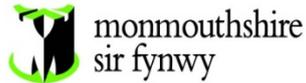


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County Hall  
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NP15 1GA

Wednesday, 11 March 2020

## Notice of Reports Received following Publication of Agenda.

### Audit Committee

Thursday, 19th March, 2020 at 2.00 pm,  
County Hall, The Rhadyr, Usk, NP15 1GA

Attached are reports that the committee will consider as part of the original agenda but were submitted to democratic services following publication of the agenda.

Item No	Item	Pages
5.	Annual Performance Review of Investment Committee	1 - 56

**Paul Matthews**  
Chief Executive

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<b>SUBJECT:</b>	<b>INVESTMENT COMMITTEE PERFORMANCE REVIEW</b>
<b>MEETING:</b>	<b>AUDIT COMMITTEE</b>
<b>DATE:</b>	<b>19<sup>TH</sup> MARCH 2020</b>
<b>DIVISION/WARDS AFFECTED:</b>	<b>ALL</b>

## 1. PURPOSE:

- 1.1 To present the first performance review of the Investment Committee for consideration and in accordance with the requirements of the Asset Investment Policy.

## 2. RECOMMENDATIONS:

- 2.1 For the Audit Committee to consider and scrutinise the first performance review of the Investment Committee.
- 2.2 To consider the proposals for improvement outlined in the report and resulting from audit work undertaken and a review of the current Asset Investment policy and the governance arrangements and controls currently in place to oversee investment activity considered by the Investment Committee.
- 2.3 To receive a verbal update at the meeting following consideration of the Performance Review by the Investment Committee at its meeting on 18<sup>th</sup> March 2020.
- 2.4 For Audit Committee members to determine any further recommendations for improvement.

## 3. KEY ISSUES:

### Background

- 3.1 In May 2018 Council approved a revised Asset Management Strategy. The strategy had been updated in order to provide strategic direction aligned to and reflecting priorities outlined in the Corporate Plan, and which included the need for a more commercial approach to the management, sale and development of assets.
- 3.2 The Strategy outlined a set of key themes which included a targeted approach to commercialisation. This included the adoption of an Asset Investment Policy, delivery of the County Farms strategy, optimizing returns from our existing investment properties, maximizing capital receipts and exploring other commercial opportunities.

- 3.3 The Strategy contained a new policy for the acquisition of investment assets (see appendix 3). This policy positioned the Council in a commercial context providing the framework for the acquisition of income generating assets.
- 3.4 The purpose of the policy was to help sustain Council Services and enhance the asset base by enabling a framework that allowed investment in commercial property assets in order to increase the net rental income stream for the Council and to secure potential further capital growth opportunities.
- 3.5 The Council's Corporate Plan identifies five priorities, of which one concerns the Council being "future focused". One of the key measures for this is income generation from commercial investments. This policy provides the framework for the evaluation of potential commercial property investments.
- 3.6 The intention of the Authority's investment approach is to actively seek out investment opportunities within the County of Monmouthshire, City Deal geographical boundary and neighbouring areas of economic influence which will support our economic and regeneration priorities. In order to manage and spread the risk we also look to identify investment options beyond our county boundaries that meet our criteria. The intention therefore is to work towards an investment portfolio that allows for a diversification of risk.
- 3.7 Investments are judged by SLY principles that look at security, liquidity and yield and a wider set of investment and financial criteria as outlined in the policy. Risks and appropriate mitigations are appropriately assessed against potential return and wider benefits identified.
- 3.8 Acquisitions are funded through prudential borrowing with a £50,000,000 fund originally put in place to fund acquisitions and investments over a three year period. The cost of the debt is funded from the rental streams derived from the property, with a requirement that it will provide a net surplus over and above borrowing costs.
- 3.9 An Investment Committee was established which is made up 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 is advised by the Resources Chief Officer and Officers from Finance, Estates and Legal Services. The Investment Committee has delegated authority to make investment decisions utilising the £50,000,000 allocated borrowing.
- 3.10 When considering acquisitions and investments expert advisors are procured to assist with due diligence and for the development of business cases that are subsequently brought to Investment Committee for consideration. This supplements expertise and capacity within the Authority.
- 3.11 In July 2018 the Asset Investment Policy was supported and complemented by the Commercial Strategy being approved by Cabinet. The Commercial Strategy reinforced as one of its key pillars the development of an approach to commercialising assets.

3.12 In February 2019 the definition of a commercial investment was extended beyond land and building acquisitions to include:

- Commercial loan facilities
- To build or renovate investment portfolio holdings
- An equity or debenture interest

And in order to provide suitable flexibility that allowed the Investment Committee to consider opportunities that met their investment definitions.

### **The Asset Investment Policy**

3.13 The Asset Investment Policy provides a framework for the acquisition of investment opportunities that derive a net return to the Council, provides the governance and delegated authority arrangements and establishes the necessary investment and financial criteria to be met. Investments can not only look to generate net returns to benefit the Council and its communities but also facilitate economic development or regeneration or wider policy objectives of the Council.

3.14 Individual acquisitions or investments must meet financial criteria laid out in the policy, otherwise the decision must be approved by Cabinet rather than the Investment Committee. The target income return is for returns to exceed borrowing costs by at least 2%, though a lower return can be adopted where investment brings economic growth to Monmouthshire. A target total return of at least 7% must also be achieved.

3.15 Investment criteria are also laid out to assess investments and the wider investment portfolio. These includes matters such as strength and security of income, income and capital growth, identifiable risks etc. All acquisitions are subject to a business case or an investment proposal alongside which due diligence is undertaken and that considers both the financial and investment criteria.

3.16 As with all investments there are associated risks. In terms of the income generated from them and their market value. Furthermore the ability to dispose of an asset or recover investments against security held. Commercial property investments require ongoing management to ensure that the capital value is protected and income streams are optimised. Business cases submitted to Investment Committee take into full consideration these risks and outline the extent and level of mitigation in place.

3.17 The Investment Committee takes the decisions on any acquisition or investment on the basis of business cases received and ensuring that they meet the requirements and criteria laid out in the Asset Investment Policy. The Committee is responsible for reviewing the performance of the Investment Portfolio and for reporting this to Audit Committee.

### **The need for an Annual Performance Review**

3.18 One key aspect of the Asset Investment Policy and the review principles contained therein is the requirement for an annual performance review to be undertaken of the Investment

Committee and the investment activity undertaken during that period. The purpose of the review is to ascertain performance against the following criteria:

- Governance arrangements and adherence to policy
- Relevant Market indexes
- Property performance locally
- Capital, Income and Total returns

3.19 This performance review refers solely to property acquisitions and investments that have been considered and/or made during since the Investment Committee was constituted and first met in June 2018. The review covers the period up to and including the end of February 2020. The review does not consider any other investment properties and assets such as the solar farm, the cattle market in Raglan, industrial property holdings or Innovation House.

### **Investment activity to date**

- 3.20 In practice the volume of suitable proposals considered by investment Committee has remained fairly restricted, because realistic opportunities are limited when compared against a test of suitability and risk appetite. Furthermore a number of Investment Committee meetings have had to be cancelled or postponed as a result of proposals not being sufficiently developed for consideration. Which is the nature of commercial activity and where third party negotiation and agreement is involved.
- 3.21 To date the Investment Committee has prudently only taken forward two investments being the acquisitions of Castlegate Business Park in June 2018 for £8m and Newport Leisure Park in February 2019 for £22m as they derived a sufficient return after repaying borrowing costs. In terms of the acquisition of Newport Leisure Park and as a result of the investment exceeding the financial criteria in that the investment represented more than 20% of the total £50m fund value, the decision was referred on to Cabinet who subsequently made the decision to acquire.
- 3.22 The investment in Castlegate Business Park, whilst deriving a sufficient return after repaying borrowing costs, also recognised the Council's intent to support economic development in Monmouthshire. The investment in Newport Leisure Park, an out of County investment again derived sufficient return but also afforded a level diversification of risk due to the differing industry sector focus.
- 3.23 Both of these investments are actively managed and monitored by the Council's Estates Development team in conjunction with support from Alder King as advisors and acting agents with necessary support from both finance and legal officers. Investment performance is reported as part of the Council's periodic budget monitoring arrangements.
- 3.24 No exit strategies have had to be considered or recommended to the Investment Committee. The carrying value of the investments, Land Transaction Tax and fees aside, remains in line with the original capital cost of acquisition. In terms of mitigation strategies Castlegate Business Park has seen occupancy drop from 95% since acquisition to 88%. Mitigation steps are being taken and vacant units are being actively marketed.

Furthermore, the cessation of a lease and relocation of a theatre group will provide an opportunity to remodel and re-let commercial space.

- 3.25 Both investments continue to generate positive returns to the Council. Further information is provided in the resource implications and against the financial and investment criteria in place.
- 3.26 Beyond the investment acquisitions the Investment Committee has also approved for due diligence to be undertaken on a number of other investment opportunities. These are currently in train and will be considered by the Investment Committee in due course and if the necessary investment and financial criteria are met and officers make subsequent recommendation to the Committee. A number of investments have also had due diligence undertaken and have not subsequently come forward to Investment Committee.
- 3.27 The Authority continues to actively source, pursue and consider potential investment opportunities. Future opportunities may potentially arise from the Authority's interest in housing or commercial development and that looks to support the delivery of Council's Local Development Plan, Economic Ambition Statement and Inward Investment Prospectus. As well as in meeting other policy objectives such as to aid delivery of the Digital Infrastructure Plan.

### **The Wider National Context**

- 3.28 It is worth mentioning the wider national context at this stage and in providing an objective review of commercial investment activity across Local Government in the UK. Local Authorities investing in commercial property investment has attracted a lot of interest in the media over recent years and driven by a sharp rise in local authorities borrowing for commercial purposes and to supplement their revenue budgets with rental income. But particularly a small number of authorities who have invested significantly and relative to the assets and income of the Council. The most reported of these being Spelthorne Borough Council who bought BP's Head Office for a sum reported between £360-£380m.
- 3.29 The rise in commercial activity of Councils has also prompted CIPFA to issue property investment guidance to local authorities. The guidance reinforces the legal and regulatory framework that Councils operate within and the need to have regard to the Prudential and Treasury Management Codes. And where decisions are seen to be prudent, affordable and sustainable. Furthermore, the guidance highlights the need for the risks of investments to be understood and suitably mitigated or managed. The Council has had regard to this guidance and the principles therein in putting the necessary policy framework and governance arrangements in place with its commercial investment activity,
- 3.30 The Welsh Government (WG) published revised Investment Guidance in November 2019 which placed additional reporting requirements upon local authorities. The guidance also covers investments that are not part of treasury management, for example commercial investments including property and loans and other investments in local organisations. The Treasury Policy and Strategy approved by Council in March had regard to these additional requirements and the relevant extracts, including the prudential indicators are included in appendix D.

