

## 23/06/2017 - 3 Investment Committee Remit and Membership

<b>Board paper title</b>		Paper 23/06/2017 - 3
Investment Committee Remit and Membership		
<b>Report by</b>	Stuart Ferguson	
<b>Job Title</b>	Head of Investment	
<b>Date of decision</b>	Board Meeting 23 <sup>rd</sup> June 2017	

<b>Summary</b>
<p>This paper proposes some minor changes to the remit and structure of the Investment Committee in light of the current LWARB investment strategy, which has moved away from direct funding to traditional infrastructure projects.</p>

<b>Recommendations</b>
<ul style="list-style-type: none"> <li>• To adopt the proposals for the Investment Committee structure as drafted below.</li> <li>• To delegate responsibility to the Head of Investment and Chair of Investment Committee to begin recruitment for new members.</li> <li>• To note that revised Terms of Reference for the Committee will be drafted for approval by the Board via a Written Resolution.</li> </ul>

<b>Risk Management</b>	
<b>Risk</b>	<b>Action to mitigate risk</b>
<p><b>Committee Composition</b>          The Investment Committee struggles to operate as it stands as a quorum of 3 is required and there are only 4 members, one of whose (Steve Hacking) contract is due to expire in September 2017</p>	<p>The proposals contained in this paper address this risk</p>
<p><b>Investment Sign Off &amp; Monitoring</b>          LWARB still has around £22m of capital to manage and a programme of new investments to be launched over the next 18 months. Effective governance must be in place to ensure that risk is understood and mitigated and investment returns protected and enhanced.</p>	<p>LWARB's investment programme requires effective governance – different options have been explored (summarised in this paper) and it is the conclusion of the team that an independent Investment Committee, reporting to the Board, is the most effective form of governance.</p>

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<p><b>Implications</b></p> <p><b>Legal</b></p> <p>The LWARB Order permits LWARB to establish any committee and delegate to it any authority it chooses. Other than prohibiting the Chair of LWARB to sit on a committee, the Order allows the Board to appoint any committee members it chooses. The proposals presented here do not therefore conflict with the Order.</p> <p>Terms of reference for the Committee and terms of appointment for external Investment Committee members will need to be updated.</p>
<p><b>Financial</b></p> <p>The current cost of Investment Committee members is £22k per year – the revised proposals would see costs reduce marginally to £17k.</p>
<p><b>Equalities</b></p> <p>None</p>

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<p><b>Why the paper is being presented</b></p> <p>The paper is presented in order to gain Board approval for the decisions detailed below.</p>
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<p><b>Background</b></p> <p>LWARB currently operates a two-tiered approach to investment activity approval. The Board has delegated responsibility for appraising and approving new investment decisions to an Investment Committee (“IC”) made up of Board and external members. When a new investment decision is approved by the IC then the Board has a period of 5 working days to “call in” the proposal for examination by the Board. Such a call in requires the approval of the Chair of LWARB and may only be applied where the decision made by the Investment Committee is out with the Board’s business plan and investment strategy. Where the IC believes the investment proposal sits on the edge or outside of LWARB’s investment mandate, they may also refer a decision back to the Board for approval. It is worth noting that since the establishment of the IC in its current format, none of the decisions made have been called in by the Board.</p> <p>The creation of an IC is standard governance practice for any investment body and fulfils a number of purposes, including to:</p> <ul style="list-style-type: none"> <li>• appraise investment proposals submitted by LWARB officers</li> <li>• challenge officers over investment structure and points of detail</li> <li>• provide expert analysis and feedback to help officers structure appropriate investments</li> <li>• ensure investment proposals sit within investment mandate and risk appetite of LWARB</li> <li>• identify and monitor portfolio risk and ensure objectives are being met</li> </ul>
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The specific LWARB structure was put in place because it was felt that elected members of the Board did not always have the specific financial and investment expertise necessary to effectively challenge and opine on proposals, with the “call in” mechanism providing a further layer of oversight to ensure that Board objectives were being met.

The LWARB Investment Committee structure currently comprises three LWARB members and three external members (however 2 of these positions are vacant) as follows:

*Internal Members:*

1. Melville Haggard
2. Cllr Nicholas Paget-Brown
3. Barbara Anderson

*External Members:*

1. Steve Hacking
2. Vacant
3. Vacant

Each of the members receives a payment of £3,000 per annum, with the exception of the Chair who receives £4,500 (in line with other remunerated LWARB committee members). Including payment of NI, and assuming the vacant positions are filled, the total cost of the IC to LWARB is £22k per year.

The quorum for the committee is one third of active members or four (which ever is larger) if there are six or more voting members. If there are less than six voting members, the quorum is three.

At present, as there are only four appointed members, in order for the committee to be quorate, there needs to be three quarters of the membership to make a quorum. This has proved difficult to achieve in practice over recent months. Cllr Paget-Brown has also indicated a desire to step down from the IC.

Over the past 18 months, the investment strategy of LWARB has changed significantly, away from a dedicated waste infrastructure project finance model, towards investing in early and growth stage trading businesses within the circular economy. LWARB officers recognise that the current Investment Committee remit and structure may not be the most suitable form of governance given this change in strategy. In addition, officers are aware that discussions have been held amongst Board members to gauge opinion of the most effective form of governance for LWARB activities.

The new investment strategy is geared toward fund investments and support for early stage/growth stage SMEs operating within the circular economy. Any governance structure should reflect this strategy with members having a strong grasp of commercial activity, startup investment, venture capital and private equity operating models.

