Property Acquisitions Strategy

1. Introduction

Given the prevailing financial climate of budget cuts and austerity, local government is being challenged to identify new ways to generate both revenue and capital funding streams to help bridge the gap between available funds and increasing service demands.

In common with all public bodies the Council has a property portfolio which is used to facilitate service delivery and deliver corporate objectives. The Council has been driving down holding costs through the rationalisation of its operational estate and the implementation of agile working. Whilst this process will continue to seek efficiencies, it is a process for managing costs rather than generating additional income. For that reason, it is now proposed that a more pro-active approach is developed in the form of a property acquisitions strategy. The purpose of this strategy is to:

- Provide a formal policy for the acquisition of investment properties that will derive a net return to the Council.
- Provide the governance arrangements
- Establish the criteria to support a proposed acquisition.

2. Objectives of the strategy

The strategy seeks to enable an additional income stream to the Council, either capital or revenue or both. In common with all investment opportunities, financial rewards have to be offset against risk. The objective therefore will be to minimise risk where possible, through a policy that seeks to spread acquisitions through all aspects of the commercial sector against evaluation and governance criteria discussed in this strategy.

3. Purpose of the Strategy

3.1 The purpose of this strategy is to formalise the commentary within the Councils Asset Management Strategy (AMS) and provide a robust governance framework. The AMS outlines the following:

The Estates team will actively seek opportunities for property investment where a Business Plan evidences:

- *Financial Viability – The income from the proposed investment opportunity needs to be able to fund the borrowing costs for the purchase of the asset and generate surplus income.*
- *Occupiers – Must have a strong covenant and a long leasehold interest that covers the length of any loan required to fund the purchase or be in a prime position which will reduce any void periods.*
- *Support local Whole Place Plans – e.g. acquisitions that would strengthen the viability of town centre*
- *Support Corporate Priorities*

3.2 The strategy will apply to all acquisitions of land and property, which for the purposes of this document is defined as:

Acquiring a legal interest[1] in land or property for investment purposes

3.3 The principal purpose for acquiring land and property assets will be to improve the financial position of the Council and its communities. This could be in the form of a revenue stream to the Council or to facilitate economic development or regeneration schemes.

4. Powers to acquire land and property assets.

4.1 The 1972 Local Government act provides the authority for local government to both acquire and dispose of property assets. S120 deals with the acquisition of assets as follows:

S120 Acquisition of land by agreement by principal councils.

(1) For the purposes of—

(a) any of their functions under this or any other enactment, or

(b) the benefit, improvement or development of their area,

a principal council may acquire by agreement any land, whether situated inside or outside their area.

4.2 S12 of the Local Government Act 2003 defines the parameters within which a Local Authorities may make investments:

(a)for any purpose relevant to its functions under any enactment, or

(b)for the purposes of the prudent management of its financial affairs.

The acquisition of an investment asset subject to appropriate safeguards and evaluations could reasonably meet S12(b) if undertaken in conjunction with other treasury management practices.

4.3 The power to borrow is provided via S1 of the 2003 Local Government Act. This determines that borrowing may be undertaken;

(b) for the purposes of prudent management of its financial affairs provided it does not exceed its affordable borrowing limit under s.3 Local Government Act 2003 (s.2(1) and 2(4))

5. Acquisition & Governance Framework

5.1 All proposed land and property acquisitions are to be undertaken by the Council's Estates team in accordance with prevailing legislation and the rules laid down by the relevant professional bodies. All valuations must be undertaken by a qualified[2] member of the Royal Institution of Chartered Surveyors with knowledge of the relevant local and specialist markets.

5.2 Any acquisition will require member approval in order for it to be added to the Council's capital programme. Council has adopted two criteria in order for the inclusion of an item within the capital programme:

[1] Legal interest can mean freehold or leasehold interest, but not a tenancy of will or licence.

[2] MRICS or FRICS

- The project must pay for itself
- The project must replace something from the list.

For property acquisitions it is intended that the first criteria will apply and only acquisitions that can demonstrate a revenue stream in excess of the borrowing costs will be considered.

5.3 In order for an acquisition to be considered it must at a minimum meet eligibility criteria I, ii and vii below:

i. The acquisition will result in a net annual return of 0.5% above the prevailing government gilt rate for a 20 year investment.
ii. Debt repayment has to be completed within 20 years.
iii. The acquisition will form part of a land assembly exercise to enable a wider development with either strategic, regeneration or economic development objectives.
iv. The acquisition will enable improved service delivery and release an existing holding.
v. The acquisition would not be in conflict with the Councils Local Development Plan or successive strategy.
vi. The acquisition would enable inward investment, new start-ups or business expansions.
vii. Commercial acquisitions should normally be pre-let to a tenant with a strong covenant with a minimum of 10 years unexpired on a commercial lease.
viii. If the asset to be acquired is outside the County boundary then criteria I, ii and vii would need to be satisfied.

5.4 All proposed acquisitions will need to be the subject of a Business Case which details the following:

- Address, tenure, occupiers, acquisition price & income streams, including the covenant strength of the tenant.
- Any restrictions against title, clawbacks, legal implications
- Cash flow which models anticipated internal rate of return (to include all costs associated with holding the asset, e.g. repairs, management costs, acquisition costs etc.)
- Compliance with eligibility criteria (i,ii, vii)
- Risks – These will be unique to the property but should consider tenant risk, market exposure and trends, condition

5.5 The Business case will need to be shared and agreed with the Directorate accountant prior to the proposal being presented to members for consideration.

Identification of potential investment opportunity & collation of information (assessment against criteria I,ii & vii

Creation of a Business Plan to establish viability of proposal as outlined in 5.4

If the Business Case is proven, seek approval on the proposal from Cabinet Member for Resources and Head of Finance. If the proposal is enable a wider regeneration consult with Cabinet Member for Innovation, Enterprise & Leisure.

Cabinet report seeking approval to the proposed acquisition and funding arrangements.

Full Council report seeking approval to amend the capital programme to enable the acquisition of the property.

5.6 In the event that approval is granted by Council the Estates team will undertake the acquisition of the asset on the basis of the terms reported to Cabinet / Council. Expert advice will be used where required to supplement staff resources or to provide specialist expertise.

5.7 Annual performance of investment assets acquired via this policy will be undertaken to ensure that they generate an income stream of 0.5% above prevailing government gilt rates.

5.8 In the event that a property holding does not meet its borrowing costs a review will be undertaken to determine:

- The potential to increase the revenue generated or reduce holding costs
- The anticipated sale value of the asset

If it is determined that the net sale value will realise a receipt in excess of the purchase price and that there is little potential to increase the revenue then the asset will be sold. If however the net sale value will not realise a value equal to or in excess of that originally paid the asset will be retained until such time the capital value has increased. All income and expenditure will be funded and managed by the Estates Team.

6. Risks

6.1 As with all investment opportunities the property market will be subject to fluctuations which will result in either increases or decreases to the rental value and the resultant capital value.

6.2 Illiquidity - In the event that a property needs to be sold to generate capital funds the disposal process will take a number of months to complete.

6.3 Commercial property will require management to safeguard the physical condition of the asset and the landlord tenant relationship. Regardless of contractual arrangements there will always be the risk of tenant default.