- 3.31 UK Government has also taken a direct interest. The Public Accounts Committee took an interest when assessing the financial sustainability of local authorities in 2016. And a briefing paper was produced for the House of Commons in September 2019 on local government commercial property investment.
- 3.32 A February 2020 report by the National Audit Office found councils spent £6.6bn on commercial property from 2016-17 to 2018-19 – 14.4 times more than in the preceding three years, and mostly financed by borrowing.
- 3.33 Most recently and resulting from the UK Government's budget announcement by the Chancellor consideration is being given to curb local authorities being able to use PWLB borrowing as a means to invest in commercial activity/property for purely commercial gain. So for investment assets that are solely for yield and with no direct policy purpose. This announcement came after PWLB introduced a surprise 1% hike in rates in October 2019. It is as yet unclear as to how UK Treasury will both consult and introduce measures and this will continue to be closely monitored and any potential implications will be assessed in the interim. It is seen that this potential action by UK Government is unfortunately driven by the commercial activities and behaviours of a few local authorities.

### **Audit Coverage**

- 3.34 As part of the Internal Audit plan for 2019-20 a review of Investment Property Acquisitions was undertaken and in line with the risk based internal audit approach of the Council. This review was welcomed and looked to provide an independent assessment of the control environment within which acquisitions took place and are managed. The final audit report is provided in appendix 1.
- 3.35 The process for investment property acquisitions was assessed as providing 'Reasonable Assurance'. 18 strengths were identified during the course of the audit. There were however two significant weaknesses identified relating to: (i) the tender and award of the contracts to Alder King as advisors and managing agents; and (ii) a decision made at Investment Committee on 6<sup>th</sup> March 2019 being seen as inquorate. A further nine moderate risks and four minor risks were identified.
- 3.36 Management responses have been provided and management action is being promptly taken to address the recommendations made and to continue to strengthen the arrangements in place. A number of the recommendations made were not agreed or partly agreed and management responses and justifications are provided in appendix 1.
- 3.37 Further to the work of internal audit WAO have been undertaking two separate reviews:
- a) The first of these is a study into commercialisation in local government. This aims to ensure that new commercial activities are strategically led, risks considered and appropriately scrutinised and regardless of what form they take.

The study has been undertaken by looking at five local authorities in Wales who have or are developing approaches to growing commercial activity. It looks to determine

whether Councils have established effective systems to consider and approve whether they pursue new commercial activity. The study focuses on long-term approaches to financial sustainability and how commercial activity supports organisations to deliver wider wellbeing objectives and corporate priorities. This study does not focus on the commercial acquisitions made by the Council.

The study is a National Review and will lead to a national report that will outline good practice and self-evaluation tools and that draws on evidence and research. Findings from local evaluation will be shared with the Council in a form yet to be prescribed. Fieldwork was undertaken by WAO earlier in the year and the Authority has contributed in providing information and undertaking interviews to support the study. The national report and local feedback is yet to be received.

- b) The second WAO review is the financial sustainability assessment which represents a new programme of work that is proposed to be undertaken annually going forward for each local authority in Wales. The Council produced a self-assessment and relevant members and officers were subsequently interviewed. The Authority has just received the first draft of the local report and assessment for 2019-20 and will now comment on the findings and conclusions drawn. In terms of commercial activity, a single draft recommendation is made that in pursuing its commercial strategy that the Council should ensure that it manages the associated risks of any additional borrowing. A national report will also be produced and published.

## **Risk Management**

3.38 Whilst each investment will have its own unique characteristics and associated risks, as is the case with any investment, the key risks associated with commercial and property investment and where the Council is drawing on borrowing to fund such commercial activity are:

- That all decisions to incur expenditure and to borrow are backed by effective legal powers and a resultant risk if decisions made subsequently become invalidated by changes in statutory provisions or developments in case law.
- The authority's returns are at risk, while, once incurred, borrowing costs are unavoidable. A reduction in returns could put pressure on the authority's revenue account
- Capital gains are at risk and in relation to the fair value of the property on the balance sheet, for example, where the commercial property fair value is less than the value of the debt liability.
- A risk of proportionality in terms of extent that the authority's revenue budget is reliant on income from commercial investments.
- A lack of expertise with council staff and those undertaking review and making decisions leading to poor acquisition decisions.

- A downturn in the property market or the market within which an investment is made.
- 3.39 Separate Legal counsel advice has been received and that confirmed that the Council can operate within existing legal powers and guidance and in making the commercial investments as intended. Legal advice is sought separately for each commercial investment being considered.
- 3.40 Business cases that are developed and considered by Investment Committee undertake a full and proper assessment of risk and associated risk management and mitigation strategies. Business cases are supported by detailed commercial, financial and legal due diligence with external advisors appointed as required to supplement the experienced staff in Estates, Finance and Legal.
- 3.41 Proposals presented to Investment Committee seek to describe the opportunity being considered from the perspective of the cashflows anticipated, and net returns quantified, any qualitative benefits evaluated, reasonableness of assumptions made, any risks/volatility anticipated against those assumptions, and provides the risk mitigation action proposed should those risks crystallise. There is a skewed emphasis towards the risk mitigation aspect of any proposal, not because highly speculative opportunities are being presented to Investment Committee, but instead recognising that any investment has a degree of speculation and despite commercial investment being an increasingly common aspect for local authorities to address declining central government resourcing, the stewardship of public funds and security of investment remains a key consideration to any local authority decision making.
- 3.42 Ongoing monitoring of the investments take place and risks are continually assessed. Business cases have exit strategies to mitigate any situation where a long-term erosion of capital value is anticipated.
- 3.43 Prudential indicators monitor and contain local authority borrowing levels and commercial investment activity is separately shown and further supported by the additional reporting requirements brought in by recent and revised WG Investment guidance. Further information and analysis is contained in appendix 3.

### **Proposals for Improvement**

- 3.44 One of the key outcomes from the performance review being undertaken is to reflect on proposals for improvement resulting from audit work undertaken as well as separately reviewing the current Asset Investment policy and the governance arrangements and controls currently in place to oversee investment activity considered by the Investment Committee.
- 3.45 The following proposals for improvement are recommended for the forthcoming period:
- To review and update the Asset Investment Policy and Investment Committee terms of reference as required taking on board latest guidance, internal audit recommendations and the Council's policy objectives around economic growth

- To ensure that the performance review is undertaken on an annual basis going forward
- That an overarching risk assessment is produced, maintained and reported to the Investment Committee on at least an annual basis, with any emerging risks being brought to the attention of the Committee on a timely basis
- To update the constitution to include details of the Investment Committee
- Declarations of interest forms to be completed as required by those attending Investment Committee meetings
- A performance dashboard to be developed and reported to Investment Committee on at least twice a year such as to review performance of the investment portfolio
- To ensure that any investment proposals that are not taken forward are reported back to Investment Committee
- To implement the Estates restructure and to fill current vacancies and that look to address existing capacity issues and that are resulting in the need to draw additionally on external advisors at this time
- To assess training needs of staff and members involved in the decision making process for commercial investments
- To consider the merit of independent members being added on to the Investment Committee
- To consider the need to re-introduce a sinking fund in earmarked reserves to act as a buffer against any in-year deficits caused by investment performance
- To maintain a close ongoing review of further advice and guidance, and in light of the UK Government and Chancellor's announcement and the intention to constrain local authorities commercial activities through PWLB borrowing.
- To procure a new investment advisor for commercial property investments and to ensure all future appointments are made in line with Contract Procedure Rules.
- To ensure that adequate consideration is given to the Climate Emergency and environment considerations of any investments

#### **4. OPTIONS APPRAISAL**

4.1 This report is not a decision making report. It represents a performance review of the Investment Committee and therefore no option appraisal is required.

#### **5. EVALUATION CRITERIA**

5.1 Evaluation is undertaken and required at a number of stages being:

- a) When an investment opportunity is identified or an investment proposal received and Investment Committee agrees for due diligence to be undertaken;
- b) On the submission of a proposal or business case to the Investment Committee for consideration;
- c) On an ongoing basis as part of routine and regular monitoring of commercial investments – reporting and taking action as required;
- d) As part of the annual performance review that is a requirement of the Asset Investment Policy – acting on proposals for improvement; and

- e) As part of internal and external reviews undertaken – acting on recommendations and proposals for improvement

5.2 The results of the evaluation arising from this performance review are outline in 3.42 together with the resource implications shown below.

## **6. REASONS:**

6.1 The Asset Investment Policy requires an annual performance review of the Investment Committee to be undertaken and in order to ensure that the governance arrangements, policy documentation and necessary guidance and legislation are being reviewed and adhered to.

## **7. RESOURCE IMPLICATIONS:**

7.1 As stated above the two investment acquisitions to date relate to Castlegate Business Park and Newport Leisure Park.

7.2 Of the £50m prudential borrowing capability delegated to the Investment Committee £30.7m has been spent to date and on the two acquisitions. Any additional costs of due diligence and advice incurred in exploring other commercial investment opportunities have been met from existing revenue budgets, to the extent that they aren't subsequently able to be incorporated into future investment or acquisition costs.

7.3 As a result of the acquisitions made budgeted savings have been introduced and form part of the revenue budget savings. The budgeted level of savings for Castlegate Business Park and Newport Leisure Park are £209k and £400k respectively. Most recent forecasts for the current financial year report a £73k shortfall for Castlegate and a £82k outperformance for Newport Leisure Park. Whilst this represents a net forecast shortfall against budgeted savings of £9k the two investments are contributing £618k savings over and above borrowing costs.

7.4 The original budget case for Castlegate was based on a target occupancy of 95% and which resulted in an investment return over borrowing (ROI) of 3.01%. Occupation is currently running at 88% as a result of a number of vacant units. As a result the current ROI is 1.81% which whilst falling below the 2% benchmark is being addressed currently. New units are awaiting final rental agreements being agreed and other vacant units are being actively marketed.

