Appendix 1 – Asset Investment Policy (Updated Dec 2023)

1. Introduction

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 running costs through the rationalisation of its operational estate and enabling staff to work remotely. Whilst this process will continue to seek efficiencies, it is limited to cost avoidance and efficiency savings. This policy is concerned with supporting economic and regeneration policies through prudent investments, and which in turn may generate a net revenue return to the Council.

It is recognised that there has been significant scrutiny over public agencies acquisition of commercial portfolios funded by borrowing or capital reserves. This has led to government intervention and that has placed restrictions on Councils in so far as they must not borrow to invest for the primary purpose of financial return.

This policy will outline the system process that will ensure that investments are prudent, decision-making is transparent, there are defined performance and risk management frameworks in place and accountability is embedded within the governance arrangements.

2. Objectives of the policy

2.1 To invest in opportunities within the County of Monmouthshire to support economic and regeneration policies, support job and wealth creation and improve the opportunities for Monmouthshire citizens.

2.2 To invest in opportunities within the Council's immediate geographical boundary and neighbouring areas of economic influence which will support the Council's economic and regeneration priorities.

2.3 In so far as investments generate a net revenue surplus that they help sustain Council services and in supporting Council priorities.

3. Purpose of the Policy

3.1 The policy sets out the arrangements by which the:

- Council and, as necessary, Investment Committee will assess investment opportunities
- Performance and Overview Scrutiny Committee will assess subsequent performance and risk management
- Governance & Audit Committee will seek assurance on overall governance arrangements

3.2 Investments that fall within the scope of this policy are:

- Commercial investments through the provision of commercial loan facilities
- The use of investment funding to acquire, build or renovate investment portfolio holdings

- Investments within equity or debenture interests.

3.3 All commercial investment opportunities will need to be the subject of a Business Plan which evidences that the specified financial and investment criteria set out in this policy are met.

3.4 The principal purpose for undertaking commercial investments will be to improve the financial, environmental or social wellbeing of the Council and its communities. Consideration will be given to the sustainable development principles within the business case and where possible the identification of options to reduce the existing carbon and environmental impact of potential investments.

4. Powers to acquire land and property assets.

Power to acquire and hold 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,

(c) A principal council may acquire by agreement any land, whether situated inside or outside their area.

4.2 Well-being powers

Section 2 of the Local Government Act 2000, gives local authorities the power to do:
1) Anything which they consider is likely to achieve any one of the following objects:
(a) The promotion or improvement of the economic well-being of their area,
(b) The promotion or improvement of the social well-being of their area, and
(c) The promotion or improvement of the environmental well-being of their area

Section 2 (4), of the act provides local authorities with the ability to incur expenditure, give financial assistance, enter into arrangements or agreements and provide goods services and accommodation.

The Council has previously obtained specific advice and legal counsel on the application of these powers to acquire investment assets, which has confirmed that a direct benefit to the citizens of Monmouthshire needs to be accrued from the acquisition of the assets which can be tangible i.e. the provision of new facilities, or intangible i.e. funding service delivery.

General Power of Competence

Chapter 1 (part 2) of the Local Government and Elections (Wales) Act 2021 introduced the general power of competence powers for principal councils in Wales and which have been enjoyed by English authorities since the introduction of the Localism Act. These powers enable qualifying councils to 'act in their communities' best interests' without the need to identify specific legislative powers to undertake a particular activity. The Act sets out the boundaries of the power and the limits on charging and use of the power for commercial purposes.

The power enables councils to be more innovative and lend or invest money; or setup a company or co-operative society to trade and engage in commercial activity. Use of the power is not restricted to the geographical area of the authority or for the benefit of its residents.

Power to borrow

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))

A number of English Authorities have sought advice on the extent of this power and whether it confers the right to borrow money for purely financial purposes. This is yet to be tested in the Courts; however, Welsh Government proposals seem to infer a greater degree of freedom than that afforded by the Localism Act, which confers the general power of competence to English authorities.

The Prudential Code, as updated in 2021, looked to address some of the wider concerns and where a small number of Councils had overly exposed themselves when entering into commercial investments. The Code requires the risks associated with investments for commercial purposes are proportionate to the Council's overall financial capacity (i.e. that plausible losses could be absorbed in budgets or reserves without unmanageable detriment to local services and the level of resources available to the organisation). The Code goes further to state that an authority must not borrow to invest primarily for financial return, unless directly and primarily related to the functions of the authority.

