

Report to Cabinet

Subject: Commercial Property Investment Strategy (CPIS)

Date: 19 March 2019

Author: Service Manager – Property

Wards Affected

Borough-wide.

Purpose

The purpose of this report is to:

- Obtain Cabinet support for the adoption by Council of the Commercial Property Investment Strategy (CPIS).
- Subject to approval by Council, to obtain authorisation from Cabinet to delegate decisions on the acquisition and management of Commercial Property in accordance with the details set out in this report.

Key Decision

This is a key decision. Because it is likely to result in the Council incurring expenditure which is, or savings which are significant having regard to the budget for the service or function concerned.

Recommendation(s)

THAT:

- 1) Cabinet recommends that Council approves the Commercial Property Investment Strategy (CPIS).
- 2) Subject to Council's approval of the Commercial Property Investment Strategy, Cabinet delegates authority to the GBC Chief Executive to approve commercial property acquisition under the CPIS in consultation with the Leader of the Council.

1 Background

- 1.1 Due to ongoing reductions in central government grant funding many local authorities have implemented strategies to generate additional income to support ongoing service delivery.
- 1.2 One of the strategies that GBC has explored to generate extra income is through investing in property. Members have made it clear that such investment will only be approved if it also satisfies the additional criteria of providing economic or social benefit to the borough and meets the objectives of the Gedling Plan. (The strategic background for carrying out this exploration is set out within the overarching GBC Commercialisation Strategy which was approved by Cabinet in October 2017).
- 1.3 Officers have determined that it is possible to invest in commercial property which will create the positive financial and economic or social returns required by GBC. Three different methods (Strands) of investing have been identified as meeting GBC's criteria. Each Strand is likely to produce varying degrees of financial, economic and social returns. This has led to the development of the appended CPIS which incorporates each Strand separately. The Strands are explained below:
- 1.4 Strand 1 – Tenanted Commercial Property - To enable commercial investment in tenanted properties where the objective is to increase business rates and/or rental income to GBC. The process for selecting a suitable property is detailed in Appendix A to the appended Strategy.
- 1.5 For this strand officers investigated whether it would be possible to invest in commercial, tenanted properties which would create significant financial as well as economic returns for the Borough. Such investment would have to be funded through borrowing.
- 1.6 GBC are able to fund statutorily compliant investment through borrowing from the Public Works Loan Board (PWLb) which lends at fixed rates over long periods. These fixed rates are currently preferential (c.2-3%) when compared to that which many commercial investors can access. When these costs are factored into the analysis, it is clear that some commercial property investments which meet the criteria of producing an economic or social benefit, could be acquired to produce a significant positive income over and above the repayment of debt and other costs.
- 1.7 However, advice from local property agents indicates that finding property investments that meet both the GBC economic and financial criteria of this Strand, and which are geographically located solely within the Borough, is unlikely. Success is more possible when the investment area reaches outside of the Borough boundary. The geographic areas which most closely meet the criteria, as they have the most links to the economic prosperity of the borough and are directly related to meeting the objectives of the Gedling Plan, are Gedling Borough itself and the D2N2 LEP area.

- 1.8 As the investigation showed that investing in tenanted, commercial property could satisfy GBC's financial and economic requirements, an amount of £5 million was included within the budget for this purpose and approved by Council on 5 March 2018. Expenditure can only be made from the budget for the purchase of property investments within the GBC borough or economic area, which will make a contribution to the delivery of Gedling Plan objectives whilst generating positive financial returns. The net proceeds of these returns are to be used to support GBC services.
- 1.9 The budget target for net income from £5m of commercial, tenanted property investments is £100,000 per annum. If, for whatever reason suitable investment opportunities are not found, the £100,000 will become an unachievable budget efficiency which will then have to be secured from alternative budget areas within the Council.
- 1.10 Strand 2 - GBC Owned Land - To enable investments through building on GBC-owned land to create financial returns. Similar to Strand 1, the objective will be to increase income, for example from business rates, rental income, or council tax. Also, where the business case is not viable on its own, to obtain external funding which will enable building on GBC land to create a positive return as well as economic growth.
- 1.11 For this Strand officers investigated developing extra industrial units on one of GBC's existing business parks. It was found that the process for building on GBC owned land cannot be formulaic and that each opportunity will have to be assessed on its own merits, and may be proved viable at the initial assessment and business case on varying rationale.
- 1.12 For this reason no budget has been put in place in respect of this Strand and budget approval will be requested through normal processes for each individual investment opportunity that receives approval under this Strategy.
- 1.13 Strand 3 – Acquire Commercial Property to Enhance - To enable the purchase of land or property to which value can be added to create a higher income than it is currently producing. The objective here is to increase business rates and/or rental income, or council tax income to GBC.
- 1.14 This Strand will be very much on an ad hoc basis depending what properties come onto the market. Opportunities for adding value to commercial property will not be formulaic and each case will be assessed on its own merits, and may be proved viable at the initial assessment and business case on varying rationale.
- 1.15 As with Strand 2, budget approval will be requested through normal processes for each individual investment opportunity that receives approval under this Strategy.

