

Appendix A – SHDC Commercial Property Strategy

Overall Objectives:

The Council's commercial property strategy has multiple objectives as stated below:

- To support regeneration and the economic activity of the District
- To enhance economic benefit & business rates growth
- To assist with the financial sustainability of the Council as an ancillary benefit
- To help the Council continue to deliver and/or improve frontline services in line with the Council's adopted strategy & objectives.

Desired Outcomes:

The following outcomes are desired by the application of this strategy. Each acquisition or development opportunity will be assessed on its fit with meeting the objectives stated above and should deliver one or more of the following outcomes (benefits):

- ✓ Job creation or safeguarding
- ✓ Health & Wellbeing
- ✓ Town centre regeneration
- ✓ Tourism / Increased footfall
- ✓ Business rate growth
- ✓ Improved asset utilisation
- ✓ A minimum Net yield of 1%

This strategy will be achieved by acquisitions and developments within the South Hams District. This will include the focussed acquisition of existing commercial property assets and the development of new properties which are to be let to third parties.

Risk

- The risks of acquiring property may be mitigated through the acquisition of assets with secure, long income streams, although this risk will be weighed up against the social and economic benefits of acquisitions to support commerce and trade in the District
- Acquisitions are to be made in a careful and controlled manner, with specific analysis of risk criteria carried out in the 'due diligence' stage prior to the completion of each purchase
- The portfolio will be relatively risk-averse, targeting tenants of strong financial standing and minimum unexpired lease terms of four years at the date of acquisition. However, these criteria will be considered on a case by case basis and can be outweighed in order to meet the strategy objectives

Location:

- Wherever opportunities arise within the District, in order to acquire good properties which deliver the Council's multiple objectives stated above and are deemed an acceptable risk.

Tenant mix:

- Where possible, a mix of tenants will be sought to create a balanced portfolio
- The final decision over the appropriateness of any tenant would be reviewed at the time of acquisition
- SHDC owns a significant number of commercial units already within the District, mainly smaller units and tenants with relatively low credit ratings. This reflects the historic policy of supporting small start-ups which has proved successful and continues to be. Newer acquisitions are likely to be for larger units which may have single tenant occupancy.

Lease length:

- A minimum 4 years unexpired (mean unexpired term for multi-let properties) is preferable, however this is flexible if it helps achieve the strategy objectives
- For multi-let properties, a mix of lease expiry dates are preferred, thereby limiting void risk (unless the property is purchased with a view to re-development)
- Properties would preferably be let to sound tenants on leases with a preference for 'Full Repairing and Insuring' leases for single occupiers and through internal repair obligations and a service charge for multi-let properties. There may be overriding economic reasons to move away from this position and these will be considered on a case by case basis.

For all of the above:

The final decision over the definition of "good", "secure", "strong", "long", "careful", "controlled", "acceptable", "balanced" and "risk-averse" will be agreed between the property acquisition advisers (including legal due diligence) and the individuals delegated with the responsibility to conclude the acquisition of the properties. This discretion will be based on both the risk to the capital value of the asset and its' fit with the strategy objectives.

Yield:

- The Council will only acquire properties where the running cost does not require Council subsidy. Per acquisition, a minimum net yield (an ancillary benefit) of 1.0% is to be sought, after acquisition, management, maintenance, capital repayment and funding costs. However, the Council may opt to accept a net yield return of less than 1% if the benefits of job creation or safeguarding, tourism, town centre regeneration, business rate growth or effective asset utilisation are deemed more important than a purely financial return.