The UK government's rules for access to PWLB lending now require statutory chief finance officers to certify that their local authority's capital spending plans do not include the acquisition of assets primarily for yield, reflecting a view that local authority borrowing powers are granted to finance direct investment in local service delivery (including housing, regeneration and local infrastructure) and for cash flow management, rather than to add debt leverage to return-seeking investment activity.

Authorities with existing commercial investments (including property) are not required by the updated Prudential Code to sell these investments. Authorities may carry out prudent active management and rebalancing of their portfolios. Authorities with commercial land and property may also invest in maximising its value, including repair, renewal and updating of the properties.

5. Financial Criteria

5.1 Commercial investments will be expected to meet the criteria set out below; investments outside these criteria will require approval by Cabinet with a supporting business case and reasons for deviating from the agreed protocols.

Criteria	Measure
Minimum Return	2% benchmark net return on investment per annum and over its expected lifetime (to determine this the costs of borrowing will be deducted from the gross income received).

	Where the acquisition will result in net economic growth to Monmouthshire (through the provision of jobs, additional employment floor space, local regeneration or any other measurable community benefit) a lower return can be considered, but the return cannot be lower than 0% after borrowing.
Target annual return	7% per annum, to be reviewed annually to reflect prevailing market conditions
Minimum Repayment Provision (MRP)	To be assessed on a case-by-case basis by reference to the economic life of the asset or commercial loan term. In all cases, the MRP will not exceed 50 years.
Environmental Impacts of the proposed Investment	The proposed investment will need to quantify the baseline position and identify opportunities to reduce the environment impacts.

6. Investment Criteria

Property Investments

6.1 All proposed land and property acquisitions are to be undertaken by the Council's Estates team or its appointed agents in accordance with prevailing legislation and the codes of practice of relevant professional bodies. All valuations must be undertaken by a qualified[1] member of the Royal Institution of Chartered Surveyors with knowledge of the relevant local and specialist markets.

6.2 All potential acquisitions will be assessed against the following Investment Criteria:

- Location
- Quality
- Tenure
- Title
- Portfolio blend
- Covenant strength and security of income
- Income and capital growth potential
- Potential landlord liabilities
- Identifiable risks & portfolio blend
- Development and added value opportunities
- Economic, regeneration and other key Council priorities
- Market and sectoral conditions
- Independent Valuation
- Environmental impact and sustainable development principles
- Potential exit strategy
- Sinking fund requirement

6.3 If consent is being sought to undertake borrowing to refurbish or develop a property asset a business case will be developed which considers the investment criteria set out in 6.2 above. In addition it will need to outline:

[1] MRICS or FRICS

- Statutory consents required to enable the development and the outcome of any initial investigations
- Anticipated development/ refurbishment costs
- Programme timescales
- Clarification how debt repayments will be funded in advance of rental returns.

Commercial loans, Debenture or Equity Interests.

6.4 All proposed commercial investments will be led by the Council's Finance Department or its appointed specialist technical advisors in accordance with prevailing legislation and the codes of practice of relevant professional bodies.

6.5 All potential investments will be assessed against the following investment criteria:

- Financial standing of the proposed borrower
- Company gearing and assets
- Payback periods and affordability
- Opportunity to protect investment through charges over residual assets, IPR, contracts etc.
- Potential step in rights
- Viability of investment purpose and market competition
- Loan to value ratio
- Potential risks
- Environmental impact and the sustainable development principles
- Potential exit strategy
- Sinking fund requirement

7. Governance Criteria

7.1 It will be a matter for full Council to determine whether an investment proposal is to be considered by the Investment Committee before returning to Council for further consideration. Council approval will be needed for any associated cost of due diligence, and to the extent that this cannot be funded from within the Council's existing approved budget.

7.2 The Investment Committee will be comprised of the Council Leader, Deputy Leader, Cabinet Member for Resources and the Leaders of the two largest opposition parties (political balance 3:1:1). The Committee will be advised by the Deputy Chief Executive (s151 officer) and officers from Finance, Estates and Legal Services together with specialist technical advisors.

7.3 The terms of reference, which will govern the operating practices of Investment Committee, are set out in Annex 1. Three members of the Investment Committee or their nominated deputies will need to be in attendance for the meeting to be quorate.

7.4 A minimum of a two-stage process will be adopted by Investment Committee when considering any investment proposals.

7.5 Investment Committee will need to assess their training needs to ensure that they are suitably equipped to challenge and scrutinise investment proposals. Wider consideration will need to be given to officer capability, capacity and experience and to the extent that third party advice is needed.

Stage 1

7.6 An initial business case is to be prepared which considers the financial and investment criteria set out in this policy. Provisional heads of terms, dependencies, anticipated timescales and potential risks should also be contained in the report.

