

Title of meeting:	Cabinet
Date of meeting:	26 March 2020
Subject:	Board Composition of Portsmouth City Council companies
Report by:	City Solicitor
Wards affected:	All
Key decision:	No
Full Council decision:	No

1. Purpose

- 1.1 This report sets out the basis upon which it is necessary and prudent to structure the Ravelin Group of companies. The basis for this is to provide an appropriate vehicle to enable company activity to occur that is efficient, legally accountable and transparent. The need to structure as suggested is to enable PCC to trade and generate profit beyond merely covering the initial cost of the activity.
- 1.2 Given the general power of competence under the Localism Act is not an absolute it is to be remembered that the ability to charge and or trade are constrained by sections 3 and 4 to the extent that the default position is to correctly structure a trading arm with this in mind.
- 1.3 Given that the position is that to trade effectively structures within a company construct need to be created the paper sets out below in detail the obligations and responsibilities of the Directors, Members and Officers in a liability and behaviour sense as if they are acting outside the PCC environment.
- 1.4 It is to be noted that the structuring suggested is aimed at protecting those involved and enabling onlookers to be satisfied that such companies as PCC have are being commercially run and effectively governed by the relevant elected Members involved.
- 1.5 The purpose of this report is to provide Members with advice on the board composition of companies to which Portsmouth City Council ("PCC") is the sole shareholder and in particular to approve the necessary constitutional internal decision making structures in terms of exercising the PCC shareholder function going forward.
- 1.6 To activate the dormant Ravelin Group of companies which were set up following a Council decision on 12 April 2016.

- 1.7 To draw from best practice guidance and expert external legal advice in terms of local authority companies generally as well as the legal responsibilities of company directors whilst seeking to operate in a collaborative and transparent manner.
- 1.8 Make recommendations on the governance structure of the Ravelin Group to enable the subsidiary companies to begin trading as well as providing advice relevant to all companies under the control of PCC so that Members may wish to decide (in light of the advice and recent experience) whether a protocol is to be developed to ensure consistency in the future management of PCC controlled companies by way of a shareholder committee structure.
- 1.9 This report sets out options in terms of PCC owned company director board membership composition, taking the following into account:-
- i. The expert external legal advice sought¹;
 - ii. Best practice generally
 - iii. The legal responsibilities of company directors as set out in statute and at common law;
 - iv. Potential conflicts of risk - members; and
 - v. Potential conflicts of risk - statutory officer.
 - vi. The membership of any board when PCC are seeking to rely on a particular legal exception pursuant to the Public Contract Regulations 2015 ("PCR's"); and
 - vii. The desire to work in a uniform, collaboratively and transparent manner across PCC as a whole.

2. Recommendations

- 2.1 It is recommended that:
- 2.2 The City Solicitor prepares and drafts a protocol (drawn from best practice and expert advice - attached at Appendix A and Appendix D) approved by the Governance and Audit Committee as a reference and guide for the overall corporate governance structure (i.e. company structure and board composition) relating to PCC owned companies and incorporated within the PCC's constitution.
- 2.3 In accordance with the protocol at Appendix A, that the following be approved in respect of the Ravelin Group companies:
- 2.4 A shareholder committee is established and is responsible for the oversight of the Ravelin Group companies and all other future company subsidiaries (where relevant):-
- 2.5 The Ravelin Group Shareholder Committee and draft terms of reference set out in detail in Appendix B are approved.

¹ Bevan Brittan - Board Composition advice at appendix A

2.6 Following the approval of the establishment of the Ravelin Group shareholder committee the previous delegations as contained within the cabinet decision meeting dated 26 February 2019 shall cease and the shareholder committee shall become the sole body exercising the shareholder functions of Ravelin Group companies.

2.7 Any amendments to finalise the corporate structure of the Ravelin Group and all relevant subsidiaries required to maximise the tax efficiency of the Ravelin Group and any other PCC companies is delegated to the City Solicitor in consultation with the Leader of the Council and the S.151 Officer.

3. Background

3.1. The Board composition of the companies owned and controlled by PCC has been comprehensively reviewed and considered in the context of :-

- (i) best practice (including advantages and disadvantages of appropriately experienced external directors on such board(s) in the Local Authority context);
- (ii) external legal advice in relation to potential conflicts of interest; and
- (iii) legal duties enshrined by common law and statute required of company directors hold.

