evaluate and report upon the degree to which strategic goals have been achieved.</li> <li>• Limitations on the range of acceptable management actions.</li> <li>• The relationship between the board and management, including their respective roles and responsibilities.</li> <li>• The process of corporate governance at ALC.</li> </ul> </li> </ol>

Exhibit 12.1 - cont.  
Atlantic Lottery Corporation  
Findings

<i>Criteria</i>	<i>Criteria Assessments</i>	<i>Observations</i>	<i>Key Suggestions / Recommendations</i>
<p>There should be sufficient, appropriate and timely information available and reporting on the Corporation's plans and performance, from both the financial and program perspectives.</p>	<p>Criterion partially met</p>	<ol style="list-style-type: none"> <li>1. The external auditor has issued unqualified audit opinions relating to financial statements provided in the ALC annual report.</li> <li>2. Management provides the board with regular financial reporting, including budget comparisons and variance explanations.</li> <li>3. There is an established annual planning and budgeting process. The board approves resulting plans and budgets.</li> <li>4. Management has not been asked by the board, and does not provide regular reporting that addresses the degree to which non-financial corporate strategic objectives have been achieved. Only two of the eleven corporate strategic objectives are addressed in management reporting to the board, and both are financial objectives.</li> <li>5. The 1997 annual report of ALC does disclose the corporate mission and strategic objectives, an improvement over prior years.</li> <li>6. The ALC annual report, the board's key accountability document, does not provide performance reporting information that would allow the reader to assess the degree to which the corporation has met its corporate strategic goals, and therefore its mission.</li> </ol>	<ol style="list-style-type: none"> <li>1. The board should consider if it continues to be in support of the current corporate strategic objectives of ALC. If so, it should ensure that it obtains sufficient appropriate information from management to evaluate the degree of achievement of the current corporate strategic objectives. If not, the board should rewrite the corporate strategic objectives to bring them into line with what the board feels is needed to achieve the corporate mandate. (See R14 in the shareholder's audit report.)</li> <li>2. The board should have the annual report enhanced to make it an ALC accountability document for the use of shareholder provinces and stakeholders. As a minimum, there should be a narrative explaining initiatives taken to meet each individual strategic objective and an analysis of the degree of achievement of the objective. However, a longer-term goal should be to develop and present a set of performance indicators that would allow the reader to objectively assess the degree of corporate success in achieving each strategic objective. (See R8 in the shareholder's audit report.)</li> </ol>

