TROPICAL DEPRESSION

by **John Sedgwick**

photographs by **Deborah Schwartz**

The will of a princess created the Bishop Estate, now worth billions. It was supposed to help educate the children of Hawaii. Instead, according to its critics, it is providing a life of luxury to its trustees and fueling the island's political machine.

THE KAMEHAMEHA SCHOOLS occupy a series of broad stucco buildings that rise, grade by grade, up the verdant hillside overlooking the sparkling towers of downtown Honolulu. This increasing elevation makes a fit symbol for the schools' lofty educational ambitions, and also for the mounting problems of their sole benefactor: the $15 billion-plus Bishop Estate.

Endowed by the will of a land-rich Hawaiian royal named Princess Bernice Pauahi Bishop, the Kamehameha Schools (the plural is vestigial, left over from when there were separate schools for boys and girls) are a point of rare pride for islanders. The schools are dedicated to providing a top-quality education to native Hawaiians, whose ranks have been drastically thinned by poverty and disease since the first colonists arrived two centuries ago. More than 3,200 students are currently enrolled, from kindergarten through 12th grade, and, remarkably, virtually all of them plan to go on to college. "For many Hawaiians, Kamehameha is the only hope they have of a better life," says Beadie Kanahele Dawson, the lawyer for Na Pua, a group of concerned Kamehameha alumni, faculty and students. "It's their one chance."

Those hopes, in the view of Na Pua activists, are now seriously endangered by a number of Hawaiian officials who were supposed to safeguard the schools but seem to be plundering them instead. Front and center in the scandal are the five trustees of the Bishop Estate, whose sole purpose is to provide for the Kamehameha Schools. Incredibly, the trustees pay themselves around $900,000 a year apiece, believed to be by far the largest sum accorded to any nonprofit trustees in the nation. Although only one of the five has any direct experience in managing a large trust, the other trustees have taken it upon themselves to act not in a standard supervisory fashion, but as hands-on chief executives, carving up areas of the trust's business to run as their own private fiefdoms. Technically, each acts only with the others' approval, but in effect they have had something closer to free reign.

It is a mark of the abysmal failure of this arrangement that, on the investment side, none of the trustees seems even to know the full value of the estate's holdings, making it impossible to evaluate the trust's recent financial performance. The trust owns fully 8 percent of the state of Hawaii, or 368,000 acres, making it the largest single landholder on the islands. Its portfolio also includes a bank in China, a savings and loan association in California, 300,000 acres of timberland in Michigan, substantial holdings in Columbia/HCA and 10 percent of the New York investment firm Goldman, Sachs & Co.

What all this adds up to is anybody's guess; official estimates range from $5 billion to $35 billion, with $15 billion to $20 billion the most likely. "We've never done a valuation of lands and assets," admits Oswald Stender, the one trustee who, as former CEO of the Campbell Estate, is routinely singled out as qualified for the position, and who has spoken candidly about trustee abuses. "We really didn't think we needed to know." In 1993, the Bishop Estate's annual report offered a $150 million land valuation that was, for the most part, 30 years out of date. Since 1993, the report has offered no financial disclosures of either assets or income. It may be no coincidence that between 1993 and 1996 the trust lost a staggering $242 million.

A better understanding of the estate's finances might well have come in handy for the trustees as they made critical decisions about the schools' future. Indeed, the "lead trustee" for educational matters, a former gym teacher named Lokelani Lindsey, cited budgetary constraints when, in 1995, with the consent of her fellow trustees, she summarily cancelled Kamehameha educational outreach programs that employed 170 teachers and served more than 30,000 Hawaiian children and adults.

