



VCT Webinar

Monday 17 August 2020, Noon

Ahead of the upcoming General Meeting and Annual General Meeting (“the Meetings”) of the VCT to be held on 28 August 2020, the Board would like to invite you to join a Webinar with Board members to discuss the proposed changes to the Investment Management Agreement and the Administration Agreement and the future direction of the VCT. The Webinar will be held at noon on 17 August 2020.

We will be addressing a selection of questions from shareholders which have been asked in advance. If you have any questions you would like to raise with the Board, please add these to your response when confirming your attendance, the deadline for which is 5pm on Wednesday 12 August 2020.

Please let me know if it is your intention to join the Webinar and please submit your questions by emailing me at Terry.Back@edge.uk.com.

We are using the Zoom video service and the details for the call will be emailed to you when you inform us that you will participate.

Background Paper

1. Background

Much has happened at the Company since the Annual General Meeting (AGM) at the end of August 2019. In the year leading up to that AGM, your Board had been in ongoing dialogue with the Investment Manager about the future of our investment in Coolabi Group Limited (“Coolabi”). Both the Investment Manager and the Board were conscious that approximately 70% of the VCT’s value comprised its investment in Coolabi. This concentration was significant because Coolabi, although a profitable business, was still investing more cash into its intellectual property assets than it was generating from its operating activities. Were this to continue, Coolabi could have an ongoing funding requirement which, because of State Aid rules, the VCT could not satisfy.

Before the last AGM, Coolabi and the Investment Manager had already completed a selection process for the appointment of an adviser to consider the future strategic opportunities open to Coolabi, including an outright sale of the business, although we were unable to discuss this at that AGM.

At that meeting, although over 94% of votes were not cast, c.3.75% of the remainder voted against the reappointment of three of the Directors, leaving myself as sole Director. Motions were also voted down on the reappointment of Auditors (3.25%) and the adoption of the Directors’ remuneration report (3.67%). In the weeks following the AGM, I contacted a number of shareholders to better understand the reasons behind the voting at the AGM.

‘I’ class shareholders in particular told me that their votes were a protest at what they saw as apathy on the part of the Board in the face of a planned exit share class with a single significant investment showing no signs of disposal and, what they considered, excessive management charges being levied on them. Both points had merit; the first we had addressed, but I was not at liberty to discuss it; the second was already under consideration.

In the middle of September the Investment Manager informed me that it had negotiated a sale of the VCT’s £1m ‘H’ class holding in DeltaDNA for £4.73m (a disposal which, incidentally, contributed to the ‘H’ share class having the second-best performance of any VCT share in 2019).

As sole Director at the time, under the Company’s governance documents the Board was not quorate and I was not authorised to approve this deal.

Having spent the previous two weeks in discussion with shareholders, and having considered their views, I decided to ask Sir Robin Miller and Lord Howard Flight to accept reappointment to the Board pro tem. My reasons included to (a) have a quorate Board to approve the DeltaDNA transaction, (b) complete the work that the Board had started on cost reductions and future strategy, (c) provide the corporate history and memory predating my more recent appointment, and (d) assist in finding a new independent director to join the Board.

At that time I said an additional director would be appointed to the Board as soon as possible, someone demonstrably independent of the other Board members and the Investment Manager and with a good knowledge of the VCT sector - thereby bringing a fresh and knowledgeable eye to the consideration of the Company's future.

Having taken soundings with the Company's advisers and a sample of the Company's shareholders who voted at recent AGMs, during late September and October 2019 we carried out a search process for a new director. We appointed Sir Aubrey Brocklebank, a chartered accountant who worked for a Merchant bank initially in corporate finance and then Venture Capital. Sir Aubrey has sat on the board of eleven VCTs of which he has chaired nine, and several AIM listed companies of which he has chaired four. Especially against the background of the last AGM, I believe that the VCT was fortunate to recruit a director with Sir Aubrey's knowledge of the VCT marketplace, as well as his experience and sense of judgement. At the time of the announcement of his appointment in November 2019 we also announced that Lord Howard Flight would be stepping down from the Board at the forthcoming AGM.

At the same time I also told shareholders that the VCT would aim to hold a General Meeting prior to the Company's financial year-end on 29 February 2020 to consider a statement setting out the Board's decisions concerning the future of the Company, followed by a vote on whether the newly appointed directors continue in office. I apologise to shareholders for failing to meet this deadline. It has not been through any lack of effort by the Board in the interim period, but rather from allowing Sir Aubrey to get fully up to speed together with learning on my part how long the process would take to complete. We have also been engaged in a dialogue with ShareSoc for much of 2020. Although these discussions have been very helpful in reaching the position we are in now, they added considerably to the timetable of the process.

The fact that we are not living in ordinary times has also been a significant factor in the delay.

Also in November we announced that following a tender process we had appointed UHY Hacker Young as Auditor to the VCT.

From November 2019 the reconstituted Board has focussed on two matters to be the subject of the Meetings - future strategy and cost control, discussed in more detail below.

In December 2019 the Board commenced discussions with a number of other investment managers to see if there was a practicable alternative to the current manager. These discussions led to a formal tender process at the conclusion of which the current investment manager was reappointed under a heavily revised contract, subject to shareholder approval.

2. The Future of the Company

The Board has considered a wide ranging number of options open to the VCT. At the heart of every discussion has been the safeguarding of shareholders' interests and growth of shareholder value. The options considered have included a merger of the VCT with other VCTs, transformation of the VCT into an Investment Trust (to free us from State-Aid shackles and permit institutional investors to join our shareholder base) and the liquidation of the VCT. Each has involved discussion around the aspects of risk, commercial considerations and taxation factors and each was rejected as not being in the current best interests of shareholders.