7.7 The business case will be presented to the Investment Committee for approval to incur costs to undertake the due diligence necessary to substantiate the provisional proposal and recommendations.

Stage 2

7.7 Following the completion of due diligence, a final business case will be prepared. If the proposed investment remains prudent and in line with investment and financial criteria the business case will be presented to Investment Committee for consideration. Investment Committee will then make recommendation to full Council.

7.8 Officers will provide six-monthly investment portfolio performance and risk data to Performance and Overview Scrutiny Committee members to evaluate.

7.9 The Governance and Audit Committee will seek ongoing assurance on overall governance arrangements of commercial investments as part of the Council's overall land and property portfolio.

8. Review Principles

8.1 Six monthly performance data will be presented to the Performance & Overview Scrutiny Committee to evaluate performance against the financial criteria and business case projections. If this data illustrates that an investment is deemed to be underperforming or fails to meet any debt repayment costs, a review will be undertaken to determine:

- Wider prevailing market conditions and the impact on the investment
- The potential to increase the revenue generated or reduce holding costs
- The anticipated sale value of the asset
- Opportunities for debt refinancing
- Opportunities for step in
- Residual value against outstanding borrowing
- Consideration whether the circumstances are short, medium or long term and the potential for recovery

8.5 If it is determined that the asset's sale will realise a net value in excess of the initial investment with little potential to further increase revenue returns then the asset may be sold. In circumstances where the net sale value will not meet the initial investment, the asset should be retained and actions taken to increase the capital value. In circumstances where external factors (market conditions, changes to legislation, etc.) restrict the ability for the asset to recover this value, disposal may be considered.

8.6 All income and expenditure from property assets will be managed by the Estates Team and commercial loans by the Finance Department.

8.7 Where a property investment requires specific expertise, external agents may be instructed to manage the asset on the Council's behalf. If costs cannot be recovered from service charges, they will instead be deducted from the gross annual return.

9 Risks

9.1 As with all investments, they will be subject to fluctuations in market conditions and external factors. All investments will be considered against the security, liquidity, yield principles acknowledging that there will be variations between commercial loans, which are likely to be more liquid than property assets and have shorter paybacks. They are however unlikely to be secured against tangible assets as opposed to property investments, however their payback periods will be longer. An ongoing assessment of risk will need to be undertaken for all such investments.

9.2 Illiquidity - In the event that a property needs to be sold to generate capital funds, the disposal process may take an extended period of time to complete, dependent on the prevailing market conditions and the need to secure best value consideration upon disposal.

9.3 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.

9.4 In the event of a market downturn, it is likely that rental streams will reduce and voids may occur. This may result in the costs of borrowing exceeding revenue received; this risk can be in part mitigated through the creation of sinking funds for each investment. This is where a portion of the surplus income is ring fenced to the asset and used to fund unexpected maintenance costs or offset declining rent rolls.

9.5 When providing commercial loans, risks may arise from a change in the financial viability of the borrower, changes in the market, competition, changes in UK or Welsh Government policies. Whilst these scenarios should all be considered in the business plan, not all circumstances can be predicted as has been highlighted by the Covid 19 pandemic.

9.6 Six monthly assessments of the risk profile for the investment portfolio will enable the Performance & Overview Scrutiny Committee to evaluate and if necessary seek opportunities to mitigate the risk through for example refurbishments, or disposal of the investments.

10. Purchasing and Finance.

10.1 The Council benefits from the ability to access funding from the PWLB at relatively low interest rates and fixed repayment terms enabling certainty over debt repayments and potential yields at the point of the acquisition of an investment.

10.2 If stage 1 approval is provided by Investment Committee, due diligence costs will be incurred. If the investment proceeds these will be included in the total investment cost and funded through borrowing. If the proposal does not proceed if the abortive costs cannot be financed through existing revenue budgets, they will need to be set against the Investment Fund and repayments offset from the gross investment income.

10.3 A sinking fund will be created to manage unforeseen repair works or offset a fall in income levels to prevent the portfolio becoming a net cost to the authority. The value of the sinking fund will be determined on an individual investment basis to reflect value and risk.

11. Governance & Purchase Flow Chart

Identification of potential commercial investment opportunity & initial assessment of compliance against financial and investment criteria.

If initial assessment identifies that the criteria should be met, and to the extent that any such investment proposal could not be considered through the Council's normal decision making and scrutiny process, a report should be presented to Council requesting that the Investment Committee is convened to consider the investment proposal.