Lindsey, around whom much of the controversy has centered, also convinced the other trustees to install a new vice president who unofficially reports to her, thereby stripping the schools' longtime president of many of his

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A REPORT ON THE SCHOOLS DECRIED THE "DYSFUNCTIONAL GOVERNANCE" AND "PERVERSE TOP-DOWN DECISION MAKING" OF THE TRUSTEES AND THE OVERALL "CLIMATE OF FEAR AND INTIMIDATION" THEY HAVE CREATED.

responsibilities. She directed the curriculum office to have the kindergartners memorize the names and faces of the five trustees, and she has involved herself in such minutiae as selecting the dictionary to be used in teaching the school's Hawaiian language courses and even deciding on the lettering on a school T-shirt. The most recent review from the Western Association of Schools and Colleges accrediting commission praised the academic performance of the school but sharply questioned its management, decrying the "dysfunctional governance" and "perverse top-down decision making" of the trustees and the overall "climate of fear and intimidation" they have created. When the confidential report was published in the local newspapers, Lindsey launched an investigation, enlisting a team of lawyers to question certain faculty members to find out who leaked the story to the press.

Princess Pauahi, who married a penniless New Yorker and declined the throne of her kingdom, wrote a will endowing the Bishop Estate that was regarded for decades as a model of thoughtful propriety.

PRINCESS PAUAHI'S WILL, WHICH DIRECTS HAWAII'S SUPREME COURT JUSTICES TO SELECT THE TRUSTEES, INADVERTENTLY PUT HER ESTATE AT THE MERCY OF A POLITICAL SPOILS SYSTEM.

Such a toxic combination of arrogance, incompetence and micromanagement did not go unnoticed, and the trustees are now being investigated to determine whether they have failed in their fiduciary duties, with potential charges against them ranging from reckless irresponsibility to criminal self-dealing. In one matter that Hawaii Attorney General Margery Bronster is currently examining, several 1989 trustees allegedly invested at least $2 million of their own money in a Texas methane gas venture in which the estate also had a stake. Eventually, the estate increased its investment to $85 million, although the estate's own lawyer called the deal a "disaster" and doubted the estate would recover more than $20 million. In a *Honolulu Star-Bulletin* essay called "Broken Trust" that first drew wide attention to the Bishop Estate troubles, the five prominent Hawaiian authors of the piece charged that the trustees might not have been tempted to put in so much estate money if they hadn't been concerned about their own. One of the authors, University of Hawaii Law School's Randall Roth, finds it especially troubling that the the estate has invested more in intricate oil and gas deals than in conventional stocks and bonds, when none of the trustees has any known expertise in that rather arcane area of investing. The chief attraction of such assets, Roth believes, could be that the details can be concealed from view, and there are no Dow Jones-like benchmark measures by which to grade the results.

Such secrecy is pervasive on the investment side of the estate's business. In another case, trustee Henry Peters negotiated on behalf of a group of fellow members of the Robert Trent Jones Golf Club in Virginia to purchase a portion of the club from the Bishop Estate. That deal, too, wound up in litigation, after Peters's partners became alarmed about the terms and discovered that Peters was, in effect, both a buyer and a seller. (The matter was settled, but the attorney general is nonetheless looking into the possible conflict of interest.) And in a third instance, according to published reports, Lindsey used Bishop Estate workmen to obtain permits for the renovation of her own private house on the north shore of Oahu. It was only after several newspaper articles and many complaints that she paid back the estate. The trustees may face formal charges before long; they continue to be scrutinized by Attorney General Bronster, the Internal Revenue Service, the probate court, an internal fact-finder and both Honolulu newspapers, each of which has run more than a hundred articles since the story broke last August.

"I don't think there has been another event in Hawaii in the last hundred years that has produced as much newspaper coverage in such a short period of time," Stender says wearily. "It's constant. The whole community has come unglued." And the trustees are starting to turn against each other, as Stender and another trustee have combined to demand the removal of Lindsey. Still, the five continue to meet together twice a week in their sumptuous offices, recently redone for $12 million, and gilded in glorious koa wood. "It's very awkward," says Stender.

WHEN PRINCESS PAUAHI WROTE HER WILL in 1883, many regarded it as a model of thoughtful propriety. The will sets out the principles of the trust fully and yet so concisely that they run just two paragraphs—short enough to fit on the frieze of the gorgeous memorial chapel that stands on the campus in her honor. It established her husband, Charles Reed Bishop, founder of the first Hawaiian bank, as one of the trustees, along with four other eminences. For several generations, that system worked largely as intended. How it ultimately came to be the source of such controversy shows that even the most farsighted testators can fall victim to unintended consequences.

