

Report to: **Council**

Date: **27 March 2018**

Title: **Commercial Property Acquisition Strategy Update**

Portfolio Area: **Cllr Philip Sanders, Leader of the Council,
Strategy & Commissioning**

Wards Affected: **All**

Relevant Scrutiny
Committee: **Overview & Scrutiny Committee**

Date next steps can be
taken: **After Meeting**

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Recommendations:

That Council APPROVE & IMPLEMENT the updated commercial property acquisition strategy as detailed in Appendix A.

1.0 Executive Summary

- 1.1 On 5th December 2017 Council approved the recommendations of a report entitled "Commercial Property Acquisition Update". This agreed borrowing of up to £37.45m to implement the adopted updated strategy.
- 1.2 This report seeks to update Members on that decision and recommends updating the strategy in light of the Council's business rates pilot status and the recently issued MHCLG guidance in relation to prudential borrowing and investment.
- 1.3 Appendix A shows the recommended adopted strategy.
- 1.4 No purchases have been completed to date. As at the time of writing (16th March 2018) two bids have been accepted for off-market properties and these transactions are well advanced.
- 1.5 There are multiple objectives to this strategy, these are set out below:
- To help the Council continue to deliver and/or improve frontline services in line with the Council's adopted strategy & objectives.
 - To support regeneration and the economic activity of the Borough, the LEP area and the South West Peninsula (in that priority order)
 - To enhance economic benefit/business rates growth
 - To assist with the financial sustainability of the Council through yield being an ancillary benefit.
- 1.6 West Devon Borough Council is a business rates pilot area for 2018/19, which sets out the economic objectives of the pilot area.

Each acquisition will be assessed on its fit with meeting the objectives stated above, on a case by case basis.

- 1.7 It is important to note that the elected 'Invest to Earn' working group will consider each and every acquisition on its own merits and how it meets the Council's multiple objectives. Building a balanced property portfolio conforming to the proposed strategy could take up to two years. If approved, the Council will implement this strategy with the aid of commissioned property experts, whose costs are included within the financial projections.
- 1.8 The proposed strategy and/or implementation could be updated or ceased at any point prior to the full acquisition budget being expended, if Members determine that market conditions have deteriorated enough to make it financially unattractive. The 'Invest to Earn' working group retain the right to review the acquisition strategy at any time.
- 1.9 At this point, there is no recommendation to increase the first tranche of approved borrowing.

2. **Background**

- 2.1 On 25th July 2017 Council approved the recommendations of a report entitled "Commercial Property Investment". This agreed borrowing of up to £26.75m to implement the first tranche of the adopted Commercial Property Acquisition Strategy. On 5th December 2017 Council approved increased borrowing of up to £37.45m and increased the flexibility of the approved strategy.
- 2.2 This report seeks to update Members since that decision and recommends updating the strategy in response to recently published MHCLG guidance.
- 2.3 It is not proposed that the adopted strategy's upper spend limit of £75m or 1st tranche limit of £37.45m is updated. Appendix A shows the recommended changes to the adopted strategy. There are no additional financial implications of these changes.
- 2.4 The MHCLG (Government) guidance on Investments has stated that Councils will need to disclose several recommended indicators in their treasury management strategies going forward, for reports published after 1 April 2018.
- 2.5 The indicators that need to be disclosed after 1 April 2018 include an indicator on proportionality. This indicator assesses the amount of debt an Authority holds in relation to its Net Service Expenditure (NSE). The purpose of this indicator is to allow the reader to assess how proportional a Council's borrowing is, in relation to its Net Service Expenditure.
- 2.6 The level of borrowing for the Council's Commercial Property Acquisition Strategy has been approved at £37.45 million. This is a factor of 5.5 times the Council's Net Service Expenditure (which was £6.8 million in the Council's 2016/17 Audited Accounts).
- 2.7 There are no Government guidelines on what is an acceptable level of proportionality and it is for each Council to assess this

level themselves. The Council has carried out benchmarking on the debt levels of 200 Shire District Councils. The average debt level is £50.2 million amongst 200 Shire District Councils.