7.5 In terms of Newport Leisure Park the business case was predicated on 100% occupation and this is being maintained with some rental concessions currently in place. The original budget case was based on a 2.11% ROI and the current ROI being achieved is 2.14%.

7.6 In terms of capital value, and Land Transaction Tax and Fees aside, both investments are maintaining their value and based on the latest valuations held.

7.7 In terms of arrears of rent and service charge with tenants there are no significant issues to report other than with one tenant at Newport Leisure Park where rent and service

charges remains outstanding for the January to March 2020 period and where a statutory notice will be considered. However, this continues to be actively monitoring by estates, finance and appointed agents.

**8. EQUALITY AND FUTURE GENERATIONS EVALUATION (INCLUDES SOCIAL JUSTICE, SAFEGUARDING AND CORPORATE PARENTING):**

8.1 There are no Equality, Future Generation or wider implications directly arising from this report. This report is looking to provide a review of performance. Any implications will be assessed as required by the Investment Committee when considering any investment. All proposals for improvement look to strengthen future governance arrangements and again have no resultant potential implications.

**9. CONSULTEES:**

Chief Executive  
Head of Legal Services (Monitoring Officer)  
Chief Officer for Resources (Acting S151 Officer)  
Finance Manager – Central Accountancy  
Head of Commercial, Property, Facilities & Fleet  
Interim Estates Manager

**10. BACKGROUND PAPERS:**

Appendix 1 – Investment Property Acquisitions - Internal audit report  
Appendix 2 – Welsh Government guidance on Local Authority investments  
Appendix 3 – Treasury Policy & Strategy 2020-21 (Extract)  
Appendix 4 – Asset Investment Policy 2018  
Appendix 5 – Investment Committee Terms of Reference

**11. AUTHOR:** Peter Davies, Chief Officer for Resources

**12. CONTACT DETAILS:**

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monmouthshire  
sir fynwy

**PRIVATE & CONFIDENTIAL**

INTERNAL AUDIT REPORT

INVESTMENT PROPERTY ACQUISITIONS  
2019/20

Date of Fieldwork	<i>February – July 2019</i>
Date of Report Issue	<i>March 2020</i>
Report Status	<i>Final</i>
Report Author	<i>Sarah Griffiths, Senior Auditor Mark Stenner, Principal Auditor David Walton, Audit Manager</i>
Issued on Behalf of	<i>Andrew Wathan, Chief Internal Auditor</i>
Issued to	<i>Debra Hill Howells, Head Of Commercial, Property, Facilities &amp; Fleet Peter Davies, Chief Officer Resources</i>

## **INTRODUCTION**

This audit has been carried out in accordance with the 2019/20 Audit Plan, which was approved by Audit Committee on 13th June 2019 after consultation with the Authority's Senior Leadership Team and Directorate Management Teams.

During 2018/19, Council approved the borrowing of £50 million to make acquisitions to bring additional funding in to the Council and to allow a more commercially minded approach with the view to identifying additional revenue streams.

At the time of the review, MCC had finalised one acquisition, which was the purchase of Castlegate Business Park, Caldicot. This purchase and the management of the site, was the primary focus of the review. A second major purchase, of Newport Leisure Park was ongoing whilst the audit was in progress, but the audit testing was focused on the earlier Castlegate acquisition.

## **SCOPE & OBJECTIVE OF THE AUDIT**

The objective of the audit was to carry out a review of the Council's arrangements for the acquisition of investment property.

The following control objectives were examined during the audit:

- The Authority has an appropriate strategic and policy framework to govern and control their investment property acquisitions.
- A governance structure has been established to have oversight of the Authority's investment property acquisitions, to facilitate decision making and provide a robust monitoring function.
- Investment decisions have been made based upon detailed business cases, in consultation with expert external and internal advisors.
- Detailed borrowing options assessments are undertaken and presented to the Investment Committee to inform decision making. Relevant payments are made in line with the Authority's Financial and Contract Procedure Rules. Potential income is assessed and specific budget codes are established to manage and monitor the financial arrangements for investment properties.
- Robust risk management processes are in place to protect the Authority and to safeguard its assets. All assets are appropriately insured to mitigate against any loss.

It should be noted that due to the timing of the audit, only the purchase and management of Castle Gate Business Park was reviewed. Assurance on this acquisition only, can be taken from this review.

## **CONCLUSIONS & AUDIT OPINION**

Overall, a number of strengths were highlighted in this review. Some weaknesses were also revealed by the audit, which is understandable given that investment property acquisitions is a new and emerging area for the Authority to be involved in.

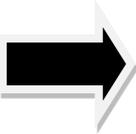
Two significant weaknesses were identified, the first surrounding the tender and award of contracts to Alder King as advisors and managing agents. The second related to the Investment

Committee meeting held on 6<sup>th</sup> March 2019, when only 2 of the 5 nominated Committee members were present and hence the meeting was inquorate. Despite this, the meeting proceeded and decisions were taken, in breach of the Committee's own terms of reference.

A further nine moderate risk issues were identified as well as four minor risks. Audit recommendations have been included to help address the significant and moderate risk issues identified and to strengthen the control environment to manage any risks arising.

**Appendix 1** provides a summary of the findings of the audit in table form. Each of these findings has been taken into account in determining our audit opinion on investment property acquisitions. Details of the significant and moderate risk findings and our associated recommendations are given in **Appendix 2**, which also serves as the Action Plan for this audit. Audit findings of a minor risk are listed in **Appendix 3** for management attention. Finally, a summary of control strengths identified during the audit is given in **Appendix 4**.

Overall, the process for investment property acquisitions has been assessed as providing a '**Reasonable Assurance**', which reflects that the financial and administrative systems reviewed were found to be adequately controlled, although risks identified which could compromise the overall control environment. Improvements required.



<b>SUBSTANTIAL</b>	<p>Substantial level of assurance.</p> <p>Very well controlled, with numerous strengths identified and any risks being less significant in nature.</p>
<b>CONSIDERABLE</b>	<p>Considerable level of assurance.</p> <p>Generally well controlled, although some risks identified which should be addressed.</p>
<b>REASONABLE</b>	<p>Reasonable level of assurance.</p> <p>Adequately controlled, although risks identified which could compromise the overall control environment. Improvements required.</p>
<b>LIMITED</b>	<p>Limited level of assurance.</p> <p>Poorly controlled, with unacceptable levels of risk. Fundamental improvements required urgently.</p>

**APPENDIX 1 – SUMMARY OF STRENGTHS AND WEAKNESSES**

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The table below summarises the ratings used during the review and the number of occurrences of each rating identified.

<b>RATING</b>	<b>RISK DESCRIPTION</b>	<b>IMPACT</b>	<b>TOTAL IDENTIFIED DURING REVIEW</b>
1	Significant	(Significant) – Major / unacceptable risk identified. Risks exist which could impact on the key business objectives. Immediate action required to address risks.	2
2	Moderate	(Important) – Risk identified that requires attention. Risks identified which are not business critical but which require management attention as soon as possible.	7
3	Minor	(Minimal) – Low risk partially mitigated but should still be addressed. Audit comments highlight a suggestion or idea that management may want to consider.	4
4	Strength	(No risk) – Good operational practices confirmed. Well controlled processes delivering a sound internal control framework.	18

**APPENDIX 2 – SIGNIFICANT/MODERATE RISK ISSUES IDENTIFIED AND ACTION**

No.	Audit Ref.	Issue & Risk	Audit Comment	Recommendation	Who is Responsible	When will the action be Implemented
1	2.3	<p>The Investment Committee meeting of 6/3/2019 was attended by only 2 of the nominated Committee members, therefore the meeting was not quorate in line with terms of reference for this Committee.</p> <p><b>Risk - Decisions taken could be subject to challenge</b></p>	<p>The Investment Committee terms of reference require 3 members to attend for the meeting to be quorate. However, at the meeting on the 6<sup>th</sup> March 2019, only 2 of the designated Committee members attended (the Leader &amp; Cabinet Member for Resources). The three other nominated Committee members all gave apologies for absence. Cllr Davies was also present, but is not identified in the terms of reference or on the Council website as being a nominated member of the Investment Committee.</p>	<p>If meetings are not quorate, reports should be deferred to a later date when the meeting can be reconvened to take decisions in line with the terms of reference.</p> <p><b>Management Response:</b> <b>Agreed. This approach has already been adopted.</b></p>	<p>Democratic Services</p>	<p>Now implemented</p>

**APPENDIX 2 – SIGNIFICANT/MODERATE RISK ISSUES IDENTIFIED AND ACTION**

No.	Audit Ref.	Issue & Risk	Audit Comment	Recommendation	Who is Responsible	When will the action be Implemented
2	3.2	<p>Tender evaluations for the role of external consultants were not available.</p> <p>No tender exercises had been undertaken to appoint Alder King to undertake due diligence on the acquisition or as managing agents.</p> <p><b>Risk – Value for money may not be obtained.</b></p> <p><b>OJEU Regulations breached. Potential legal challenge from alternative service providers.</b></p>	<p>Alder King were appointed as advisors. We were informed that a mini competition had been undertaken and that 3 providers had been invited from a framework.</p> <p>Whilst tender documentation was available, there was no evidence available to demonstrate scoring or evaluations of the submissions received. It was reported that a previous member of staff had undertaken the evaluation and the documentation could not be located. From the documentation available, this exercise was to appoint an advisor up to the value of £25,000 spend.</p> <p>It was noted that there had been no tendering process to appoint Alder King to undertake due diligence on the acquisition or, subsequently, to act as managing agents. In 2018/19, MCC spent £188,826 with Alder King. This level exceeded in a single year the OJEU threshold governing procurement activity for supplies and services for local authorities (the threshold was £181,302 in 2018/19).</p>	<p>In future, tender evaluations should be retained and stored in a central location, allowing them to be accessed even if the person undertaking the evaluation leaves the Authority's employment.</p> <p>A tendering exercise should be undertaken at the earliest opportunity to appoint managing agents for the acquired properties. Alder King should be notified of this intention.</p> <p>The tendering exercise should be undertaken in line with the Authority's Contract Procedure Rules and EU procurement legislation.</p> <p>When the next property is acquired, the award of due diligence work should be done via a tender exercise.</p> <p><b>Management Response:</b></p> <p><b>The appointment of managing of Alder King as our investment advisors was subject to a mini tender via the Crown Commercial Services framework as Audit were advised. The appointment of Alder King as managing</b></p>	<p>Head Of Commercial, Property, Facilities &amp; Fleet</p>	<p>June 2020</p>

