Bath & North East Somerset Council		
DECISION MAKERS:	**Councillor Tim Warren, Cabinet Member: Leader of the Council** **Councillor Charles Gerrish, Cabinet Member: Finance and Efficiency**	
DECISION DATE:	**On or after 16th February 2019**	EXECUTIVE FORWARD PLAN REFERENCE: E
TITLE:	Acquisition of income generating investment to incorporate within the Commercial Estate to move to full approval from provisional.	
WARD:	N/a	
AN OPEN REPORT CONTAINING EXEMPT APPENDICES		

List of attachments to this report:

Appendix One – Business Case (Exempt by virtue of Paragraph 3 of Schedule 12A of the Local Government Act 1972)

Appendix Two – Valuation Report (Exempt by virtue of Paragraph 3 of Schedule 12A of the Local Government Act 1972)

Appendix Three - B&NES Commercial Estate Investment Strategy 2018-19 http://www.bathnes.gov.uk/sites/default/files/banes_investment_strategy.pdf

1 THE ISSUE

1.1 This report sets out the terms of the proposed acquisition of income generating investment property to move to full budget approval from provisional budget approval.

2 RECOMMENDATION

The Cabinet Members are asked to approve:

2.1 The acquisition of an investment property which is in line with MHCLG guidelines as it is within the Bath and North East Somerset boundary.

2.2 Capital expenditure on the acquisition of the property and any necessary adjustments to the 2018/2019 capital budget to reflect this approval.

3 RESOURCE IMPLICATIONS (FINANCE, PROPERTY, PEOPLE)

3.1 A budget of £47.5m was provisionally approved by Council in February 2018 for property acquisitions and is currently forecast at £43.7m for 2018/19 in the Council budget setting papers. Release of this funding is subject to a business case for each investment opportunity. Total cost of the proposed acquisition is £18,930,000. This includes an estimated budget in respect of professional fees (as the due diligence is on-going) and contingency.

3.2 This report requests the full approval of the capital spend on the acquisition of the property, which is the subject of this report.

3.3 This proposal links to the already approved Medium Term Service Resource Plan which places a requirement to generate an additional £1.475 million net of income from the Commercial Estate as part of the 2017-18 to 2019-20 budget period.

3.4 The acquisition costs will be funded by service supported borrowing, costs of which have been factored in against future rental income projections. The business case assumes long term borrowing for the entire purchase and on this basis the level of annual rent of £980,624 offers good value for money as it delivers net income after borrowing costs on an annual basis of £279,439 which is a 1.48% yield on the initial investment, as well as providing the economic benefits as set out in paragraph 4.5 of this report.

4 STATUTORY CONSIDERATIONS AND BASIS FOR PROPOSAL

4.1 Changes were introduced by The Ministry of Housing Communities and Local Government (MHCLG) to the Prudential and Treasury Management Codes in February 2018 which covered the following areas:-

- **Transparency and democratic accountability**
  The revised guidance retains the requirement for an Investment Strategy to be prepared at least annually and introduces some additional disclosures to improve transparency. The changes to the CIPFA Prudential Code include a new requirement for local authorities to prepare a Capital Strategy. (The strategy must be in place for 2019/20 and will be approved as part of budget setting for 2019/20. A Commercial Estate Investment Strategy 2018/19 was included as part of the budget setting proposals for 2018/19 and is attached at Appendix 3).

- **Principle of contribution**
  This requires local authorities to disclose the contribution that non-core investments make towards core functions. Authorities' core objectives include 'service delivery objectives and/or place-making role.' This clarification has been made to recognise the fact that local authorities have a key role in facilitating the long term regeneration and economic growth of their local areas and that they may want to hold long term investments to facilitate this.

- **Introduction of a concept of proportionality**
  This requires local authorities to disclose their dependence on commercial income to deliver statutory services and the amount of borrowing that has been committed to generate that income based on an understanding of the overall risk that they face.

- **Borrowing in advance of need**
  By bringing non-financial investments (held primarily or partially to generate a profit) within the scope of the Investment Guidance, it is clear that borrowing to fund acquisition of non-financial assets solely to generate a profit is not prudential. The Investment Guidance requires local authorities who have borrowed in advance of need solely to generate a profit to explain why they have chosen to disregard statutory guidance. The assumption is that any out of area purchases are only held for this purpose. This is not applicable in this case as it is not an out of area acquisition.

4.2 In terms of the Corporate Strategy the acquisition has direct relevance in the following areas:

- A strong economy & growth – The Council is able to exercise active management over its property holdings and seek to ensure a varied portfolio mix and diversification of risk.