3.2. PCC is currently the sole shareholder/wholly owns the following companies:

- Ravelin Property Limited;
- Ravelin Group Limited.
- Portico Shipping Limited;
- Victory Energy Supply Limited.

3.3. Following the Ravelin Group cabinet report dated 26 February 2018 a review of the current structure of Ravelin Group Limited ("Ravelin Group") and Ravelin Property Limited ("Ravelin Property") was carried out. The current board membership is set out below for reference.

Ravelin Hold Co

Tristan Samuels
Wayne Layton
Julian Pike

Ravelin Property

Tristan Samuels
Tom Southall
Julian Pike

3.4. It will be noted that when these companies were initially incorporated they included statutory officers and Members of the then administration.

4. The Shareholder

4.1. The shareholders are the owners of any company. In all current cases PCC is the sole shareholder of PCC owned companies. In relation to Ravelin, PCC is the sole shareholder of Ravelin Hold Co which in turn, is the sole shareholder of Ravelin Property and potentially any further subsidiaries.

- 4.2. Shareholders control a company through the appointment and removal of directors and certain statutory rights. In addition, shareholders may exercise control in accordance with rights given to them either in the articles or a separate contract with the company: "a shareholder's agreement".
- 4.3. The shareholder's agreement will put mechanisms in place to provide PCC with strategic control over the operation of the company through the right to approve a business plan and the requirement that certain listed decisions - "reserved matters". Reserved matters are those which are referred back to PCC and are not within the ability of the directors to decide upon. Whether or not the company is to be structured as a Teckal company or not (see section 10 below above) will have an impact on the reserved matters.
- 4.4. An example set of reserved matters which seek to ensure that control of the company is reserved to PCC as Shareholder are found within schedule 1 of the Bevan Brittan advice². For example:-
- i. The removal of any directors (including any terms on which such directors are removed from their office as directors) other than Council appointed directors;
 - ii. Adopting or amending the Business Plan of each respective Company and any in-year changes; and
 - iii. Agreeing or approving any other material services to be provided by the Company to a third party the total value of which the Board reasonably expects will exceed £100,000 [value used for example purchases only].
- 4.5. There are a number of ways upon which PCC can exercise the shareholder function. The premise is about the strategic control over the companies' activities and therefore the legal advice concludes it is usual for this function to be exercised by the Members of PCC. Depending on the level of control retained under the shareholder's agreement this could be through all shareholder decisions:-
- 4.5.1. going to Cabinet;
 - 4.5.2. **a committee of Cabinet (shareholder committee) being established to undertake some or all decisions (see point 5 below), or,**
 - 4.5.3. certain decisions being delegated to certain Members (e.g. portfolio holder) and / or senior officers.

Note - It could well be that the structure of the governance of any PCC company is a mixture of all three - noting that PCC (acting as shareholder) can delegate any decision making as per the above.

5. Shareholder Committee.

²Bevan Brittan - Board Composition advice - appendix A - schedule 1

- 5.1. The Cabinet has authority to undertake shareholder functions of Ravelin Hold Co and to supervise and approve any substantial matters of any subsidiary company. There is a need to ensure that decision making is both flexible and conducted in a timely manner whilst noting the need to conflict of interest issues.
- 5.2. The proposed governance structure for the Ravelin Group of companies is contained within appendix B. This sees a proposal of a new shareholder committee being established. This model could be equally applied to other PCC owned companies.
- 5.3. The shareholder committee shall consist of a majority from the Administration and 1 Member from all other parties, drawn from the elected Members of the Council. Subject to below, other Members of the Council (who are not directors of any of the companies concerned) may attend and vote as substitutes in the event that an appointed Member of the Shareholder Committee is unable to attend.
- 5.4. As the role of the Shareholder Committee is to advise and discharge executive functions in relation to company matters and to exercise the role of the Shareholder Representative, only Cabinet members can be members of the Shareholder Committee with voting rights, although other Cabinet members and non-Cabinet members can be invited to attend, without voting rights along with 1 member from each opposition group who shall be invited to attend who will not have voting rights.
- 5.5. The Leader will be the chairman of the Shareholder Committee and will have the casting vote in the event that a majority decision cannot be reached. A Vice Chair will be selected from the elected members of the Shareholder Committee.
- 5.6. The necessary quorum for the meeting will be no less than 3 elected and vote rights bearing Cabinet Members of the Council present.
- 5.7. Meetings
 - 5.7.1 The Shareholder Committee will meet as regularly as required to ensure proper exercise of its functions but not less than quarterly.
 - 5.7.2 The members of the Shareholder Committee may invite the Chief Executive, Section 151 Officer, City Solicitor, Officer of the Council or their deputies and any other persons as required who will be the advisors to the Shareholder Committee.
 - 5.7.3 It is anticipated that the directors of companies will be invited if their input is required to make an informed decision.
- 5.8. Administration
 - 5.8.1 The agenda of the meeting together with any supporting documentation will be provided to members of the Shareholder Committee at least 5 working days in advance. This notice period may be waived if the Chair of the Shareholder Committee so agrees.