According to Stender and others, the underlying reasons for the trustees' problems are twofold: the high rate of pay and the politicized selection process. Neither, alone, would have been enough to create such a scandal; together, they made it all but inevitable.

Princess Pauahi made no provision for her trustees to be compensated for their services. Few trustees are, after all, beyond the rewards of social status and public service, and sometimes an honorarium of $500 or $1,000 for attending a meeting. In 1928, however, the Hawaiian legislature passed a little-noticed law that allowed the trustees of charitable trusts like the Bishop Estate to receive a portion of the gross annual revenues in compensation, a portion that subsequently rose to 2 percent. It is unclear to what extent, if any, trustees of that era took advantage of this provision. By the 1970s, they were receiving $50,000 each, which may not have been excessive, considering that many of the trustees were devoting considerable time to the enterprise. The pay shot skyward in the 1980s, however,

The Bishop Memorial Chapel, which stands on the campus in Princess Pauahi's honor. The principles of the trust are spelled out on the frieze inside the chapel.

after the U.S. Supreme Court upheld the constitutionality of a Hawaiian land reform act declaring that certain homeowners have the right to purchase the land under their dwellings at market rates, even if the landholder does not wish to sell. The act forced the Bishop Estate to sell land as it had never done before. By now, it has unloaded nearly 40,000 acres. "That created a bunch of cash," Stender says—so much that even without taking the full 2 percent, each trustee soon received nearly $1 million in annual fees. And by forcing the trust to convert real estate to more liquid assets, the windfall created a pot of money for the trustees to play investor with.

Beadie Kanahele Dawson, a lawyer for Na Pua, a group of concerned Kamehameha alumni, faculty and students, is seeking legal standing for the organization to serve as a permanent watchdog of the Bishop Estate.

THE TRUSTEES CONTROL MORE PRIVATE LAND THAN ANYONE ELSE IN THIS STATE. IT'S FRIGHTENING. THEY CONTROL OUR ELECTED OFFICIALS," SAYS DAWSON.

The princely compensation did not escape the attention of the political establishment, which quickly recognized that the trusteeships were some of the juiciest political appointments ever to be dispensed by an American official. And here is where the law of unintended consequences came in: Princess Pauahi's will, which named the justices of Hawaii's Supreme Court as selectors of the trustees, inadvertently put her estate at the mercy of a political spoils system that, in the 1980s, was operating at full throttle. Unlike most states, Hawaii has never had a true two-party system, in which each party serves as a brake on the excesses of the other. Hawaii is also the only state that was once a monarchy, which may be a related fact. In any case, the Democrats, having been in power since mid-century, have taken to acting like bratty royals, concerned far more with extending their influence—by controlling, among other things, the Bishop Estate sinecures—than with serving the public.

Former governor John Waihee, for example, appointed all the justices, who in turn selected the current trustees in accordance with the princess's will. Waihee was accused by the "Broken Trust" authors of using the judicial appointment process to reward political allies with trusteeships. "It's a matter of power," says Dawson. "Political power for Waihee. The trustees control more private land than anyone else in the state. They control developers, they control banks, they control big business. Because they are so wealthy and so strong, they control the legislature. It's frightening, but the trustees control our elected officials in this state."

The "Broken Trust" authors claim that Waihee himself sought to be selected as a trustee after he had completed his governorship, though he denies this. In any case, he was not chosen, but ▶

the current list of trustees still reads like a who's who of the Hawaiian Democratic Party establishment: the former speaker of the house, Henry Peters (who actually started serving while still speaker); the former senate president, Richard "Dickie" Wong; a close Waihee associate named Gerard Jervis, who is former head of the House Judicial Selection Commission that helped choose the Supreme Court justices; and Lokelani Lindsey, a longtime Democratic Party activist. The sole nonpolitical trustee, Oswald Stender, was selected only after the justices were hopelessly deadlocked over two politically connected candidates. "None of them would vote for the other guys' guy, so they turned to me," Stender says. "They didn't even interview me."