### **Options**

The LWARB team has considered different options for governing investment decisions and outlined the advantages and disadvantages of each below:

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### Option 1 – Retaining the current IC structure and format

#### Advantages:

- Retains knowledge of members, who understand LWARB operations and objectives;
- Existing members have already input and understand LWARB's business plan and have agreed strategic direction;
- High level of scrutiny and challenge provided to LWARB officers when proposals are presented;
- Provides flexibility to assess proposals if a decision is required outside agreed meeting dates – additional support or guidance is also often provided outside formal meetings;

#### Disadvantages:

- Has proven difficult to achieve a quorum over the past 18 months given small pool of current members and resignations received;
- The Board may feel disenfranchised/ remote from investment decision making;
- Current skillset of membership may no longer be as relevant to investment strategy – for instance there is no specific circular economy expertise and limited early stage investment or entrepreneurial experience;

### Option 2 – Disbanding the IC with all decisions reverting back to the Board for approval.

#### Advantages:

- Single point of approval;
- Puts all decision making in the hands of Board members, potentially ensuring more stringent adherence to LWARB objectives;
- Gives confidence to Board members that they are aware of the detail of all investment activity undertaken;
- Should be fewer new investment decisions to be made now that LWARB has moved away from a direct investment model – proposals should already have been identified and included within the current business plan, approved by the Board.

#### Disadvantages:

- Board members do not always have the appropriate skills and experience to effectively assess investment proposals and challenge and support officers. This increases the risk that poor investment decisions are made leading to financial loss for LWARB. This has been exemplified by Cllr Paget-Brown asking to step down from IC as he no longer feels he has the requisite skill set;
- The Board meets infrequently, yet investment decisions, particularly those relating to portfolio companies, often have to be made at relatively short notice.
- If the Board was responsible for all new investment decisions and portfolio monitoring as well as discussing other strategic LWARB matters and standing agenda items, then Board meetings would need to significantly lengthen, probably upwards of 5 hours.
- The Board would inevitably have to delegate more responsibility to officers, which is not good governance practice and again adds risk;

### Option 3 – Retaining IC but amending & expanding membership and terms of reference to align with new investment strategy.

#### Advantages:

- Retains independent, skilled governance structure that the Board and officers can rely on

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- to provide considered oversight of LWARB investment activity;
- Ensures that the right skills are in place to effectively scrutinise, challenge and guide LWARB investment proposals;
- Realigns structure to reflect a greater focus on portfolio monitoring and future programme development;
- Provides greater certainty that a quorum can be met for meetings.

### Disadvantages:

- Board still may feel remote from oversight of investment decision making;
- Potential additional cost to LWARB if increase membership and retain same payment rate;

### Proposal

On balance, given the Board does not have a significant amount of commercial or investment experience, LWARB officers believe that retaining an IC is important, which would eliminate Option 2.. However, we also recognise that the Board is ultimately responsible for the financial performance of LWARB and investment decisions can have a material impact on the future viability of LWARB. Therefore our recommendation for a revised governance procedure is as follows:

1. IC to be retained with some amendments to remit and structure (see below)
2. For all **new** investment decisions (including requests for follow-on money to portfolio investments), the IC to continue to appraise and input into proposals as currently operates – if happy with the proposal, a 1 page summary recommendation to be provided to the Board, signed by IC Chair
3. Board to approve all **new** investment decisions
4. For all other **existing portfolio** investment decisions, the Board to delegate authority to the IC to appraise, input and approve those decisions, to ensure that any issues within a portfolio company can be dealt with quickly to protect value. However, should the decision result in a negative financial impact greater than £200,000 to LWARB, or if the decision, in the eyes of the IC Chair, could cause significant reputational damage to LWARB (such as a significant press story) then the Board must approve the IC's recommendation.
5. All decisions made over **existing** portfolio investments to be reported to the Board at the next scheduled meeting.

Essentially this proposal continues the existing governance procedure but with a positive Board approval process replacing the current call-in mechanism. In addition, some changes are proposed to the IC to ensure that it has the right skills to align with our circular economy focused investment strategy.

**Composition** – IC to comprise 3 Board members and 4 external members. Quorum to remain 4 members (unless the membership drops to below 6, when it will be 3 members) but to require at least 2 Board members and 1 external members. Observers from GLA and London Councils will continue to attend meetings.

**Internal Members** – Retain Melville Haggard (as Chair) and Barbara Anderson given their financial experience. Given the Chair of the Board is not allowed to sit on the IC, it is suggested that Cllr Mahfouz could be appointed given his role as Board circular economy champion. Chair

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of the Board to be provided with the IC papers in advance of the meeting and given an opportunity to feed in to the process.

**External Members** – Retain Steve Hacking and recruit a further 3 members with backgrounds in circular economy business, venture capital and early stage business support.

**Meeting Frequency** – IC to meet at least 4 times a year, with an ability to call ad hoc meetings (in person or remotely) should any investment decision be required in between scheduled meetings.

**Meeting Agenda** – Quarterly meetings to be more focused on portfolio management as few new investment proposals will need to be considered. IC paperwork to be amended by LWARB officers to more effectively capture and analyse relevant portfolio data.

**Costs** – payments made to IC members to be reduced to £2,000 each (£3,000 to the Chair) to reflect the lower number of expected meetings. Despite one additional member, overall cost to LWARB is reduced slightly to £17k including NI payments.