Powers to Invest/Acquire Property

- 1.16 The principal sources of power for local authorities to invest and acquire property include:
- the specific investment power set out under Sections 12 and 15 of the Local Government Act 2003;
 - GBC's specific land acquisition power under Section 120 of the Local Government Act 1972;
 - Section 2 of the Local Authorities (Land) Act 1963
 - acting pursuant to the council's general power of competence under Section 1 of the Localism Act 2011.

1.17 Local Government Act 2003

Section 12 makes it clear that a local authority may invest for any purpose relating to its functions under any enactment, or, for the purposes of prudent management of its financial affairs. Section 15 of the above Act does go on to say that a local authority must have regard to such guidance that the Secretary of State may issue. In February 2018 the Secretary of State issued new guidance on Local Government Investments ("the Guidance"), which widened the definition of an investment to include all of the financial assets of a local authority as well as other non-financial assets held primarily or partially to generate income. This and other guidance is considered in more depth below. The power of acquiring property as an investment is established however in the 2003 Act.

1.18 Section 120 of the Local Government Act 1972

Section 120 allows local authorities to acquire land, including buildings, for the purposes of (a) "*any of their functions*" or (b) "*for the benefit, improvement or development of their area*". There is a range of case law, in respect of this power which has clarified that the acquisition need not be within a Council's area provided the purpose of the acquisition is in line with the legislation.

1.19 Local Authorities (Land) Act 1963

Section 2 of this Act, gives authorities the power to, for the benefit or improvement of their area, erect any building and construct or carry out works on land. A local authority may also repair, maintain and insure any building or works erected, constructed or carried out under the power and generally may deal with any such building or works in a proper course of management. This power would support Strand 3 of the Council's Strategy.

1.20 Localism Act 2011

Section 1 of the Localism Act gives authorities the power to do anything that individuals generally may do. This power is not limited by the existence of other specific powers to the extent that they overlap with the power. Where this power is being exercised for a commercial purpose this should be done through a company. In relation to "commercial purpose" recent case law has provided some clarity around this namely the case of *Gordon Peters v London Borough of Haringey v Lendlease Europe Holdings Ltd* [2018] EWHC 192 (Admin) where Mr Justice Ouseley stated:

"Still less do I think that it was, it intended that doing "things" which might generate a profit or return for the council, a commonplace of many council activities related to its land assets, and which the council could then put to use

for its functions, should now be done and only lawfully done through a company, and indeed not through an LLP”

- 1.21 The specific powers in the 2003 and 1972 Acts provide the powers for investment in commercial property. Whilst GBC may be acting commercially by investing in property to try and achieve a return, which is a requirement of the authority's financial prudence, the CPIS is not solely about profit generation. The CPIS is about sound financial investment in properties that deliver economic benefits for residents, employment opportunities and generate return that can support Council services against a backdrop of ever decreasing financial support.

Statutory Guidance

- 1.22 Recently statutory guidance has been issued in relation to investments. Some of this is in response to large investments, in terms of percentage of the specific investing council's budgets that have been made outside of certain council's immediate geographic and economic areas.
- 1.23 Consideration has been given to the most relevant guidance and regulations including the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code and the CIPFA Treasury Management Code of Practice (the Code).
- 1.24 A summary of what has been considered is detailed below.
- 1.25 The Local Government Act 2003 (the Act) and supporting regulations requires GBC to 'have regard to' guidance issued by the Secretary of State.
- 1.26 In December 2017 changes to the Prudential and Treasury Management Codes brought about a major extension of the function of the S151 officer role - the required role for all councils under statute of responsible financial officer. Section 151 officers are also now responsible for:
- Preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management over a significant time-frame;
 - Ensuring that the capital strategy is prudent, sustainable and affordable in the long term, and provides value for money;
 - Ensuring that due diligence has been carried out on all treasury and non-financial investments, and is in accordance with the risk appetite of the authority;
 - Ensuring that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing;
 - Ensuring the proportionality of all investments so that the authority does not undertake a level of investment which exposes it to an excessive level of risk compared to its financial resources;
 - Ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long-term liabilities;

- Provision to Members of a schedule of all non-financial investments including material investments in subsidiaries, joint ventures, loans and financial guarantees;
- Ensuring that Members are adequately informed and understand the risk exposure taken on by the authority;
- Ensuring that the authority has adequate expertise, either in-house or externally provided, to carry out any non-financial investments;
- The creation of Treasury Management Practices which specifically deal with how non-financial investments will be carried out and managed.

1.27 In February 2018 the MHCLG Investment Guidance (the Guidance) widened the definition of an investment to include all the financial assets of a local authority as well as other non-financial assets held primarily or partially to generate a profit. This wider definition includes investment property portfolios as well as loans made to wholly owned companies or associates, joint ventures or third parties. The Guidance applies for financial years commencing on or after 1 April 2018.