**APPENDIX 2 – SIGNIFICANT/MODERATE RISK ISSUES IDENTIFIED AND ACTION**

No.	Audit Ref.	Issue & Risk	Audit Comment	Recommendation	Who is Responsible	When will the action be Implemented
Page 19				<p><i>agents for the 2 investment properties was commissioned via the CCS framework. The largest issue however remains the payment of agent's commission for acquisition which is the largest contribution to the aggregated fees. This is payable to the agent that introduces the property and would not always be Alder King.</i></p> <p><i>We will procure a new investment advisors appointment, but if the introducing agent is not our investment advisor, commission fees will still be liable.</i></p>		

APPENDIX 2 – SIGNIFICANT/MODERATE RISK ISSUES IDENTIFIED AND ACTION

No.	Audit Ref.	Issue & Risk	Audit Comment	Recommendation	Who is Responsible	When will the action be Implemented
3	1.3	<p>Critical success factors were not clearly identifiable within the Commercial Strategy.</p> <p>Risks were not explored appropriately.</p> <p><b>Risk – Failure to monitor the success or failure effectively could result in poor decision making.</b></p>	<p>Although some KPI targets were set, none of these were specifically identified as being critical success factors.</p> <p>Risks have been summarised within the strategy but could have been expanded upon to provide greater detail of the threats faced. The current strategy only included 3 risks arising from property investments.</p>	<p>Critical success factors should be clearly laid out within the Commercial Strategy.</p> <p>All risks should be fully explored and documented within the Strategy.</p> <p><b>Management Response:</b></p> <p><b>Agreed in part. Risks resulting from the Commercial Strategy will result from commercial activity that is undertaken by the Authority and will be unique to any commercialisation of services or commercial acquisition or investment. Each of these will require a business case and as necessary associated due diligence which will both identify risks and mitigations. There are overarching risks relating to the delivery of the Strategy which are already captured. However, this will be reviewed further when the Strategy is subsequently reviewed and updated.</b></p> <p><b>In terms of critical success factors, this is evidenced in the Strategy by the delivery of the action plan and stemming</b></p>	Chief Officer, Resources	March 2020

**APPENDIX 2 – SIGNIFICANT/MODERATE RISK ISSUES IDENTIFIED AND ACTION**

No.	Audit Ref.	Issue & Risk	Audit Comment	Recommendation	Who is Responsible	When will the action be Implemented
				<i>from delivery of the key aims of the Strategy outlined in section 4.7.</i>		
4	2.4a	<p>The Investment Committee is not included in the current MCC Constitution.</p> <p><b>Risk - Breach of good governance. Potential for decisions to be taken outside of the approved Council processes.</b></p>	<p>At the time of the review, the most recent constitution was reviewed and published in April 2018. The Investment Committee had not been established at that point and so was not included in the Constitution.</p>	<p>The Constitution should be updated to include appropriate details in relation to the Authority's Investment Committee.</p> <p><b>Management Response:</b></p> <p><b>The Constitution is being amended by the Head of Legal Services &amp; Monitoring Officer.</b></p>	<p>Head of Legal Services &amp; Monitoring Officer</p>	<p>May 2020</p>
5	2.5	<p>Officers attending the Investment Committee were not required to complete Declarations of Interests.</p> <p>The Investment Advisor also did not complete a declaration of interests.</p> <p><b>Risk - Conflict of interests may go undisclosed, potential that information provided to Committee may not be fully independent and objective.</b></p>	<p>It was noted that there was no requirement for declarations of interest to be completed for officers attending the Committee, only elected members. Whilst officers were not decision makers themselves, for the sake of transparency and good governance, any personal interests should be declared in advance of the Committee's discussions.</p> <p>Similarly, there were no requirement for the independent advisors to complete declarations at the start of each potential deal.</p>	<p>The terms of reference should be updated to include the requirement for Officers attending the Investment Committee to complete a Declaration of Interests at each meeting.</p> <p>The Investment Advisor should also be required to complete a Declaration of Interests.</p> <p><b>Management Response:</b></p> <p><b>Agreed.</b></p>	<p>Head Of Commercial, Property, Facilities &amp; Fleet</p>	<p>May 2020</p>

**APPENDIX 2 – SIGNIFICANT/MODERATE RISK ISSUES IDENTIFIED AND ACTION**

No.	Audit Ref.	Issue & Risk	Audit Comment	Recommendation	Who is Responsible	When will the action be Implemented
6	2.6	<p>The planned criteria for the annual review of investment performance were limited and could be expanded to allow a more rounded assessment.</p> <p><b><i>Risk - Performance may be assessed on limited criteria, full impact of investments in place may not be assessed.</i></b></p>	<p>Due to the timing of the review, the first acquisition had not reached the due date for annual reporting. The Asset Investment Policy stated that:</p> <p>“An annual performance review of the Investment Committee and any acquisitions will be undertaken and reported to Audit Committee to ascertain performance against the following criteria:</p> <ul style="list-style-type: none"> <li>• Governance arrangements and adherence to policy;</li> <li>• Relevant Market indexes;</li> <li>• Property performance locally</li> <li>• Capital, Income and Total returns.”</li> </ul> <p>Consideration could be given to including the following:</p> <ul style="list-style-type: none"> <li>• Internal rate of return achieved;</li> <li>• Percentage of voids (empty property available for letting)</li> <li>• Any socio-economic targets set (e.g. to stimulate economic activity with the County);</li> <li>• Identification of any under-performing investments; and</li> </ul>	<p>A comprehensive template for the annual performance review should be developed and agreed. This should be used for each review.</p> <p><b><i>Management Response:</i></b></p> <p><b><i>Where appropriate the performance review will be broadened to include measures where information is readily available and is relevant to the performance of the portfolio.</i></b></p>	<p>Chief Officer, Resources</p>	<p>March 2020</p>

APPENDIX 2 – SIGNIFICANT/MODERATE RISK ISSUES IDENTIFIED AND ACTION

No.	Audit Ref.	Issue & Risk	Audit Comment	Recommendation	Who is Responsible	When will the action be Implemented
			<ul style="list-style-type: none"> <li>Disposals/proposed disposals of any under-performing or surplus to requirements investment properties.</li> </ul>			
7	3.3	<p>No truly independent advice was sought over the purchase of Castlegate Business Park.</p> <p><b><i>Risk - Information provided to inform the purchase decision may not be fully independent or objective.</i></b></p>	<p>It was noted, that MCC were informed of the availability of Castlegate Business Park by Alder King. Alder King therefore benefitted from the sale in fees.</p> <p>Alder King also provided financial figures and oversaw the due diligence processes.</p> <p>No further independent advice was requested by MCC prior to agreeing the site purchase.</p>	<p>Consideration should be given to obtaining an independent opinion on future investment purchases.</p> <p><b><i>Management Response:</i></b></p> <p><b><i>Not agreed – any agent would be bound by the standards of the RICS to provide unbiased professional opinion. This approach would result is us getting an independent valuation of an independent valuation. In the event of any deficiency in the advice provided, we would have recourse through their professional indemnity, the RICS and potentially the courts.</i></b></p>	n/a	n/a

**APPENDIX 2 – SIGNIFICANT/MODERATE RISK ISSUES IDENTIFIED AND ACTION**

No.	Audit Ref.	Issue & Risk	Audit Comment	Recommendation	Who is Responsible	When will the action be Implemented
8	5.1	<p>The risk assessment relating to the Castlegate acquisition was limited and lacked information on the evaluation and management of risks identified.</p> <p><i>Risk - Risks may not be adequately assessed, meaning management of these risks may be insufficient.</i></p>	<p>Risks of the acquisition were included in the Business Case, which was presented to the Investment Committee.</p> <p>The risks were listed and some context given, but there was no measurement of the level of risk involved or evidence of how these risks would be managed.</p>	<p>Formal risk assessments should be completed for each acquisitions. Evidence of monitoring of risks should be retained.</p> <p><b>Management Response:</b></p> <p><i>Not agreed. A risk assessment was prepared based on the findings of the due diligence and input from internal and external advisors. The risks were challenged by the Chief Officer and Assistant Head of Finance and mitigating actions were required and included in the business case.</i></p> <p><i>Risks are managed at monthly meetings and will continue to be so.</i></p>	n/a	n/a

**APPENDIX 2 – SIGNIFICANT/MODERATE RISK ISSUES IDENTIFIED AND ACTION**

No.	Audit Ref.	Issue & Risk	Audit Comment	Recommendation	Who is Responsible	When will the action be Implemented
9	5.2	<p>Copies of the maintenance programme for Castlegate Business Park could not be provided to Audit at the time of the review.</p> <p><b><i>Risk - Maintenance may not be undertaken in a timely manner. Anticipated future maintenance costs may be understated in acquisition decision making.</i></b></p>	<p>Maintenance arrangements for Castlegate Business Park were managed by Alder King. These were included in the service charges paid by tenants.</p> <p>Copies of this maintenance programme had been requested by Internal Audit, but were not provided to us during our review.</p> <p>As Alder King oversee this process, copies of the programme should be retained by the Council to enable MCC to monitor the work undertaken/ ensure compliance to the planned maintenance schedule and also to ensure that the Authority's asset is being maintained effectively.</p>	<p>A copy of the maintenance programme should be obtained, retained by MCC and monitored to ensure compliance.</p> <p><b><i>Management Response:</i></b></p> <p><b><i>A maintenance programme is available and is monitored on a monthly basis.</i></b></p>	<p><i>Head Of Commercial, Property, Facilities &amp; Fleet</i></p>	<p><i>A maintenance programme is prepared on an annual basis to inform the service charge and monitored monthly.</i></p>

**APPENDIX 3 – MINOR RISKS IDENTIFIED**

No.	Audit Ref	Issue	Audit Comment	Noted
10	1.4	<p>The Asset Investment Policy did not include any overview of the Council's ethical standpoint, which may impact on the nature of properties that the Authority would be willing to invest in (e.g. would any potential investments that could be seen as harmful to the environment be considered, etc.).</p> <p><b>Risk - Potential reputational damage if investments made are viewed as unethical. Possibility of costs incurred in researching potential investments, which are then declined by the Investment Committee on ethical grounds.</b></p>	<p>The current Strategy did not include any reference to what the Council was, or was not, prepared to invest in.</p>	<p>Agreed, this needs a further report to Full Council to agree this position.</p>
11	2.1	<p>Evaluation of the Investment Committee's effectiveness was not included in their terms of reference.</p> <p><b>Risk - Committee may potentially fail to keep up to date with best practice or new initiatives.</b></p>	<p>The terms of reference should include the requirement for a regular self-review of the effectiveness of the Committee, to allow for new ideas and initiatives to be implemented over time.</p>	<p>Noted.</p>
12	3.1	<p>Unsuccessful investment opportunities were not formally documented or reported to Committee.</p> <p><b>Risk - Potential investment opportunities may not be brought to the attention of the Investment Committee and the reasons for their rejection not disclosed.</b></p>	<p>As an initial assessment of potential investment opportunities, the Head Of Commercial, Property, Facilities &amp; Fleet Services and Alder King carried out a rough calculation of the expected return for each scheme. Where the 2% target return after borrowing costs was not met, the investment opportunity was rejected, although any with potential scope for economic development opportunities were referred onwards.</p> <p>These discounted investment opportunities were, however, not recorded or reported to the Investment Committee.</p>	<p>Noted – not clear what value this will add, however if required by IC then a schedule can be prepared and presented to IC.</p>

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APPENDIX 3 – MINOR RISKS IDENTIFIED

No.	Audit Ref	Issue	Audit Comment	Noted
13	3.7	<p>Disposal process outlines in the Asset Investment Policy did not fully accord with those stated in the Authority's Contract Procedure Rules</p> <p><b><i>Risk - Investment property disposals may be undertaken in breach of the Authority's established Contract Procedure Rules.</i></b></p>	<p>The Asset Investment Policy briefly outlines how investments could be identified as non-performing and steps which could be taken for disposal. There was, however, no reference to disposal at <b>peak value</b> as outlined in the Authority Contract Procedure Rules.</p> <p>The Contract Procedure Rules also mention the need for agreement from the Head of Finance for disposals for over £5k. Section 8.4.1 states: "Assets for disposal must be sent to public auction except where better Value for Money is likely to be obtained by inviting Quotations and Tenders. (These may be invited by advertising on the Council's intranet site)."</p>	<p>The disposal of surplus operational assets is different from the sale of commercial investments, Given that if a commercial investment is generating peak income it would be generating an income surplus which is one of the core principals of the investment and therefore it is unlikely we would seek an exit strategy at that point. This needs to be considered as part of the constitution amendments.</p>

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## APPENDIX 4 – CONTROL STRENGTHS IDENTIFIED

No.	Audit Ref.	Strength Identified
14	1.1a	The Authority has a Commercial Strategy, which sets out strategic direction/objectives. This is linked, to the Authority's latest Corporate Plan and consistent with the documented strategic objectives.
15	1.2	The Commercial Strategy is integrated with the other key strategic and policy documents of the Council
16	1.4a	An Asset Investment Policy had been developed covering the processes to be followed for the identification, purchase, management and monitoring of investment properties.
17	1.5	The Asset Investment Policy has been prepared in consultation with appropriate internal experts, including Finance, Legal and Estates, and has been based upon good practice guidance for the local government sector.
18	1.5a	Specific actions and performance targets were included in Service Business Plan.
19	2.1a	An Investment Committee has been established to govern the Authority's property investments. Terms of reference were in place for the Investment Committee.
20	2.5a	Declarations of interests were sought for elected members attending the Investment Committee (although see finding 5 above).
21	3.3	Based on the figures provided, the Castlegate Business Park was purchased in line with the Asset Investment Policy and Capital Programme.
22	3.3a	The Castlegate acquisition was the subject of a Business Case, which was created in conjunction with the Council's Finance team.
23	3.4	<p>The Castlegate acquisition was subject to</p> <ul style="list-style-type: none"> <li>• A valuation report supporting the purchase price (although see finding 7 above).</li> <li>• Satisfactory building survey and assessment of economic life; and</li> <li>• Satisfactory report on title.</li> <li>• Due consideration of any existing tenancies, facilities management services, etc.</li> </ul>
24	3.5	Approval for the Castlegate acquisition was obtained from the Investment Committee.

## APPENDIX 4 – CONTROL STRENGTHS IDENTIFIED

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No.	Audit Ref.	Strength Identified
25	3.6	The Castlegate acquisition was conducted in accordance with the Authority's Contract Procedure Rules and Financial Procedure Rules.
26	4.1	A borrowing options assessment was undertaken by Finance.
27	4.2	Cost of borrowing had been compared to the potential income to ensure that the threshold of return anticipated was to be met.
28	4.3	Individual/specific cost centres had been developed to account for all related costs and income to allow effective management of each acquisition.
29	5.3	Castlegate Business Park was found be appropriately insured.
30	5.4	The Authority had registered the ownership of its investment property assets and retained title deeds to evidence this.
31	5.5	The Authority's investment properties had been included in appropriate asset recording systems.

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## EXTRACT – TREASURY POLICY &amp; STRATEGY 2020-21

## Annex C - Prudential Indicators

Capital Expenditure £m	2018/19 actual	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget
General Fund services	39.6	27.6	27.9	20.3	19.6	5.9
Commercial investments (£50m total pool)	30.7	16.7	2.6	0.0	0.0	0.0
<b>TOTAL</b>	<b>70.3</b>	<b>44.3</b>	<b>30.5</b>	<b>20.3</b>	<b>19.6</b>	<b>5.9</b>

Proportion of Financing Costs to net revenue stream	2018/19 actual	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget
Interest £m	3.3	3.8	3.8	3.8	3.9	3.8
MRP £m	4.6	5.7	6.3	6.4	6.6	6.8
<b>Total Financing costs £m</b>	<b>7.9</b>	<b>9.5</b>	<b>10.1</b>	<b>10.2</b>	<b>10.5</b>	<b>10.6</b>
Net Revenue Stream (£m)	150.4	154.3	160.8	163.3	165.9	168.6
<b>Proportion of net revenue stream %</b>	<b>5.2%</b>	<b>6.1%</b>	<b>6.3%</b>	<b>6.2%</b>	<b>6.3%</b>	<b>6.3%</b>

Capital Financing Requirement	31.3.19 Actual £m	31.3.20 Estimate £m	31.3.21 Forecast £m	31.3.22 Forecast £m	31.3.23 Forecast £m	31.3.24 Forecast £m
Commercial Investments CFR (including solar farm)	35.1	50.7	51.4	49.3	47.2	44.3
Other Loans CFR	148.8	158.0	158.8	160.7	174.8	175.9
<b>Total Loans CFR</b>	<b>183.9</b>	<b>208.7</b>	<b>210.2</b>	<b>210.0</b>	<b>222.0</b>	<b>220.2</b>
Other Debt Liabilities CFR	2.4	2.4	3.4	3.4	3.4	3.4
<b>Total CFR</b>	<b>186.3</b>	<b>211.1</b>	<b>213.6</b>	<b>213.4</b>	<b>225.4</b>	<b>223.6</b>

A comparison of Net and Gross Debt to Capital Financing Requirement (Loans CFR)	31.3.20 19 actual	31.3.202 0 forecast	31.3.202 1 budget	31.3.202 2 budget	31.3.202 3 budget	31.3.202 4 budget
Net Debt	158.0	182.0	174.8	170.1	181.4	178.1
Gross Debt	178.3	197.0	189.8	185.1	196.4	193.1
Loans CFR	183.9	208.7	210.2	210.0	222.0	220.2

<b><u>Authorised &amp; Operational Borrowing Limits</u></b>	<b>2019/20 for comparison</b>	<b>2020/21 limit</b>	<b>2021/22 limit</b>	<b>2022/23 limit</b>	<b>2023/24 limit</b>
Authorised limit - borrowing	248.2	230.0	225.3	236.6	233.3
Authorised limit - PFI, leases & Right of use assets	4.4	5.4	5.4	5.4	5.4
<b>Authorised limit - total external debt</b>	<b>252.6</b>	<b>235.5</b>	<b>230.7</b>	<b>242.0</b>	<b>238.7</b>
Operational boundary - borrowing	218.0	210.8	206.1	217.4	214.1
Operational boundary - PFI, leases & Right of use assets	2.9	3.9	3.9	3.9	3.9
<b>Operational boundary - total external debt</b>	<b>220.9</b>	<b>214.8</b>	<b>210.0</b>	<b>221.3</b>	<b>218.0</b>

nb - Authorised limit is higher than CFR as CFR is not a limit but an indicator of debt requirement

## Annex D - Additional requirements of Welsh Government Investment Guidance

The Welsh Government (WG) published revised Investment Guidance in November 2019 which places additional reporting requirements that are not integral to this Authority's treasury management processes, upon local authorities. The guidance also covers investments that are not part of treasury management, for example commercial investments including property and loans and other investments in local organisations.

The Authority has taken regard of the recommendations within the WG investment guidance revised in 2019 (for implementation 2020/21) and incorporated them where relevant into the above Treasury Management Strategy Statement (TMSS). There are however some specific areas of the WG investment guidance which are not explicitly outlined in the above TMSS and these are covered further as follows:

**Climate change:** The Authority's investment decisions consider long-term climate risks to support a low carbon economy in line with its declaration of a Climate Emergency in 2019. The Authority's aim is to make the county of Monmouthshire zero carbon by 2030 and will revise the Corporate Plan, Well-being Plan, Local Development Plan and other relevant plans and policies in support of this. It will call on the Welsh Government and the UK Government to provide the necessary powers, resources and technical support to successfully meet the 2030 target.

**Financial and Non-financial Investments:** The Authority's investments contribute to its service delivery objectives and/or promote wellbeing as follows:

- treasury management investments support effective treasury management activities,
- loans & other investments in local organisations provide financial support to those organisations to enable them to deliver local public services that would otherwise be provided directly by the Authority, and
- commercial investments provide a net financial surplus that is reinvested into local public services.

More information about the categories of investments can be see below in Table C1

*Table C1: Types of Investments and Limits*

Type	Specified	Other Loans	Other Non-specified	Financial / Non-financial
<b>Treasury management</b>	Investments with Government, Local Authority, Bank & Building Soc Deposits, CDs, MMFs, Bonds etc *	NA	Investments which are long term or with counterparty not of high credit quality - £6m Limit. Strategic pooled funds and REITS - £6m Limit *	<b>Financial</b>
<b>Assistance to local organisations/relevant to Council functions</b>	Loans to other Local Authorities, Joint ventures with LA's and LA wholly owned subsidiaries **	Loans to local enterprises, charities, 3 <sup>rd</sup> party companies, part non-LA Joint ventures **	Shares in local enterprises, charities, 3 <sup>rd</sup> party co's, part non-LA JVs including seed funding to SRS Ltd ****	<b>Financial</b>
<b>Commercial financial investments</b>	NA	Loans to part non-LA Joint	Shares in part non-LA Joint	<b>Financial</b>

		ventures and 3 <sup>rd</sup> party entities ***	ventures and 3 <sup>rd</sup> party entities ***	
<b>Commercial Property investments</b>	NA	NA	This includes the Solar Farm, Castlegate & Newport Leisure park ***	<b>Non-financial</b>
<b>Long standing Property Investments</b>	NA	NA	This includes the county farms portfolio, shops & industrial units	<b>Non-financial</b>

\* The Limits on these investments are detailed in table 3 & in the Price risk indicator in the Main report

\*\* Rather than include an explicit limit on these type of investments, a business case will be made for each individual investment and capacity made available in an existing budget or a new budget approved by Council for any possible losses.

\*\*\*Rather than include an explicit limit for these type of investments, approval is required by the Investment committee and Council prior to any such investments. To date £4.5m has been approved and spent on the Solar Farm and an additional £50m was approved in May 2018, of which £31m has been invested to date.

**Specified investments:** The WG Guidance defines specified investments as those:

- denominated in pound sterling,
- due to be repaid within 12 months of arrangement unless the counterparty is a local authority,
- not defined as capital expenditure by legislation, and
- invested with one of:
  - the UK Government,
  - a UK local authority, parish council or community council, or
  - a body or investment scheme of “high credit quality”.

The Authority defines “high credit quality” organisations and securities as those having a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher. For money market funds and other pooled funds “high credit quality” is defined as those having a credit rating of [A-] or higher.

**Other Loans:** The WG Guidance defines a loan as a written or oral agreement where the authority temporarily transfers cash to a third party, joint venture, subsidiary or associate who agrees a return according to the terms and conditions of receiving the loan. For the purpose of applying the WG guidance within this strategy document, where such arrangements are treasury investments, also meeting the definition of a Specified Investment they are classed as Specified investments not loans see Table C1.

A local authority may choose to make loans & other investments in local enterprises, local charities, wholly owned companies and joint ventures where relevant to Council functions and to promote local economic growth.

**Valuation of Loans and Receivables:** The Authority uses an allowed ‘expected credit loss’ model for loans and receivables as set out in *International Financial Reporting Standard 9 Financial Instruments* as adopted

by proper practices to measure the credit risk of its loan portfolio. Appropriate consideration is given to state aid rules and competition law. The Authority has appropriate credit control arrangements to recover overdue repayments in place.

Loans may also be made for commercial purposes. Whilst these assets will be valued as above, the limits and assessment of security will be addressed as in the Commercial investments section below.

**Other Non-specified investments:** Any financial investment not meeting the definition of a specified investment or a Loan is classed as ‘Other non-specified’. This category applies to investments over one year and with counterparties not of high credit quality. It also applies to units in pooled funds and shares in companies. Limits on non-specified investments are also shown in table C1; the Authority confirms that its current non-specified investments remain within these limits.

**Commercial investments:** This category covers financial and non-financial investments held primarily or partially to generate a profit. It includes investment property & also loans made for commercial purposes. Security is determined by comparing each asset’s purchase price to its fair value using the model in International Accounting Standard 40: Investment Property as adapted by proper practices. The Authority’s current Investment Property portfolio is divided into long held Investment Properties such as County Farms and the three more recently acquired commercial Investment Properties. With regard to this latter group, at 31<sup>st</sup> March 2019, the Authority’s newly acquired investment property portfolio was held in the Authority’s accounts at a book value of £35.6m. This is more than the capital cost of acquisition and enhancement to date of £35.2m and is considered to provide security for the capital investment made. A full report to Audit committee on these investments is due in the coming months, which will also outline the income which has been received into the revenue account since purchase.

The total of the Authorities usable reserves is £13.1m. This represents 37% of the value of the Authorities Commercial Investment Properties acquired to date. Due to the due diligence process undertaken before Commercial Investments are entered into and the forecast income over the lifetime of the assets, these investments are considered to be prudent by the Authority.

**Liquidity:** The Authority’s liquidity management has been detailed in the main Treasury report with regard to treasury activities. Before supporting local entities or placing a commercial investment the impact on liquidity is fully addressed, most commonly by taking out loans of an appropriate maturity to ensure funds are available for the life of the activity. £40,000 of seed funding was placed with SRS Ltd in 2011/12 with the intention of it remaining there for the long term to support that entity.

Compared with other investment types, property is relatively difficult to sell and convert to cash at short notice and can take a considerable period to sell in certain market conditions. To ensure that the invested funds can be accessed when they are needed, for example to repay capital borrowed, the Authority will follow its Investment strategy for Commercial assets which ensures that any borrowed capital will be repaid with annual income earned from the investment or that an exit strategy identified during the due diligence will be followed.

**Yield (net profit):** The Authority utilises its profit generating investment activity to achieve a balanced revenue budget. Table C2 below details the proportion of treasury & commercial income to total revenue income and therefore its contribution to meeting the costs of delivery of the Authorities primary functions. Revenue monitoring is carried out for the whole Authority on a quarterly basis. Any Authority wide shortfall, including shortfalls resulting from lower than budgeted returns from Investments, will be addressed as part of that process to bring the Authority’s outturn position back on track.

*Table C2: Proportionality of Investment income to total revenue income*

	2019/20 Forecast £m	2019/20 Forecast £m
Total revenue income	147.3	147.3

Budgeted Profit from treasury investments	0.2	
Budgeted Profit from the 3 newer Commercial Investments		0.7
Proportion	0.14%	0.47%

**Investment advisers:** The Authority has appointed Arlingclose Limited as treasury management advisers and has used Alder King as advisers for the last 2 Commercial investment Property Acquisitions. The quality of these services is controlled by the Internal Estates team and also the Investment Committee appointed to oversee the Commercial Investments.

**Borrowing in advance of need:** Welsh Government guidance is that local 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 Authority, after having regard to the provisions in this guidance has entered into its commercial investments utilising Local Authority investment powers, which allow for the prudent management of its financial affairs where carried out reasonably and in accordance with an authority's primary function to serve the public. Returns from commercial investments help to ensure there are sufficient funds to continue to provide public services.

**Capacity and skills:** The Section 151 officer is responsible for ensuring that those elected members and statutory officers involved in the investment decision making process have appropriate capacity, skills and information to enable them to:

1. take informed decisions as to whether to enter into a specific investment;
2. assess individual investments in the context of the strategic objectives and risk profile of the local authority; and
3. understand how the quantum of these decisions have changed the overall risk exposure of the local authority.

The Audit Committee has a delegated responsibility to scrutinise the treasury management activity of the Authority, which ensures that elected members have the necessary opportunity to assess whether officers are operating within the boundaries of both the prudential framework and the internal boundaries approved within the TMSS. The Audit Committee is provided with training by the Authority's Treasury Management advisers periodically and have been presented with a questionnaire to assess further training requirements.

**Commercial deals:** The investment committee is responsible for ensuring that those tasked with negotiating commercial deals have the appropriate skills and access to information to allow them to operate with regard to the principles of the prudential framework and regulatory regime within which the Authority operates.

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Welsh Government  
**STATUTORY GUIDANCE ON  
LOCAL GOVERNMENT INVESTMENTS**

Issued under section 15(1) (a) of the *Local Government Act 2003* effective for financial years commencing on or after 1 April 2020

**POWER UNDER WHICH THE GUIDANCE IS ISSUED**

1. The following guidance is issued by Welsh Ministers under section 15(1) (a) and 24 of the *Local Government Act 2003*. Under that section local authorities are required to “have regard” to “such guidance as Welsh Ministers may issue”.

**DEFINITIONS OF TERMS**

2. In this guidance, **2003 Act** means the *Local Government Act 2003*.
3. **Local authority** has the meaning given in section 23 of the 2003 Act (and in regulations made under that section). To the extent that this guidance applies to community and town councils and charter trustees (see paragraph 12), a reference to a “local authority” includes those councils and trustees.
4. An **investment** is something held or a transaction which relies upon the power in section 12 of the 2003 Act<sup>1</sup>. That is for any purpose relevant to its functions under any enactment, or for the purposes of the prudent management of its financial affairs. This covers all of the financial and non-financial assets a local authority has invested money into primarily or partially for the purpose of generating a surplus including investment property. As such this may include investments that are not managed as part of normal treasury management processes or under treasury management delegations.

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<sup>1</sup> <https://www.legislation.gov.uk/ukpga/2003/26/section/12>

5. The definition of an investment also covers loans made by a local authority to one of its wholly-owned companies or associates, to a joint venture, or to a third party.
6. The term does not include *pension fund and trust fund investments*, which are subject to separate regulatory regimes and are therefore not covered by this guidance.
7. A **long-term investment** is any investment other than one which is due to be repaid within 12 months of the date on which the investment was made.
8. A **credit rating agency** is one of the following three companies: *Standard and Poor's; Moody's Investors Service Ltd; Fitch Ratings Ltd.*
9. For the purposes of this guidance a **loan** is a written or oral agreement where a local authority temporarily transfers cash to a third party, joint venture, subsidiary or associate who agrees a return according to the terms and conditions of receiving the loan. This definition does not include a loan to another local authority, which is classified as a specified investment.
10. A **specified investment** is an investment which all of the following applies
  - (a) the investment is denominated in sterling and any payments or repayments in respect of the investment are payable only in sterling;
  - (b) the investment is not a *long-term investment* (as defined in paragraph 7) with the exception of a loan to another local authority;
  - (c) the making of the investment is not defined as *capital expenditure* by virtue of regulation 20(1)(d) of the *Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003 [SI 3239 as amended]*;
  - (d) the investment is made with a body or in an investment scheme of *high credit quality*; or with one of the following public-sector bodies:
    - (i) the United Kingdom Government
    - (ii) a local authority in England or Wales (as defined in section 23 of the 2003 Act) or a similar body in Scotland or Northern Ireland
    - (iii) a town or community council.

## APPLICATION

### **Effective date**

11. This guidance applies for financial years commencing on or after 1 April 2020 and supersedes the guidance issued April 2010.

### **Local authorities**

12. This guidance applies to all local authorities in Wales.

### **Town and Community councils and charter trustees**

13. This guidance applies to Town and Community Councils and Charter Trustees with total investments expected to exceed £250,000 at any time during the financial year.

14. All other town and community councils and charter trustees whose investments are not expected to exceed £250,000 shall have due regard to this guidance and give priority to security and liquidity rather than to yield for any investments they undertake. The level of detail and specific requirements outlined in this guidance will therefore not apply but all Town and Community Councils or Charter Trusts should;

- (i) agree a Capital Strategy before the start of the financial year as a minimum; this can be undertaken as a part of the budget setting process;
- (ii) agree appropriate limits for each category of investments it plans to carry out;
- (iii) agree a process that effectively monitors the strategy in year, and;
- (iv) ensure that all investments are in Sterling;

## **INVESTMENT STRATEGY**

### **Preparation**

15. For each financial year a local authority must prepare at least one investment Strategy (“the Strategy”) in accordance with the disclosures and reporting requirements specified in this guidance.
16. The function of a Capital Strategy in CIPFA’s updated Prudential Code is to ‘set out the long-term context in which capital expenditure and investment decisions are made and gives due consideration to both risk and reward and impact on the achievement of priority outcomes. Therefore where a local authority prepares a Capital Strategy in line with the requirements of the Prudential Code, a Treasury Management Strategy in line with the requirements of the Treasury Management Code or any other publicly available document, the disclosures required for the strategy can be incorporated into those documents.

### **Approval**

17. The Strategy should be approved by the full council. For authorities without a full council such as Fire & Rescue Service authorities, the Strategy should be approved at the closest equivalent level.

### **Timing**

18. Welsh Ministers recommend that for any financial year an investment Strategy (“the initial Strategy”) should be prepared and approved before the start of that year.
19. The initial Strategy may be replaced by another Strategy (“the revised Strategy”) at any time during the year, on one or more occasions, subject to the same process of approval. The initial Strategy should specify circumstances in which a revised Strategy is to be prepared, but a revised Strategy may be prepared in other circumstances, if at any time it is considered appropriate.

### **Publication**

20. The initial Strategy and any revised Strategy should, when approved, be made available to the public free of charge, in print or online.

## **KEY POLICY PRINCIPLES**

21. The Strategy should set out the authority's policies for the prudent management of its investments and for giving priority, firstly, to the security of those investments and, secondly, to their liquidity. It should therefore identify the procedures for monitoring, assessing and mitigating the risk of loss of invested sums and for ensuring that such sums are readily accessible for expenditure whenever needed.

### **POWER TO INVEST**

22. Local authority investment powers are for any purpose relevant to its functions and for the purposes of the prudent management of its financial affairs. As with all local authority powers they must be used reasonably and in accordance with an authority's primary function to serve the public, for example, to provide public services and to promote its wellbeing.

### **CLASSIFICATION**

23. Financial and Non-financial Investments made by local authorities can be classified into one of three main categories;

- (i) Investments held for treasury management purposes;
- (ii) Commercial investments; and
- (iii) Other Investments relevant to council functions.

24. Where local authorities hold treasury management investments, they should apply the principles set out in the CIPFA Treasury Management Code. They should disclose the contribution these investments make to the objectives of the local authority to support effective treasury management activities.

25. Local authorities should disclose the contribution that commercial investments i.e. an investment in a for-profit enterprise involved in the buying or selling of goods and services, with the expectation of generating cash flow make towards the service delivery objectives and/or to promote wellbeing.

26. Local authorities should disclose the contribution that other investments make towards the service delivery objectives and/or to promote wellbeing.

27. Local authorities should disclose to what extent investment decisions consider long-term climate risks to support a low carbon economy.

## **Financial Investments**

28. Financial investments can fall into one of three categories;

- (i) ***Specified Investments***
- (ii) ***Loans***; and
- (iii) ***Other Non-specified investments***

### *Specified investments*

29. Where the investment is made with a body or in an investment scheme of *high credit quality*, Welsh ministers recommend that the Strategy should define *high credit quality* (and where this definition refers to *credit ratings*, paragraph 47 is relevant)

### *Loans*

30. A local authority may choose to make ***loans*** to local enterprises, local charities, wholly owned companies and joint ventures as part of a wider strategy for local economic growth. If adopting a narrow definition of prioritising security and liquidity these loans may not be viewed as prudent.

31. However local authorities can make such loans whilst having regard to this guidance if they can demonstrate in their strategy that;

- (i) Financial exposure to these type of loans is proportionate;
- (ii) They have used an allowed 'expected credit loss' model for loans and receivables as set out in *International Financial Reporting Standard 9 Financial Instruments* as adopted by proper practices to measure the credit risk of their loan portfolio;
- (iii) Appropriate consideration has been given to state aid rules and competition law;
- (iv) They have appropriate credit control arrangements to recover overdue repayments in place; and
- (v) The local authority has formally agreed the total level of loans by type that it is willing to make and their total loan book is within their self-assessed limit.

### *Non-specified investments*

32. With regard to ***non-specified investments*** (i.e those not meeting the definition of a specified investment or a loan), Welsh Ministers recommend the Strategy should:

- (a) set out procedures for determining which categories of such investments may prudently be used (and where these procedures involves the use of *credit ratings*, paragraph 47 is relevant);
- (b) identify which categories of such investments have identified as suitable for prudent use during the financial year;
- (c) state the upper limits for the maximum amounts both individually and cumulatively which, at any time during the financial year, may be held in each identified category (the limits being defined by reference to a sum of money or a percentage of the local authority's overall investments or both) and;
- (d) For the overall amount which may be held in non-specified investments confirm that investments have remained within those limits.

### **Non-Financial Investments**

33. As defined in paragraph 4 of this guidance non-financial investments are non-financial assets held primarily or partially to generate a profit. Where a local authority holds a non-financial investment, it will normally have a physical asset or assets that can be realised to recoup the capital invested.
34. Local authorities should consider whether the asset retains sufficient value to provide security of investment using the fair value model in *International Accounting Standard 40: Investment Property* as adapted by proper practices.
35. Local authorities should consider whether the scale of commercial investments including property are proportionate to the resources of the authority and consistent with the requirements of the Prudential Code and the Treasury Management Code.
36. It is vital that local authorities understand the impact of investments in commercial activities in both the medium-term financial plan and longer-term. It is important that local authorities understand the impact of such investments over their term, to ensure there is long-term affordability and financial sustainability/resilience relating to them.

## **SECURITY, LIQUIDITY AND YIELD**

37. A prudent investment policy will have two underlying objectives;

- (i) **Security** – protecting the capital sum invested from loss; and
- (ii) **Liquidity** – ensuring the funds invested are available for expenditure when needed.

38. The generation of **yield** is distinct from these prudential objectives.

However, this does not mean that local authorities are recommended to ignore potential revenues. Once proper levels of security and liquidity are determined, it will then be reasonable to consider what yield can be obtained consistent with these objectives.

### **Security**

39. The Prudential Code sets out clearly that the prime policy objective of a local authority's treasury management investment activities is the security of funds, and that a local authority should avoid exposing public funds to unnecessary or unquantified risk.

40. Where fair value of non-financial investments is sufficient to provide security against loss, the Strategy should include a statement that a fair value assessment has been made within the past twelve months, and that the underlying assets provide security for capital investment.

41. Where fair value of non-financial investments is no longer sufficient to provide security against a material loss, the Strategy should provide detail of the mitigating actions that the local authority is taking or proposes to take to protect the capital invested.

42. Where a local authority recognises a material loss in the fair value of a non-financial investment as part of the year end accounts preparation and audit process, an updated Strategy should be presented to full council. This could be provided as part of the next budgeting setting process and should detail the impact of the loss on the security of investments and any revenue consequences arising from therefrom.

### **Liquidity**

43. For financial investments that are not treasury management investments or loans the Strategy should set out the procedures for determining the maximum periods for which funds may be prudently committed. It should

also state what those maximum periods are and how the local authority will stay within its stated investment limits.

44. For non-financial investments the Strategy should set out the procedures for ensuring the funds can be accessed when they are needed, for example to repay capital borrowed. It should also state the local authority's view of the liquidity of the investments that it holds, recognising that assets can take a considerable period to sell in certain market conditions.
45. Where local authorities hold non-financial investment portfolios they can choose to assess liquidity by class of asset or at portfolio level if appropriate.

#### **Yield (net profit)**

46. Local authorities may consider it necessary to utilise their profit generating investment activity to achieve a balanced revenue budget. Where this is the case the Strategy should detail the extent to which funding expenditure to meet the service delivery objectives and or promote wellbeing in that local authority is dependent on achieving the expected yield. The Strategy should detail the local authority's contingency plans should it fail to achieve the expected yield.
47. The assessment of dependence on profit generating investments and borrowing capacity allocated to funding these should be disclosed as a minimum over the life cycle of the Medium Term Financial Plan. However, an assessment of longer term risks and opportunities is strongly advised.

## **INVESTMENT RISK**

### **Risk assessment**

48. Welsh Ministers recommend that the Strategy should set out the authority's approach to assessing the risk of loss before entering into and whilst holding investments, making clear in particular:

- (a) To what extent, if any, risk assessment is based upon credit ratings issued by one or more credit rating agencies.
- (b) Where credit ratings are used, how frequently credit ratings are monitored and what action is to be taken when ratings change; and
- (c) What other sources of information are used to assess or monitor risk.

### **Treasury management advisers**

49. Welsh Ministers recommend that the Strategy should state:

- (a) Whether and, if so, how the authority uses external advisers offering information, advice or assistance relating to investment; and
- (b) How the authority monitors and maintains the quality of any such service.

## **INVESTMENT OF MONEY BORROWED**

50. Authorities must not borrow more than or in advance of their need purely in order to profit from the investment of the extra sums borrowed.

51. Where a local authority, after having regard to the provisions in this guidance and the CIPFA Prudential Code, decides to depart from any of the explicit provisions of those publications, it will still need to ensure it meets the requirements of the powers and duties afforded by Chapter 1 of the Local Government Act 2003. Additionally the Strategy should;

- (iii) Identify the legal powers that support the proposed transactions;
- (iv) Demonstrate the exercise of these powers are reasonable;
- (v) Explain the local authority's policies in investing the money borrowed, including how it demonstrates value for money and can ensure the security of such funds; and
- (vi) Confirm the authority wishes to proceed by approval from full council.

## **CAPACITY SKILLS AND CULTURE**

52. The Strategy should disclose the steps taken to ensure those elected members and statutory officers involved in the investments decision making process have the appropriate capacity, skills and information to;

- (i) enable them to take informed decisions as to whether to enter into a specific investment;
- (ii) assess individual assessments in the context of the strategic objectives and risk profile of the local authority; and
- (iii) enable them to understand how the quantum of these decisions have changed the overall risk exposure of the local authority.

53. The Strategy should disclose the steps taken to ensure those negotiating commercial deals are aware of the core principles of the prudential framework and of the regulatory regime within which local authorities operate.

54. Where appropriate the Strategy should comment on the corporate governance arrangements in place to ensure accountability, responsibility and authority for decision making on investment activities within the context of the local authority's corporate values.

***Welsh Government November 2019***

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# Asset Investment Policy

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## 1. Introduction

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 policy. The purpose of this paper is to:

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

## 2. Objectives of the policy

2.1 To help sustain Council Services and enhance the asset base by investing in commercial property assets in order to increase the net rental income stream for the Council.

2.2 The Council's Corporate Plan 2017 – 2022 identifies five priorities, the last of which is a "future focussed Council". One of the key measures for this is *income generation from commercial investments*. This policy will provide the framework for the evaluation of potential commercial property investments.

2.2 We will actively seek out investment opportunities within the County of Monmouthshire, City Deal geographical boundary and neighbouring areas of economic influence which will support our economic and regeneration priorities. In order to manage and spread the risk we will also identify investment options beyond our county boundaries which meet our criteria.

## 3. Purpose of the Policy

3.1 The purpose of this policy 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 Criteria are met –In accordance with financial parameter's detailed below*
- *Investment Criteria are met – in accordance with the investment criteria detailed below.*

3.2 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.

##### *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.

We have obtained specific advice 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

Welsh Governments White Paper, *Reforming Local Government: Resilient and Renewed*, makes provision for the introduction of the general power of competence for Welsh local authorities to bring us in line with the powers already held by our English counterparts. The WLGA have advised that the White Paper proposals will provide powers which will allow 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.

## 5. Financial Criteria

Individual acquisitions should meet the criteria set out below, acquisitions outside these criteria will require approval by Cabinet with a supporting business case and reasons for deviating from the agreed protocols.

- 5.1 Target Fund Value - £50 Million Pounds over a three year timeframe to be reviewed annually.
- 5.2 Maximum Lot size        No greater than 20% of the Target fund value
- 5.3 Minimum Return - total cost of borrowing (interest and repayment) Target Income Return – 2% above the annual cost of borrowing (interest and repayment). Where the acquisition will result in net economic growth to Monmouthshire (through the provision of jobs, additional employment floor space, local regeneration etc) the Investment Committee can adopt a lower return, but the return cannot be lower than 0%.
- 5.4 Target Total Return - 7% per annum, to be reviewed annually to reflect prevailing market conditions.
- 5.5 Minimum Repayment Provision (MRP) will be assessed on a case by case basis by reference to the economic life of the land and buildings but in all cases will not exceed 50 years.

## 6. Acquisition & Governance Framework

- 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 rules laid down by the relevant professional bodies. All valuations must be undertaken by a qualified<sup>1</sup> member of the Royal Institution of Chartered Surveyors with knowledge of the relevant local and specialist markets.
- 6.2 All potential investment acquisitions will be assessed against the following Investment Criteria at both a portfolio and asset level
- Location
  - Quality
  - Tenure
  - Portfolio blend
  - Strength and security of Income
  - Income and Capital growth potential
  - Potential Landlord Liabilities

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<sup>1</sup> MRICS or FRICS

- Identifiable Risks
  - Development and added value opportunities
  - Economic, Regeneration and other Key Council priorities
- 6.3 All proposed acquisitions will need to be the subject of a Business Case which will be created in conjunction with the Council's Finance team. The report will consider both the Financial and Investment Criteria
- 6.4 The Business Case will be presented to the Investment Committee which will be made up 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 Resources Chief Officer and Officers from Finance, Estates and Legal Services.
- 6.5 The Investment Committee will have delegated authority to make prudent decisions on the acquisition of investments utilising the £50,000,000 allocated borrowing. There will need to be 3 members in attendance for the meeting to be deemed quorate.
- 6.6 All acquisitions will be subject to
- An independent valuation report supporting the purchase price
  - Satisfactory building survey and assessment of economic life
  - Satisfactory report on title

## 7. Review Principles

- 7.1 An annual performance review of the Investment Committee and any acquisitions will be undertaken and reported to Audit Committee to ascertain performance against the following criteria:
- Governance arrangements and adherence to policy
  - Relevant Market indexes
  - Property performance locally
  - Capital, Income and Total returns.
- The Investment Strategy will be reviewed annually and adjusted to reflect prevailing market circumstances.
- 7.2 In the event that a property holding is deemed to be underperforming or fails to meet any debt repayment 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
- 7.3 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.

7.4 Where the asset is located away from the County or has specific management skill requirements, external agents may be instructed to manage it on our behalf, all costs incurred will be deducted from the gross annual return.

## 8 Risks

8.1 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.

8.2 Illiquidity - In the event that a property needs to be sold to generate capital funds the disposal process will generally take in the region of 6 – 12 months to complete, dependent on the prevailing market conditions.

8.3 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.

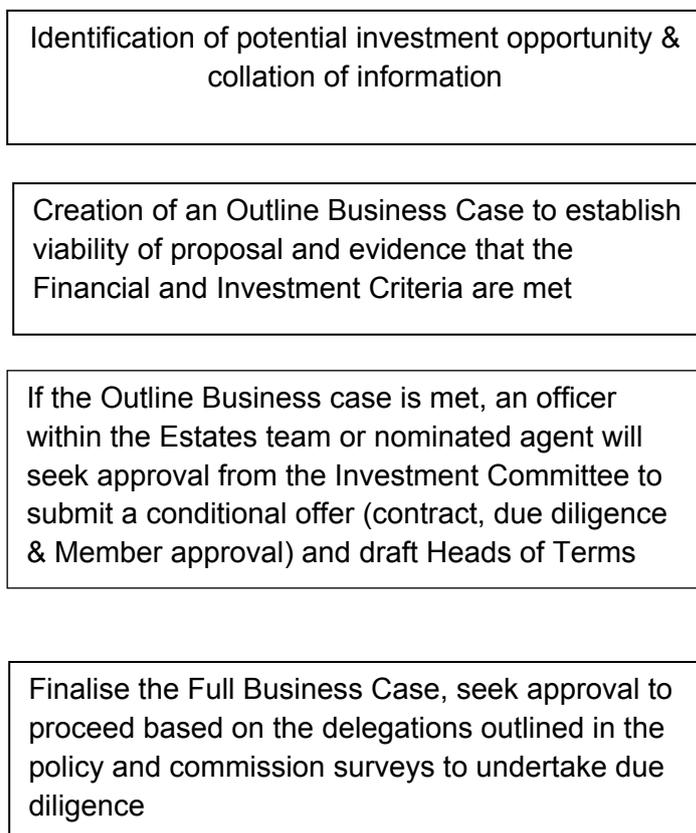
## 9. Purchasing and Finance.

9.1 - The Council benefits from the ability to access funding from the PWLB at relatively low interest rates and fixed repayment terms enabling the acquisition of land & property assets

9.2 - Alongside the purchase price the Council will incur fees at the point of purchase such as Legal and specialist fees, Land Transaction Tax and VAT. In the event no revenue funding is available these will be treated as Capital costs and aggregated into the total borrowing required.

9.3 A fund will be created to top slice net rental income to manage repairs, maintenance, staff resources and improvements, to prevent the portfolio becoming a net cost to the authority.

### 10.1 - Governance & Purchase Flow Chart



Commence legal process for purchase of the investment. Until exchange of contracts, all negotiations and investigations will be on a 'subject to contract' basis.

Exchange contracts. Council now financially committed to purchase.

Pre completion searches and arrange draw down of funds to complete transaction.

Post completion - payment of Land Transaction Tax and other fees, make arrangements for rental payments and ongoing property / portfolio management.

Complete Transaction, assume liability for the property. Update relevant colleagues internally and update terrier and other databases.

Undertake annual assessment to review financial return and compliance with policies outlined in this policy.



## Terms of Reference – Investment Committee

Purpose:	To hold strategic oversight and responsibility for the implementation of the Asset Investment Strategy.
Membership:	The Committee shall be made up of the Leader, Deputy Leader, Cabinet Member for Resources and the Leaders of the two largest Opposition Parties. This reflects the political balance of the current administration and will be subject to review following a local government election within the Monmouthshire Constituency to ensure that the political balance remains.
Chairman:	The Leader of the Council
In attendance:	Leader of the Liberal Democrats Chief Executive Chief Officer, Resources Head of Legal Services Head of Commercial and Integrated Landlord Services Head of Finance Monmouthshire County Council Officers as required Specialist advisors as required
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 investment opportunities arise on an ad hoc basis and will meet a minimum of 2 times a year to review the performance of the investment portfolio.

## Terms of Reference

1. The Committee will take decisions on the acquisition of investment land and property and development opportunities
2. Scrutinise business cases and ensure that they are in accordance with the approved Asset Investment Policy.
3. Keep under review the performance of the asset investment portfolio, ensuring that it meets the agreed financial benchmarks within the Asset Investment Policy and that identified risks are actively managed.
4. Agree mitigation and exit strategies for poorly performing assets.
5. Provide an annual position statement for Audit Committee to review on the asset investment portfolio.
6. To execute the powers of authority delegated by Council.

7. Members will act in the best interest of the corporate entity.