5.8.2 The meetings of the Shareholder Committee will be minuted which will subsequently be approved at the next meeting.

5.9 It is proposed that following the approval of the establishment of the shareholder committee, the structure of Ravelin Group shall look as described in appendix B:

If approved, the role of the shareholder committee shall be as detailed in the terms of reference (appendix B) and summarised below:-

- Exercise shareholder function of Ravelin Group companies;
- Approve or reject business plans of Ravelin Group Companies;
- Monitor performance and financial delivery against business plans;
- Exercise decision making over Reserved Matters;
- Approve or reject appointment of directors.

6. The role of a director.

6.1. The role of the director does have some limitations placed upon it, as appointed directors will be in control of the operation and management of a company subject to the control of PCC acting as shareholder (as prescribed by the shareholders agreement) (see: shareholder at section 4 above).

6.2. Many of the duties of directors were not prescribed by statute but rather, have evolved through the courts and have become established in the body of case law. Including (but not limited to):-

- i. fundamental duty of all directors and those acting in a fiduciary capacity to act honestly and in good faith and in the best interests of the company and its members as a whole; and
- ii. a duty to exercise a reasonable degree of skill and care in any dealings between the company and third parties.

6.3. The companies Act 2006 codified such director's duties and sets out a statutory statement of duties - this is detailed at section 8 below. It should be noted that this is not a comprehensive list of duties and does not covers all duties that a director may owe to a company.

Size and composition.

6.4. There is no set size or composition of a board of any local authority owned company. The company purpose will affect the structure, including whether the entity is to be a 'Teckal' company or not (see section 10 below). The issues PCC should consider in respect of the board composition of each company include (but are not limited to):

- i. the appropriate mix of skills and experience required;
- ii. the extent to which any board will be made up of executive or non-executive members. Executive being those who are employees of the company, and non-executive being those not employed, being either officers or members from PCC and / or independent directors;
- iii. the required mix of skills and experience required;
- iv. the need to demonstrate sufficient control when required for a Teckal company (see section 10 below) independence if required to achieve non-contracting authority status).
- v. the potential conflicts which could hinder the effective operation of the board or present issues for individuals when acting within PCC.
- vi. The purpose and commerciality of the company. The membership of the board will need to comprise and to speak well with the market of the particular speciality (housing development etc.) to ensure fluidity in terms of responding to market needs.

6.4.1. The key terms of the letter(s) of appointment of directors, such terms will include:-

- i. The availability of the director - noting the requirements for frequent board meetings in the early trading phases; and
- ii. The need for flexibility in terms of last minute board meeting requirements in cases of emergency decisions during the early incorporation phase.

- 6.5. The Bevan Brittan advice note ³ sets out the key considerations which should be taken into account when looking at the relevant skills and experience of the board (see section 6 of appendix A). This should be reviewed on a case by case basis for any newly created company noting the objective and functions of the company.
- 6.6. The relevant skills and experience of each individual director needs to be reviewed against the company aims, purpose and functions (pursuant to the business case). Bevan Brittan provide the example of: "***if the property company is concerned with implementation of development projects the board should have individuals with skills and experience relevant to that function***".
- 6.7. In accordance with best practice, there should be a mechanism by which independent people selected through open recruitment should be considered for membership on any PCC owned company board on the basis of the specific skills, expertise and experience.