1.28 The Guidance requires that strategies in relation to investments be approved by Full Council on an annual basis and sets out the disclosure and reporting requirements. Any mid-year material changes to such strategies will also be subject to Full Council approval.

1.29 The Guidance sets out the Government's position on borrowing in advance of need, which is that Authorities must not borrow more than, or in advance of their needs, purely in order to profit from the investment of the extra sums borrowed. The Council must have regard to the Guidance, but if exceptionally a local authority chooses not to have regard to the provision on borrowing and funds an investment activity purely to make a profit then the guidance requires them to explain the rationale. GBC is not intending to borrow to purchase investments purely in order to profit – it will only purchase investments that support the objectives of the Gedling Plan.

1.30 GBC has had regard to all relevant guidance in preparing the CPIS and is satisfied that the CPIS does not depart from this. The Council's Prudential and Treasury Indicators and Capital Strategy approved by Council on 4 March 2019 reflects the intention to invest in tenanted commercial property and demonstrates, as required, that approved investment levels are proportionate for Gedling in terms of the Council's overall capital investment and borrowing need and its impact on the revenue budget.

GBC standing Orders in relation to making decisions to invest in property

1.31 GBC's own Standing Orders for dealing with land provide that all purchases of land and/or buildings shall be the subject of a valuation report by the District Valuer or the Council's Director. In terms of authority to purchase commercial properties, this is an executive decision to be taken by the Portfolio Holder for Resources and Reputation, and depending on whether the value exceeds

£500,000 it will be a key decision. Key decisions are required to be publicised 28 days in advance of their making except in urgent situations where a procedure is prescribed.

- 1.32 The commercial property market moves at pace and commercial properties tend to be on the market for less than one month. In order to ensure that opportunities to acquire properties are not missed due to delays in decision taking, it is proposed as part of the CPIS that authority to acquire commercial properties is delegated to the Chief Executive in consultation with the Leader of the Council. Decisions to acquire properties will only be taken where the decision is in compliance with the CPIS.
- 1.33 The purpose of this report is to ensure that Council are content with the process of acquisition as laid out in the CPIS so that there is clarity around what types of property are being acquired and in what circumstances. Key decisions which involve acquisitions over £500,000 will still be publicised, however, depending on the timescales involved in the acquisition it may be that the urgency provisions are utilised. This involves reporting to the Chair of Overview and Scrutiny.

2 Proposal

- 2.1 GBC has devised the CPIS to provide a framework to enable investment opportunities that meet its requirement for financial returns, as well as other criteria including preference for a geographical location which is economically or socially beneficial to GBC, to be purchased and managed and if appropriate, disposed of. The CPIS complies with financial and legal legislation and guidance and provides a clear and robust process for the acquisition and management of commercial property. It is proposed that Cabinet recommend that Council approve the CPIS.
- 2.2 In order to ensure that commercial property acquisition can keep pace with the market whilst ensuring good governance it is proposed that subject to Council's approval of the CPIS, Cabinet approve the governance arrangements and decision making processes set out in the report, that the Chief Executive be authorised to approve in consultation with the Leader of the Council, the acquisition of commercial property in line with the CPIS subject to budget approvals being in place.

3 Alternative Options

- 3.1 Members could decide not to approve the CPIS. However, investment in commercial property requires the preparation of a Strategy to ensure openness and transparency in the Council's investments, and investment will only be undertaken where it is financially prudent to do so. Purchasing investment property could therefore become unworkable without having the CPIS in place and the planned income generation, currently estimated at £100,000 per annum, to support Council services and the Gedling Plan would be an unachievable budget efficiency target which will then have to be

secured from alternative budget areas within the Council.

- 3.2 Cabinet could not approve the proposed delegations as part of the CPIS and the decision making power would remain with the Portfolio Holder or Cabinet. However this may mean that opportunities to act quickly in property acquisition are lost as the administrative approval process may delay timescales.

4 Financial Implications

- 4.1 In respect of Strand 1, the Council has set a target budget of £100,000 to be generated from the £5m commercial investment. This is based upon a net 2% after taking into account any costs or loan repayments.
- 4.2 As the target budget of £100,000 is already established within the Medium Term Financial Plan, any decision to not invest the £5m in commercial investments that have a sound business case will have an impact on the long term finances of the Council, and would need to be addressed in future financial years as part of the Medium Term Financial Plan (MTFP).
- 4.3 There are currently no financial implications in respect of Strands 2 and 3 and any arising budget requirements will be the subject of future reports.
- 4.4 It must be noted that the £5m investment budget for Strand 1 is an approved amount for the purposes of the MTFP. However, similar to Strands 2 and 3, additional budgets may be requested on the production of satisfactory business cases and suitable financial returns.

5 Appendices

- 5.1 Appendix 1 - Commercial Property Investment Strategy (CPIS)

6 Background Papers

- 6.1 None

7 Reasons for Recommendations

- 7.1 To generate income to support council services.
- 7.2 To provide economic or social benefit to the borough and meet the objectives of the Gedling Plan.
- 7.3 To obtain relevant delegations to enable investments to be purchased at speed.