The Bishop Estate trustees, from left: Richard Wong, Oswald Stender, Lokelani Lindsey, Gerard Jervis, Henry Peters.

THE OTHER TRUSTEES THOUGHT THAT [THE CRITICISM] WOULD GO AWAY," SAYS OSWALD STENDER, WHO HAS SPOKEN CANDIDLY ABOUT THEIR MISTAKES. "I SAID, 'IT'S NOT GOING AWAY.'"

In retrospect, it might have been better if the duly appointed trustees had responded to their windfall by thanking their stars and heading to the beach. Instead, they busied themselves in a frenzy of trust-related activity that seemed designed largely to justify their colossal paychecks. "The only way they could begin to get away with [their huge compensation] was to emphasize that they were paid the money for being CEOs," speculates "Broken Trust" author Roth. Even though Princess Pauahi's will specifically required all significant matters to be decided collectively, many of the trustees appear to have arrived at a tacit understanding: You go along with my pet project in the schools, say, and I won't oppose yours in investments.

Many Hawaiians knew perfectly well that the schools and the trust were being managed abominably, but they figured it wasn't their place to say anything. "It's a cultural custom," says Na Pua's Beadie Dawson. "We honor our institutions by honoring their leaders." There was also the concern that if anyone spoke out, the IRS might crack down by closing out the school's tax-free status.

The Bishop Estate trustees might well have escaped scrutiny altogether if Lindsey hadn't made so many enemies through her administration of the schools. Infuriated by her behavior, in the spring of 1997 a former Kamehameha teacher named Nona Beamer wrote a letter to the Supreme Court justices demanding Lindsey's impeachment. "If the Supreme Court has the power to hire trustees," she told reporters afterward, "they should be able to fire them, too." After she went public, some 700 Kamehameha students, alumni and teachers joined a solemn protest, marching two by two from the royal mausoleum, where Princess Pauahi is buried, to the Supreme Court's offices, and from there to the headquarters of the Bishop Estate, where they requested a meeting with the trustees, only to be ignored.

"The other trustees thought that [the criticism] would go away," says Stender. "I said, 'It's not going away.'" The marchers became the Na Pua organization, with Dawson as unpaid legal counsel. The "Broken Trust" essay appeared shortly thereafter, in August 1997. "We saw that what the Na Pua people were doing was a real triumph of the spirit, and we wanted to support it," says Randall Roth. That essay in turn provoked the new governor, Benjamin Cayetano, to direct his attorney general to investigate.

NOW, MORE THAN A YEAR LATER, reform is coming slowly. The Hawaii legislature has narrowly and reluctantly passed legislation that limits trustee compensation to a "reasonable" amount. Although the definition of reasonable was left open, the new standard will almost certainly bring the annual compensation well ▶

down from $900,000. The Na Pua group is seeking legal standing to act in the name of the beneficiaries of the trust, thereby establishing a permanent watchdog over an estate that had previously operated without any outside supervision. Matters at the Supreme Court remain cloudy. Four justices have relinquished their roles as selectors of Bishop Estate trustees, but it is not clear if power will shift to the probate court, as the justices intend, or merely revert exclusively to the fifth justice, Robert Klein. But even if all the justices give up the responsibility, they may not get off the hook. By law, the justices may be culpable under the "negligent hire theory," meaning that they could be held accountable for their carelessness in choosing such trustees. Ironically, the justices had always defended their role in the selection process by saying that they were acting solely in their individual capacity. This defense may come back to haunt them, for, according to the University of Hawaii's Roth, it could leave them unable to claim judicial immunity for any estate-related misdeeds.

The royal mausoleum, where Princess Pauahi is buried.

THE I.R.S. INVESTIGATION IS PROCEEDING SILENTLY, AND THAT MAY BE THE ONE FOR THE TRUSTEES TO FEAR. A NEW LAW ALLOWS THE GOVERNMENT TO GO AFTER TRUSTEES, NOT JUST A TRUST ITSELF, FOR BAD BEHAVIOR.