- 2.8 The Council will consider proportionality on a case by case basis for each acquisition as part of the decision making process, with information provided to the Invest to Earn Member group, the s151 officer, the Head of Paid Service and the Leader of the Council.

3.0 Commercial Property Acquisition

- 3.1 The Member 'Invest to Earn' working group have reviewed a number of potential acquisitions since the strategy was adopted last July.
- 3.2 No purchases have been completed to date. As at the time of writing (16th March 2018) two bids have been accepted for off-market properties and these transactions are well advanced and due diligence checks are being undertaken. Assuming satisfactory results, these transactions will move towards exchange and completion.
- 3.3 A number of other opportunities have been considered by officers and the 'Invest to Earn' group with two proceeding to unsuccessful bid stage. Officers continue to scour the market in conjunction with the retained advisors.
- 3.4 At this point, there is no recommendation to increase the first tranche of approved borrowing. As at the time of writing (16th March 2018), no borrowing has yet taken place in relation to this strategy. Borrowing will not be taken in advance of need to facilitate this strategy – borrowing will only be undertaken when a bid has been accepted, a transaction is progressing towards exchange and the s151 officer is confident that the results of the due diligence completed necessitates that borrowing.
- 3.5 It is the intention of this report to make clear the Council's multiple objectives of this strategy, in light of the recently published MHCLG guidance. Legal counsel has been undertaken as part of this process. The legal powers by which the Council can implement this strategy are unchanged.
- 3.6 The adopted strategy is shown in Appendix A. All other elements are to remain as per the current strategy (i.e. delegations / governance arrangements). There are no financial implications of this change.

4.0 Options available and consideration of risk

- 4.1. The overall objectives of this strategy are set out below:
- To help the Council continue to deliver and/or improve frontline services in line with the Council's adopted strategy & objectives
 - To support regeneration and the economic activity of the Borough, the LEP area and the South West Peninsula (in that priority order)

- To enhance economic benefit/business rates growth
 - To assist with the financial sustainability of the Council through yield being an ancillary benefit.
- 4.2. West Devon Borough Council is a business rates pilot area for 2018/19, which sets out economic objectives of the pilot area. The Council's 2018/19 budget includes income from the implementation of this Commercial Property Acquisition Strategy, as an ancillary benefit. Each acquisition will be assessed on its fit with meeting the objectives stated above, on a case by case basis.
- 4.3. Property acquisition is a dynamic area which generally does not sit well with traditional officer, committee and Council meeting schedules and structures. Decisions often need to be made quickly otherwise opportunities can be missed. Research shows that where Councils undertake this activity, there is an increasing level of delegation, enabling them to move quickly when properties come to market. This is implicit within the adopted and recommended strategy.
- 4.4. Members could opt to follow, amend or reject the recommendations.
- 4.5. Legal counsel has been undertaken as part of this process. The legal powers by which the Council can implement this strategy are unchanged from before.
- 4.6. The strategy looks to mitigate risks by setting specific criteria for purchases and necessary due diligence must be completed before officers and the 'Invest to Earn' group recommend any purchase.
- 4.7. The Council cannot remove all risk from this strategy, but the strategy is built in such a way to mitigate the risk as much as possible.

Proposed Way Forward

- 5.1 It is proposed that if the Council approve this report's recommendations, the new strategy will be adopted immediately.

6.0 Implications

Implications	Relevant to proposals Y/N	Details and proposed measures to address
Legal/ Governance	Y	<p>Advice on the relevant powers and appropriate vehicles for delivering these proposals has been sought from external specialist advisers and legal counsel. Legal counsel opinion has been obtained which sets out the various powers available to the Council, which supports the Council's proposed strategy as described in this report.</p> <p>This proposal is consistent with the Council's powers to borrow and invest under the Local Government Act 2003 and section 1 Localism Act 2011 (the general power of competence) and / or section 120 Local Government Act 1972 (power to acquire land).</p> <p>The Council is empowered to buy pursuant to section 120 of the Local Government Act 1972. Section 1 of the Local Government</p>