- An efficient business – the acquisitions contribute significantly towards achieving the Council's strategic review targets as well as the Directorate Plan income generation aspirations.

4.3 In line with the Council's Financial Plan the income will support the provision of frontline services, including adult social care; children; and environmental services pursuant to the Council's general power of competence under s.1 Localism Act 2011.

4.4 The acquisition of the property is in pursuance of the benefits (and in particular those of an economic nature) that it will confer upon the Council and its area, in accordance with s120 of the Local Government Act 1972. The acquisition aligns itself with the Council's Investment Strategy for the Commercial Estate.

4.5 The economic benefits conferred to the Council and its area specifically include:

4.5.1 Diversification and mitigation of risk to the portfolio, in terms of sub-sector and type;
4.5.2. Council resourcing - the acquisition will provide resources required to support the provision of frontline services, which benefits the Council and its area directly; and
4.5.2. Opportunity – There are limitations in terms of demand and supply within the geographic area.

5 THE REPORT

5.1 The Council has been given an opportunity to purchase an investment property which is held freehold in an 'off market' transaction.

5.2 The property is within the Local Authority area boundaries.

5.3 The investment opportunity is let to three tenants. The leases vary in length and covenant strength. The first lease event is an expiry in March 2023, followed by other possible lease events, in 2031 and 2043. The rent is £980,624 per annum and after payment of the Council's debt costs (based on the expected annuity loan rate, and the assumed acquisition date of 1st March 2019), a net income of £279,439 per annum, after the first year, will be receivable.

5.4 A purchase price of £17,850,000 has been agreed in principle. In addition the Council's acquisition costs total £1,080,000.

5.5 There is a service charge which is payable by the tenants (based on their respective gross internal areas, as a percentage of the gross internal.) We understand that there is 100% recovery. The service charge budget for the period expiring 31 March 2019 is £77,803, and the previous year's budget was £76,697.

5.6 Due diligence is underway and is on-going.

5.7 At the time of reporting Creditsafe Ratings for the tenants considered the investment to be secured by strong covenants.

5.8 The units are capable of being split further or alternatively re-configured on site if future redevelopment was considered. Notably there are various rights of access afforded which would need to be contemplated.

5.9 In accordance with the Commercial Estate Investment Strategy 2018/19 the Council is looking to diversify its portfolio. However due to the lack of suitable investment product within the Council's own geographical area, this is an opportunity to acquire accommodation within its border and diversification of asset type, albeit within the same sector.

5.10 External acquisition Agents have been engaged to assist with the purchase and also an independent Valuer to support the business case.

5.11 The investment has not been brought to the open market although discussions have been on-going with the Vendor's agent due to the Council being considered to have a 'special' purchaser interest.

5.12 An independent valuation report has been commissioned for the proposed acquisition and it is contained at Appendix Two. This confirms the purchase price represents market value. The report states that the agreed purchase price and resulting yield profile produced falls within the higher range of what they deem acceptable to investors and may not be replicated in the market. However, they are of the opinion that it represents the market value of the Property.

5.13 Location and site plans are included in the Valuation Report in the Appendix.

5.14 The offer made to date is subject to Cabinet Member approval to the items contained in the 'Recommendation' section above.

5.15 The acquisition is to be funded principally through long term borrowing.

5.16 More detailed analysis of the acquisition and supporting business case is provided within the appendix attached to this report.

5.17 The investment was introduced to the Council by an investment agent working for an independent firm. The investment was introduced in November 2018, although the property was not placed ‘under offer’, with agreement to heads of terms until 19th December 2018. These terms set out a timetable for exchange and completion of the acquisition and which necessitate the use of the special urgency provisions.

6 RATIONALE

6.1 The rationale for these decisions is largely on a value for money basis, having considered the risks to the Council of not taking them. Documents to support the rationale are contained in the Appendices.

7 OTHER OPTIONS CONSIDERED

7.1 None

8 CONSULTATION

8.1 The decision is being taken under the special Urgency provisions of the Council’s constitution (Rule 15). The Chief Executive, Monitoring Officer (Head of Legal and Democratic Services), Section 151 Officer (Chief Financial Officer) and the Corporate Director responsible for Economy and Growth have been consulted. The Chair of the Resources Policy Development and Scrutiny Panel has been informed.

9 RISK MANAGEMENT

9.1 A risk assessment related to the issue and recommendations has been undertaken, in compliance with the Council's decision making risk management guidance.

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<tr><td>Contact person</td><td>Richard Long 01225 477075/07980 998 589</td></tr>
<tr><td>Background papers</td><td>None</td></tr>
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