As for the investigation of the Bishop Estate trustees, it is proceeding at a pace that makes the Monica Lewinsky affair seem like swift justice. Just to give one example: The attorney general subpoenaed at least 16 boxes of basic tax records last October. The Bishop Estate trustees responded by challenging the subpoena in lower court. When that failed, they appealed to the state Supreme Court, which, under the circumstances, had to recuse itself and defer to an ad hoc collection of substitute justices, who eventually agreed with the lower court's ruling. The estate then delivered four of the sixteen boxes. "They were playing games on the rest of it," says Attorney General Bronster. Finally, in late June, the estate delivered 11 more, leaving at least one still unaccounted for. "And that was just one subpoena," says Bronster. How many subpoenas have there been? "Lots." Eventually, according to Bronster, the offending trustees might not only be forced out, but be required to return to the estate any payments the courts deem excessive, with possible surcharges for wrongful behavior. And, if it turns out that there was any illegal self-dealing, they may be subject to criminal prosecution as well.

Meanwhile, the IRS investigation proceeds silently, and that may be the one for the trustees to fear. For this could mark one of the first significant actions that the IRS has taken under the 1996 Intermediate Sanctions law, which allows them to go after trustees, not just a trust itself, for bad behavior. "Because we are large and national, I really believe the IRS wants to make an example of us," says Stender. The other trustees must have thought so too. Since 1995, the Bishop Estate has paid hundreds of thousands of dollars to former governor Waihee's law firm to lobby against the law, although it is hard to see how this move aids the estate's beneficiaries. Such activity, however, may reflect the general anxiety of trustees everywhere as they wait to see how the new IRS rules will affect them. (In a peculiar twist, U.S. Treasury Secretary Robert Rubin's objectivity has been called into question by a deal he made with the Bishop Estate. Rubin pays the estate several hundred thousand dollars a year to guarantee that ►

the value of his investment in Goldman, Sachs, where he used to be co-chairman, does not decline while he is in office. Rubin's ostensible aim is to remove his stake in the firm's performance, thereby eliminating any conflict of interest with his policymaking. But this has created yet another potential conflict of interest, given his authority over the IRS in the Bishop Estate case.)

There are many lessons here for trustees about the dangers of hubris, the necessity of respecting a founder's intentions and the indispensability of common sense. But one conclusion is overwhelming: Trustees must remain trustees, and not succumb to the temptation to become chief executives. The reasons are plentiful, and most are illustrated by the Bishop Estate fiasco. Mainly, if the trustees do become chief executives, as these trustees did, there is no one to fire when administrative matters go seriously awry, and thus no quick way to set them right. Trustees and chief executives provide critical balance to a nonprofit organization, just as directors and CEOs do in for-profit corporations. As supervisor and supervised, strategic thinker and tactician, each has a different perspective, and together they provide a kind of depth perception that neither one could achieve alone.

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In the spring of 1997, Kamehameha students, alumni and teachers marched from the royal mausoleum to the Supreme Court's offices, and then to the headquarters of the Bishop Estate, where they requested (and were denied) a meeting with the trustees.

CRAIG KOJIMA/LOS ANGELES TIMES PHOTO

The Bishop Estate and the Kamehameha Schools will ultimately be made whole again. But that will come only after terrible hardships for devoted loyalists of the school, and will be too late to help many other students who could not be served because of the budgetary shortfalls cited by Lindsey. If that outreach program had survived, 30,000 more Hawaiian schoolchildren would have been educated each year. Other Kamehameha schools might been built on other islands. The current campus might have been expanded so that, for example, more than just 8 percent of the preschoolers who presently apply can get in. Vocational programs might have been added for those students who aren't intellectually qualified for college. A lot, in short, can be done with assets in excess of $15 billion, and the lost opportunities are painful to enumerate.

In the end, maybe it all comes down to money, both for the trust and the trustees. In some cases this seems clearer than others. Lindsey and Wong bought million-dollar homes when they were appointed trustees. Stender points out, however, that others continued to live in the same houses, and drive the same cars. "Yeah," he says. "Jerry still drives the same Jeep he always did." If the investigations prove even a few of these damaging accusations, the errant trustees may not be able to hold on to their cars and houses, old or new, very much longer. ■

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