		<p>Act 2003 provides a power to the Council to borrow for the purposes of any enactment.</p> <p>Disposal of any of the acquired properties will have to be undertaken in accordance with the provisions of section 123 Local Government Act 1972.</p> <p>In order to lawfully implement the acquisition strategy, each proposal (including the funding strategy for purchases) should be reviewed as part of a decision to purchase or sell, and tested for value for money, and regulatory compliance.</p> <p>There is an overriding duty toward prudent management of risk, and officers, including the Council's section 151 officer owe a fiduciary duty in relation to given transactions.</p> <p>There is a duty on the Council to have regard to Statutory Guidance on Local (the New Guidance) Government Investments. As such, as part of the due diligence, officers consideration of each particular investment will need to include consideration of all the legal circumstances of the particular case, including, with respect to the utilisation of the investment power, whether having given due regard to the New Guidance, there is, exceptionally, scope for nonetheless borrowing in order to make the investments.</p>
Financial	Y	<p>The Council will purchase assets directly on balance sheet and therefore the direct costs of purchase and acquisition can be capitalised. This will include costs such as stamp duty, legal fees, due diligence and agency fees.</p> <p>When individual purchase decisions are made, a bespoke business case will be produced alongside a package of due diligence information to support the decision making process. The delegated authorities approving a purchase will need to be satisfied that any proposed acquisition not only delivers best value but also meets the criteria contained within the Commercial Property Acquisition Strategy and has proper regard to how the acquisition meets the Council's multiple objectives of the strategy.</p> <p>Part of the business case for each commercial property acquisition will be an assessment of the Internal Rate of Return (IRR) calculation.</p> <p>Any PWLB borrowing to fund the acquisition of commercial property is not secured on the property acquired.</p> <p>PWLB borrowing rates are fixed for the term of the loan. Individual borrowing decisions will be taken prudently in line with the Council's treasury management strategy and by officers within that function. The Council will not exceed its affordable borrowing limit to implement this strategy.</p> <p>The Council has adopted the CIPFA Code Of Practice for Treasury Management and produces an Annual Treasury Management Strategy and Investment Strategy in accordance with CIPFA guidelines.</p> <p>This amended Commercial Property Acquisition Strategy does not create a direct financial impact.</p>

Risk	Y	<p>The security risk is that the capital value of an acquired property falls. Whilst this would have an effect on the Council's balance sheet, this loss will only be realised if the Council chooses to sell the property and incurs a capital loss. The liquidity risk is the risk of failure of a tenant within one of the acquired properties.</p> <p>The yield risk is that the ancillary income derived from the acquired assets will alter during the life of the asset. This will be actively managed; with specialist agents commissioned to manage the asset and its tenants. Properties will only be acquired if they have a minimum of 5 years unexpired lease term and are located in areas deemed to be attractive for future lettings / sales, limiting the risk to the Council's portfolio.</p> <p>The Council already owns and operates a property estate valued at circa £20m. It therefore has experience of managing such an estate and can act as an intelligent client to fulfil the proposed strategy, with the aid of commissioned property experts. The cost of these experts has been included in the financial projections from this strategy.</p>
Comprehensive Impact Assessment Implications		
Equality and Diversity	N	Not Applicable
Safeguarding	N	Not Applicable
Community Safety, Crime and Disorder	N	Not Applicable
Health, Safety and Wellbeing	N	Not Applicable
Other implications	N	Not Applicable

Supporting Information

Appendices:

Appendix A – Recommended Commercial Property Acquisition Strategy & Criteria

Background Papers:

- Commercial Property Acquisition Strategy Update, presented to Council December 5th, 2017
- Investment in Commercial Property, presented to Council July 25th 2017
- Investment in Commercial Property, presented to Hub Committee June 20th 2017
- Statutory Guidance On Local Government Investments (3rd Edition)
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/678866/Guidance_on_local_government_investments.pdf
- Proposed Changes To The Prudential Framework Of Capital Finance
<https://www.gov.uk/government/consultations/proposed-changes-to-the-prudential-framework-of-capital-finance>