³ Bevan Brittan - Board Composition advice - appendix A

7. Local Authority Companies - structures - best practice guidance.

- 7.1. Deemed as "*one of the notoriously difficult areas of law*"⁴ is the issue of members and officers being tasked with decision making requiring the disclosure of interests in other external organisations (companies). This is apparent with issues arising out of a conflict of interest when persons are involved in a dual capacity - i.e. a member and/or statutory officer who is also a director.
- 7.2. Members and officers who are appointed to act for external companies must keep at the forefront of their minds that they will owe fiduciary duties to both PCC and any relevant other company. When acting for PCC - acting in the best interests of the Council, council taxpayers and the wider public interest. Equally if acting as a director of a company as an officer and/or member ensuring they are acting in the best interests of the company, meaning their shareholders, their employees and their creditors.
- 7.3. In January 2016, the Cabinet Office published *Guidance for Directors of Companies Fully or Partly owned by the Public Sector* attached at appendix C. This is a helpful note which highlighted the law⁵ regarding directors liabilities in terms of conflict and indemnity.
- 7.4. Following on from this *the Code of Practice (committee structure and officer example) developed by The Lawyers in Local Government Group* (attached at appendix D - ("the Code")) was drafted to assist local authorities to work their way through difficult issues arising when setting up a wholly and/or party owned company.
- 7.5. The Code sets out a detailed best practice approach to the practical implications of how a Council as a (shareholder) member of a company might make decisions relating to that company through a separate **Council shareholder committee** providing oversight from a shareholder's perspective of the company's business and take relevant decisions on "*reserved matters*". - see section 4.4 above.
- 7.6. The best practice guidance confirms (note the below in italics is taken directly from the guidance provided within Appendix D):-

The structure [described above] creates a governance process whereby, so far as appropriate under this Code's principles, the company is left to get on with its business. Following the UK Corporate Governance Code, the companies will utilise a unified board, with appropriate non-executive directors providing outside expert help and with board committees (such as an audit committee) to provide oversight and ensure delivery.

The Leader, in turn, will seek to inform the executive decisions and to hold the company to account by utilising a reflection of the company board structure in the form of a Shareholder Committee, including external expertise and sub-groups. The

⁴ Local authority Companies and Partnerships - practical handbook - Robert Hann

⁵ s.117 Companies Act 2006

*role of this group is to provide the necessary oversight from a shareholder's perspective that the parameters, policies and boundaries that the executive as the shareholder has established for the company are being adhered to. **In it, the Leader (or his or her appointee) remains the decision maker but the shareholder committee act as advisors in the making of those executive decisions.***

Such a Shareholder Committee is considered to be an effective means of governance of the companies. This is because it allows for decision making and discussion in an informed atmosphere, which also provides the executive with:

- *a mechanism to communicate the shareholders' views to the company; and*
- *a means to evaluate the effectiveness of the company board and the delivery of the company performance against strategic objectives.*

It is intended that the Leader (or his/her appointee) will make most decisions concerning the executive's role in respect of company interests at meetings of the Shareholder Committee (in a similar manner to the Leader's executive decisions made at various partnership boards and the health and well-being board).

It is envisaged that key decisions concerning the companies will, however, still normally be made at meetings of the Cabinet.

8. Members.

As advised by Bevan Brittan, whilst members can be directors of PCC owned companies, this can create conflict issues for members relating to:

- the Code of Conduct for Members; and
- the risk of decisions made by Members who are also directors of the company being challenged on the basis of bias or predetermination or bias.

8.1. Directors who are Members must disclose any potential conflicts of interests and observe the requirements of the Code of Conduct of PCC⁶ and a clear audit trail of this is necessary. Members acting as directors need to bear in mind (when undertaking their PCC role) to behave in ways which avoid any suggestion of bias or predetermination.

8.2. Whilst the Monitoring Officer ("MO") is potentially able (in limited and prescribed circumstances) to grant a dispensation which covers disclosable pecuniary interests⁷ this does not avoid always the potential of accusations of bias or predetermination.

8.3. It is difficult in practical terms for the member to deal with a matter and it lays both the member and PCC open to allegations of bias and potential challenge.

⁶ Localism Act 2011

⁷ Localism Act 2011

8.4. Directors owe duties and are personally liable to a company (under both statute⁸ and at common law - for example in relation to confidentiality). These duties are to:-

- Act within powers ⁹
- Promote the success of the company¹⁰;
- Exercise independent judgement ¹¹;
- Exercise reasonable skill, care and diligence¹²
- Avoid conflicts of interest ¹³;
- Not to accept benefits from third parties;¹⁴ and
- Declare interest in a proposed transaction or arrangement with the company¹⁵.