Value & Cost:

- Acquisitions and development initiatives will be funded using predominantly borrowing or any other unallocated or available Council reserve or capital receipt.
- The Executive and Council will consider the borrowing limit for the Strategy as part of the Medium Term Financial Strategy in September 2018. It is envisaged in December 2018, Full Council will need to approve a revised Treasury Management Strategy which would increase the borrowing limits of the Council (depending on the recommendations from the various bodies), to facilitate implementation of this strategy. As part of this report, the Council will also include the new proportionality indicators to address the Government guidance issued in February 2018.
- Larger lot sizes are favoured - smaller size properties have disproportionately higher management costs and expose the Council to greater property void risks, but the economic and trade benefits of buying smaller units may outweigh this.
- Acquisition costs are forecast not to exceed 7% (Stamp Duty Land Tax (SDLT) / Legal / Agents / Due Diligence). These costs are to be contained within the overall strategy budget

Funding:

- This is to be secured on a case by case basis on the most commercially advantageous terms available predominantly through borrowing or any other unallocated or available Council reserve or capital receipt
- The term will not exceed the expected remaining life of the property, but as a rule, the Council wishes to secure borrowing over a maximum 50 year term. Capital repayments will seek to repay a minimum of 50% of the capital value of any acquired property.

Tax Implications:

- Due to the Council holding the asset, it is not anticipated that there will be any corporation tax or income tax implications from this strategy
- Some properties may be VAT elected, meaning VAT must be charged to tenants. This will be dealt with on a case by case basis and will be covered by the due diligence connected with that acquisition. The Council is able to charge and recover VAT
- Capital Gains Tax would not apply to assets sold from Council ownership. This position may change if a company were to be used to hold the acquired asset.

Exit Strategy:

- The Council is not looking to actively trade commercial property within the first 5 years of ownership of any acquired property, however this is flexible if required to meet this strategy's objectives
- If it is determined that the most prudent action is to sell an individual asset, this will be considered on a case by case basis and will be acted upon in consultation with the 'Investment Group' Chair, Leader, S151 officer and Head of Paid Service
- It is proposed that all properties will be held as Council Assets. This may change if the Council were to set-up a trading company and it was found to be commercially advantageous for such a vehicle to hold the asset
- It is important to note that there would be early repayment charges if borrowing used to acquire a commercial property were to be repaid before the end of the loan term. However, Public Works Loan Board (PWLB) lending is not secured against property, so would not inhibit the asset being traded during the loan period. An alternative asset could be purchased (& held) with any sale receipt.

Governance Arrangements:

Acquisitions & Developments

Acquisitions and developments must conform to the adopted commercial property strategy. Any deviation from the agreed strategy will require Council approval.

Specialists will be commissioned to act on behalf of the Council to source suitable properties and manage the acquisition due diligence process.

Delegated authority to be given to the Head of Paid Service, in consultation with the S151 officer, Leader of the Council and Chair of the 'Investment Group' (or their deputy). Each receive one vote to proceed with purchase. In the event of a split decision, the S151 officer has the casting vote.

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 Investment Group Members, the s151 officer, the Head of Paid Service and the Leader of the Council.

Before a final decision to proceed with a development or acquisition is made, local ward members will be briefed and be able to share their views with the Investment Group.

The 'Investment Group' will determine its chair and will receive details of potential purchases from the Assets CoP. They will vote on whether to bring a potential purchase decision to the Head of Paid Service.

The same governance arrangements will be used to approve capital expenditure relating to any development projects and the subsequent granting of leases in excess of 15 years as recommended by the Assets CoP Lead, on a project by project basis.

Running / Review

If the management of the acquired assets cannot be managed in-house by existing resources, it will be outsourced to property professionals. The cost of this management is to be deducted before calculating the net yield. The Investment Group to receive regular reporting to confirm portfolio composition and performance. Regular reporting to Audit Committee as required.

Disposal

Once acquired, decisions relating to the ownership of any acquired properties will be dealt with in-line with the Council's constituted scheme of delegation.

Disposal will be considered if the portfolio breaches the approved strategy. Decisions to be made in consultation with the 'Investment Group' Chair, Leader of the Council, S151 officer and Head of Paid Service.

Resources:

The work to filter, appraise and recommend investment and development opportunities will be undertaken within the Assets CoP. This will be supplemented by specific consultant advice as required and associated costs built into the business case for each project. The Assets CoP has strong relationships with a number of local and national consultants who will be required to support the projects. Examples of this include (but are not limited to): CCD Properties (development specialists), Arcadis (building technical due diligence), Womble Bond Dickinson (legal due diligence) and Savills (commercial property investment advice).