Although shareholders in the same VCT, the interests of the 'H' and 'I' shareholders are not completely aligned and the Board intends to adopt the following strategy for each of the share classes in the future:

'I' shareholders - as a planned-exit fund, there is an imperative to realise our remaining two investments in the 'I' class. The smaller investment, Mirriad, is AiM listed, relatively insignificant in size and should be easy to realise. The Board is therefore focussed on the Coolabi investment.

We aim to maximise the value of the Coolabi investment through a successful realisation. When considering alternative investment managers, we concluded that none of them had the skills and contacts of Edge Investments in respect of a sale process and that a change of manager could seriously jeopardise the chances of a successful sale process. Since the appointment of an independent adviser a number of sale enquires have been received, two of which were generated by the Investment Manager, which is working closely with the independent adviser.

Whilst a disposal of our Coolabi investment in the short term is desirable for the VCT, it is by no means certain it will happen this year. Consequently, it is also important to control future costs to shareholders in respect of 'I' share management fees which could otherwise diminish value over time. This has been achieved by the reduction to a **zero-cost** management fee from the end of the Company's current financial year, agreed with the Investment Manager.

This reduction requires shareholder approval.

The Board is in regular contact with the Investment Manager in respect of developments on Coolabi and will continue to be so until the realisation of the 'I' class.

'H' Shareholders – the Board believes that the 'H' class funds are invested in companies that could deliver some good cash returns in the short to medium term. At least three of the eight investments currently held are capable of being disposed of in the coming 1-3 years.

The Board intends to continue to pay annual dividends in respect of the 'H' class, initially at an annual rate of 4p per share. Where disposals are made giving rise to significant gains, the base dividend level will be enhanced in line with the Company's stated policy on dividend distributions.

The Board believes that it is in shareholders' interests for the Investment Manager to continue to co-invest alongside Edge Creative Enterprise Fund, a fund also managed by Edge Investments. This arrangement (under which four of the 'H' share class' investments have already been made) has three distinct advantages for the VCT: it provides access to an investment management team that is highly experienced in the sector, it gives access to very significant deal-flow and gives it the ability to invest in opportunities that would otherwise be well above its financial range.

Following the repayment of the 'I' class of shares, the Board wishes to raise further share capital for the 'H' class on a regular basis to provide further funds for investment. The Investment Manager shares this desire and believes that there will be significant opportunities for further investment in the sector over the coming years as the country comes out of the recession arising from the Covid-19 pandemic.

The Board wishes to reintroduce a share buy-back facility for the 'H' shares as soon as is practicable.

Costs – The Board has examined all of the costs incurred by the VCT. The highest single cost (2020: 44% of total) is the investment management fee. Under the new contract proposed by the Investment Manager, the 'I' share cost reduces to zero as from 1 March 2021. The 'H' share fee remains the same at 2.25%.

Another significant historic cost for the VCT has been the Administrative Services cost. In the current year this amounts to just under £325,000. As a consequence of the tendering process we undertook, with effect from the beginning of the next financial year this is reduced to only £50,000.

This reduction requires shareholder approval.

Further details of the proposed new contract will be set out in the circular to shareholders. The total (including VAT) investment management and administration cost for each of the three years ended 28 February 2019 - 2021 was £1,125k, £944k, £864k respectively. This is estimated to reduce to £246k for 2021; an overall drop of 78% across the four years.

The Board has also effected savings across expense categories other than those paid to the Investment Manager. We have estimated that the total (including VAT) payable for each of the four years ended 28 February 2019 - 2022 is £385k, £319k, £242k and £198k; an overall drop of 48% across the four years

A full analysis of costs is set out below:

y/e 28 Feb:	actual 2019 £'000	actual 2020 £'000	budget 2021 £'000	budget 2022 £'000
management fees				
H class	159	126	171	186
I class	595	437	305	-
total management fees	754	563	476	186
directors fees	69	65	61	53
cosec & accountancy	88	79	60	30
administration	309	317	323	50
audit	46	35	29	29
VCT status advisory	11	9	9	9
print & stationery	31	29	24	24
other	89	51	69	29
irrecoverable VAT	113	115	103	34
Total	1,510	1,263	1,154	444

The Board - As part of the cost review, the Board also considered the composition of the Board. Given the completion of our work and the relative complexity of the business going forward, we believe that the Company only requires three Directors.

The resignation of Lord Howard Flight brings the Board down to this number and although we will miss his knowledge and experience in the VCT arena, we believe that Sir Aubrey Brocklebank has brought a similar skillset to the Board.

In conjunction with our plans for the future of the 'H' class of shares, we have invited Sir Peter Bazalgette to join the Board. Sir Peter has a wealth of experience in the Creative Industries. and will replace Sir Robin Miller, who has signalled his intention to step down from the Board after a short handover period.

Lord Flight and Robin Miller have between them given over twenty two years of service to the Board and I would like to record my appreciation for the help and assistance that I have received from them in completing the cost and strategic reviews over the last year.

Although this completes our proposed Board transitions, following on from our discussions with ShareSoc we have also invited Robin Goodfellow to join the Board, to assist it with the process of realising the remaining I Share class assets. Robin brings considerable VCT experience from his other appointments. During our discussions he was diligent, proactive and decisive and we welcome him to the Board.