8.5. Members acting as directors may be faced with regular conflicts in relation to the above duties, in particular the duties to promote the success of the company, to exercise independent judgement, and to avoid conflicts of interest.

9. Officers.

9.1. The Bevan Brittan advice¹⁶ does conclude that it is generally easier to manage the conflicts for an "officer director" than for a Member as requirements around conflicts are usually contained in the contract of employment or implied at common law. As such, this is a key area that PCC must consider in terms of reviewing employment terms as well as the letter of appointment for directors. PCC can agree to (i) officers continuing to act despite potential conflicts; (ii) agree not to take action against them where they are required to act contrary to the interests of PCC due to their role as director; and (iii) agree to their remuneration as a director.

9.2. The conflict issue is still very apparent however, and there is a risk that officers who are also directors of PCC companies may (if they are involved in making decisions about the company wearing their PCC officer hat) be open to challenge that their decision is influenced by bias and/or by pre-determination (that they have made their mind up because of the company role and are not making the decision objectively and fairly).

9.3. The Bevan Brittan advice¹⁷ concludes that the risk is best mitigated by PCC **not putting Council officers who are responsible for material decisions relating to a company as directors of the company.** Furthermore it concludes and **advises against statutory officers (monitoring officer, s.151 officer and the Head of Paid Service) being appointed as directors as they may be required to undertake their statutory roles in relation to the company at some point which would raise difficult conflicts.** Subject to the objects of the company, this could in the future be extended to other 'statutory' directors such as Director of Children's

⁸ The majority consolidated within the Companies Act 2006 ("CA 2006")

⁹ s.171 CA 2006

¹⁰ s.172 CA 2006

¹¹ s.173 CA 2006

¹² s.174 CA 2006

¹³ s.175 CA 2006

¹⁴ s.176 CA 2006

¹⁵ s.177 CA 2006

¹⁶ Bevan Brittan - Board Composition advice - appendix A

¹⁷ Bevan Brittan - Board Composition advice - appendix A

Services, Director of Adult Services and Director of Public Health being directors of relevant companies.

- 9.4. It should be noted that PCC (acting as shareholder) has the greater degree of control and it is key to note the shareholders role to fully make any decision as to membership of any PCC company board.

10. Teckal.

10.1. The "Teckal" (named after the legal case) exemption allows for PCC to structure a company in such a way so that contracts can be awarded without a tender under the Public Contract Regulations ("PCRs")¹⁸ (i) by PCC to said company (ii) by said company to PCC and (iii) by one company to another. PCC may potentially be able to rely on this exemption if contracting with any of the companies in a way that might otherwise trigger an obligation to run a compliant procurement - i.e. a direct award. The PCR's prescribe a number of conditions which must be met in order for the company to benefit from the exemption, including:-

- PCC must exercises a degree of control which is similar to that which it exercises over its own departments (the control limb);
- 80% of the activities of the company are entrusted to it by PCC (the activities limb); and
- where there is no private participation in its capital.

10.2. If PCC wishes to use the Teckal exemption then the governance framework will need to be designed and implemented to ensure compliance with the "control" limb of the test, this will be prescribed within the shareholders agreement and include:-

- right to appoint and remove specified number of board directors;
- sign off a periodic business plan – this may be an annual plan or a multi-year plan updated on a rolling basis; and
- exercise control over key decisions through the requirement for unanimous approval of certain reserved matters.

11. Integrated Impact Assessment.

11.1. The contents of this report do not have any relevant equalities impact and therefore an Integrated Impact Assessment is not required.

12. Legal implications

12.1. The City Solicitor's comments are contained within this report.

¹⁸ Regulation 12(1) Public Contract Regulations 2015

13. Director of Finance's comments

13.1. There are no additional financial implications expected to arise from the recommendations contained within this report.

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Signed by:

Appendices:

- Appendix A- Bevan Brittan - Board Composition Advice
- Appendix B - Ravelin Group Shareholder Committee and draft terms of reference
- Appendix C - published Guidance for Directors of Companies Fully or Partly owned by the Public Sector
- Appendix D - Code of Practice (committee structure and officer example) developed by The Lawyers in Local Government Group

Background list of documents: Section 100D of the Local Government Act 1972

The following documents disclose facts or matters, which have been relied upon to a material extent by the author in preparing this report:

Title of document	Location

The recommendation(s) set out above were approved/ approved as amended/ deferred/ rejected by
..... on

.....
Signed by: