Arun District Council

Property Investment Strategy 2017-2022

Author: **Paul Broggi - Property and Estates Manager**
Adopted 13 September 2017

ARUN
DISTRICT COUNCIL

Contents

page

Property Investment Strategy

1. Purpose 2
2. Background 2
3. Strategy Aim 3
4. Key considerations for acquisitions 3
5. Financial Considerations 3
6. Property Investment Risk 4
7. Corporate Implications 4
8. Governance Arrangements 5

1. Purpose

The purpose of this strategy is to set out the following:

- The Council's objectives for acquiring property assets as a form of investment.
- The financial implications of the Property Investment Strategy and the establishment of a Property Investment Fund.
- The key risks associated with property as an investment and the processes that will be undertaken to identify, assess and mitigate those risks.
- The Corporate implications of the Property Investment Strategy.

2. Background

The current uncertainty regarding Central Government funding means that Councils need to identify alternative methods of generating income.

As a result there has been increasing pressure on Councils to generate income from their assets. The aim of the Property Investment Strategy is to provide a broad set of principles for the Council to undertake property acquisitions with the aim of generating a return for the Council.

- **Asset Portfolio**

Arun's current general fund asset portfolio comprises corporate properties that are occupied by Council departments, properties which are leased out and properties that are used for community facilities together with land and structures for communal use.

The portfolio consists of 109 properties that generate income for the Council. Annual income generated is circa £575k from the rental of these properties. These properties consist of:

  - Properties predominantly held for service delivery (these assets also create an income stream from rental of part of the buildings), generating an income of £28,160;
  - Lease properties, generating an income of £487,662;
  - Leased properties – Concessionary Rentals (these properties have been let at a less than market value to organisations that provide a service to the community), generating an income of £10,589;
  - Concessions, generating an income of £48,776.

- **Asset Reviews Process**

Asset reviews are undertaken to establish the extent to which assets are to be retained, disposed of or amended to bring the performance of those assets into line with the Councils policies and requirements. Where possible, this involves lease restructuring, reviewing existing use and lease terms. This can sometimes be restricted by the terms of the lease and each case must be reviewed individually.

As part of the Asset Review process the Council has reviewed its accommodation at the Civic Centre in Littlehampton and has relocated staff within the building in order to free up ground floor office space.

The Council's review its general fund assets on an on- going basis. Many existing leases are fixed under contract and so the Council is unlikely to be successful in obtaining variations to these leases unless the leaseholder(s) were in agreement. As and when leases are either due to end or they come up for rent review Property & Estates are taking a commercial approach in order to ensure that best value is attained.

3. Strategy Aim

The aim of the Strategy is to ensure a long-term increased source of income from a balanced property investment portfolio. This income stream can then be used by the Council to maintain, extend or improve service delivery.

The strategy for acquiring property investments will aim to:

- Maximise rental income and minimise operational and management costs to ensure the best return is generated for the Council.
- Pursue opportunities to increase financial returns (rental receipts and capital appreciation) and improve the investment value of commercial assets.
- Promote collaborative working with adjoining owners, developers and other external stakeholders in order to maximise value.

The Property Investment Strategy covers a 5 year period (2017 – 2022) and will be reviewed and updated bi-annually.

4. Key considerations for acquisitions

There are a number of factors that determine the return on an individual property and these will be considered for each potential investment.

These factors are:

- **Covenant Strength** – the ability of the tenant to pay the rent on time and in full. It is important to note that the Council will not invest in properties where the occupiers are generally seen to be undertaking activity which is contrary to its corporate values.
- **Lease length** – the unexpired length of the term of the lease is important in ensuring that the landlord's revenue stream is uninterrupted.
- **Rate of return** – the rate of return from the property (rental receipts), will need to be at least comparative to the returns that could be earned from alternative investments (subject to adjustments for risk and potential growth).
- **Risk** – the level of associated risk and the Council's appetite for risk must be considered. Generally, the level of risk will be higher where the return is higher. Whether this risk is acceptable to the Council must be considered in conjunction with the associated return.
- **Growth** – the Council will take into account the potential for both revenue and capital growth when assessing the strength of the potential investment.
- **Sector** – the sector of use of the property will be considered to assist in determining risks associated with that specific property sector. It will also be considered for the portfolio as a whole so that risk is adequately diversified.
- **Building age, condition and specification** – this will impact the Councils ability to lease the property and its potential capital appreciation.
- **Location** – the location is critical and will ideally enable the Council to undertake inspections and deal with management issues itself. It is intended that investing in the district should be the primary focus for property acquisitions. However, if the supply or quality of suitable new acquisitions should not be available or they are considered financially unviable within this area, opportunities over a wider geographical area may be considered. In accordance with the Localism Act 2011, the Council has the power to acquire property investments outside the district in line with the proposed Property Investment Strategy. Ultimately, any additional income will contribute to the funding of the Council's service delivery.
- **Other -** The Property Investment Strategy recognises that the financial return is not the sole factor for determining whether to proceed with an investment. It recognises the importance of wider socio-economic impacts i.e. community/ regeneration and will give due regard to these in line with the Council's overall strategic objectives.

5. Financial Considerations

The Property Investment Strategy sets out the broad principles governing the property investments that will be undertaken by the Council in the future.

The aim of these investments is to provide secure, long-term and sustainable income streams for the Council. This will ultimately enable the Council to improve its financial resilience and become less reliant on Central Government funding.

Returns from property can be both income driven (rental receipts), and by way of appreciation of the underlying asset value (capital growth). The total return these two elements provide will be the key consideration in assessing the attractiveness of a property for acquisition.

For each property investment, careful consideration will be given to the property type, age, condition and location, together with the lease structure and covenant strength of the tenant (in respect of leased properties). These are fundamental influences on the property price and returns.

The additional rental income generated from investments will provide the Council with an income stream with a view to maintain, extend or improve service delivery. Income generating activities reduce the potential for further service cuts.

The availability of funds and the speed of the decision making and approvals process is critical to enable officers to respond quickly to investment opportunities in the property market.

5.1 Property Investment Fund

To achieve the objectives of the Property Investment Strategy, it is recommended that a Property Investment Fund is established. The Property Investment Fund will not require any external borrowing as funds generated from existing Land and Property disposals will be used.

It is proposed that 75%, of any sale proceeds from land and property disposals, is automatically allocated to the Property Investment Fund within the Property and Estates Budget. Funds will be replenished by ring fencing capital receipts from the sale of non- operational properties identified.

Any expenses directly attributable to any purchase, will in accordance with accounting regulations, be charged to the Property Investment Fund as part of the cost of acquisition, and will therefore be taken account as part of the overall evaluation of the property acquisition.

6. Property Investment Risk

The Property Investment Strategy recognises that any form of investment is not without risk. The value of any investment can fluctuate over time, especially long- term investments.

The Key Risk factors specific to property investment are:

- **Acquisition Risk** – the Council may incur transaction costs without guarantee of securing the investment (e.g. the Council may be one of several bidders, or is required to pay a premium);
- **Price and cost risk** – once acquired the price or cost of the investment may fluctuate over time, which may in itself reflect variations in demand and supply;
- **Economic/ political risk** – the ability to retain or dispose of an investment may be inhibited by the economic and/ or political environment at any point in time;
- **Market Risk** – the Council's ability to influence the price, financial return or other benefits pertaining to the investment may be limited by the market in which it operates.

Risk management

The consideration of any investment will include a risk assessment that will aim to measure, as objectively as possible, the likelihood and the severity of the impact should the risks identified be realised. This will form part of the decision making process, enabling the potential benefits (financial or otherwise) to be considered in conjunction with the risks.

The Council will acquire property which produces the highest yields possible, whilst carrying an acceptable level of risk.

A process of due diligence will be undertaken prior to each completion as this is critical to the mitigation of most property risks.

The portfolio of property investments will be grown steadily, with a variety of different property assets in order to spread the risk. This represents a relatively low risk- approach to property investment.

Each case will be subject to a business case, demonstrating viability and appropriate approval will be obtained prior to completion of purchase.

Disposal of properties

The decision to sell properties may be triggered by a variety of factors and is not limited to lease events, market forces, portfolio mixes or changes in strategy. The portfolio will be open to continued appraisal and active management with a view to minimising risk and increasing returns

Should the need for any such disposal occur, it is proposed that the procedure set out in the Council's Standing Orders will be adhered to.

7. Corporate Implications

7.1 Legal Considerations

Generally, the Local Government Act 1972 empowers Councils as follows:

> *"a local authority shall have a power to do anything (whether or not involving the expenditure, borrowing or lending of money or the acquisition or disposal of any property or rights) which is calculated to facilitate, or is conducive or incidental to, the discharge of any of their functions"*

(Part VII, Section 111).

In exercising this power, the Property and Investment Strategy aims to obtain a mixed portfolio of property investments (land and property) that spreads both the return and risks.

7.2 Resources

The purchase of additional properties will require officer resources (finance, legal and property), related not only to the purchase, but also to their ongoing management.

The Property Investment Fund will be utilised to fund professional/ consultancy fees associated with the disposal and/ or acquisition of assets.

It is envisaged that the property investments will be grown steadily and as such it is anticipated that no additional resources will be required.

8. Governance Arrangements

The Councils current governance structure does not allow the Council to react quickly enough to property investment opportunities due to the timescales associated with the Individual Cabinet Member (ICM) decision requirements (prior notice of decision and call in period after the decision).

It is important that the Council is perceived as a serious investor within the property market. It is recommended that the current governance arrangements and the Council's Constitution are revised to ensure that the Council can react quickly to opportunities that arise

It is also recommended that the delegated authority levels within the Constitution are revised to:

The authority to approve the acquisition of commercial properties from the Property & Investment Fund ***up to a maximum value of £750,000 per acquisition*** *is delegated to the Director of Place in conjunction with the Cabinet Member for Technical Services and the Section 151 Officer,* ***subject to a viable business case.***

It should be noted that each case must be supported by a business case that proves that the acquisition will be viable, prior to commitment to purchase.

8.2 Reporting and Monitoring

It is proposed that the monitoring and scrutiny of any activity be undertaken by the Audit and Governance Committee via a quarterly report.

Property acquisition and/or disposal matters will also be reported through the Councils Asset Management Group.

Following the recent restructure Property & Estates are working on setting relevant service performance indicators and this will include reporting on increased revenue generation.

ARUN DISTRICT COUNCIL

Arun District Council
Civic Centre
Maltravers Road
Littlehampton
West Sussex
BN17 5LF

01903 737500
www.arun.gov.uk

Author: **Paul Broggi - Property and Estates Manager**

Adopeted 13 September 2017

Designed and printed by Arun District Council 18-01-19