Investment Committee convened, in accordance with its terms of reference

Investment Committee to undertake initial review of training needs to ensure effective scrutiny and challenge of investment

Stage 1 Approval

If initial assessment identifies that the criteria should be met, an outline business case is prepared to establish viability of proposal, evidence that the Financial and Investment Criteria are met and identification of due diligence necessary to substantiate any assumptions and analysis of risk.

If the Outline Business case meets financial and investment criteria, officers will seek approval from the Investment Committee to submit a conditional offer subject to contract, due diligence & Member approval. Due diligence will be commenced.

Commission due diligence reports, surveys, re-assess financial, and investment criteria against initial assumptions. Finalise Business Case.

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Stage 2 Approvals

Present finalised Business Case to Investment Committee for their scrutiny and decision. If investment is approved then legal processes can be implemented.

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Present finalised Business Case to Investment Committee for their scrutiny and decision. Decision to be reported to full Council for consideration.

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If Council approval is secured, legal processes to commence under delegated authority secured as part of the Council decision.

Completion of legal processes

Commence legal processes, which will be undertaken by the Council's Commercial and Property Legal Team.

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If the investment is a property acquisition, exchange contracts, which contractually commits the Council to the purchase.

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Finalise legal documentation. Arrange draw down of funds and completion of investment.

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Post completion – if property acquisition, payment of Land Transaction Tax and other fees; arrange for rental payments and ongoing property / portfolio management. Establish sinking fund with finance team.

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Update relevant colleagues / external organisations and update terrier and other software systems.

Performance Monitoring

Performance dashboard of investments and risk register to be presented to Performance & Overview Scrutiny Committee on a six-monthly basis or sooner if required.

Ongoing assessment of governance arrangements around investments and wider land and property portfolio by Governance & Audit Committee.

Annex 1 – Investment Committee Terms of Reference

Purpose: To hold strategic oversight and accountability for the acquisition of commercial investments in line with the Asset Investment Policy.

Membership: The Committee will be comprised of the following elected Members:

The Leader

Deputy Leader

Cabinet Member with portfolio responsibility for Resources

Leaders of the two largest opposition parties

The membership of the committee reflects the political balance of the current administration and will be subject to review following a local government election within the Monmouthshire County Constituency.

Chairperson: The Leader of the Council. In the absence of the Leader, the Deputy Leader will assume the Chair role in their absence.

In attendance: Leaders of the remaining opposition parties

Chief Executive

Deputy Chief Executive (S151 officer)

Chief Officer for Law and Governance (Monitoring Officer)

Chief Officer, Communities and Place

Head of Finance (Deputy S151 officer)

Head of Landlord Services

Other Council Officers as required.

Specialist advisors as required.

Deputising: Members of the Investment Committee are able to nominate a substitute elected Member to deputise for them if they are unable to attend a committee meeting. The deputy will be able to vote on behalf of the substantive Committee Member.

Democratic Services should be advised of any substitute Members, no less than 24 hours prior to the meeting, save in the event of an emergency.

Voting Rights: Will be limited to the members of the Investment Committee

Quorum: Three members of the committee

Frequency: The meetings will be convened as commercial investment opportunities arise and that require the scrutiny and oversight of the Investment Committee. Such circumstances will be determined by Council, and where it is not considered appropriate for this to be considered through the Council's usual decision making and scrutiny functions due to the commercial sensitivity involved.

Declarations of Interest: All Members, Officers and external advisors will be required to submit declarations of interest prior to discussing proceedings. Officers and external advisors with a personal or commercial interest in the proposed investment will not take part in the discussions, without the express consent of the Chair.

Investment Committee remit will be to:

1. Take decisions on proposed commercial acquisitions or investment opportunities.
2. Scrutinise business cases and ensure that proposals are in accordance with the approved Asset Investment Policy.
3. To execute the powers of authority delegated by Council in a prudent manner
4. Members of Investment Committee will act in the best interest of the corporate entity
5. The Committee will undertake review of its effectiveness and identify any training required for committee members.

Note: Ongoing Scrutiny of Commercial Investments

The Performance & Overview Scrutiny Committee will be responsible for:

a) The ongoing monitoring and review of the performance of the commercial and property investment portfolio, ensuring that it meets the agreed financial benchmarks within the asset investment policy and to ensure identified risks are actively managed.

b) To maintain oversight of mitigation and exit strategies for poorly performing investment assets, including disposals. Any disposal will need to be considered in line with the Council's disposal policy and approved by Cabinet.

The Governance & Audit Committee will be responsible for ensuring that the governance and risk management arrangements in place around the commercial and property investment portfolio, and the Council's land and asset portfolio more generally are in place and operating effectively.