

# Report

## Cabinet

---



### Part 1

Date: 17 July 2019

**Subject** Commercial Property Investment Guidelines

**Purpose** In line with previous decisions on the establishment of a Commercial Property Investment fund, to recommend and approve the 'investment guidelines' for use by the Investment Board when reviewing and selecting potential acquisitions.

**Author** Head of Finance

**Ward** All

**Summary** Cabinet approved an approach to commercialisation in their March 2019 Cabinet, which included, amongst other things, the establishment of a £50m Commercial Property Fund. This would be invested and net returns, after costs, would contribute towards the solution to the Council's on-going financial challenge. Council approved the approach within the Capital Strategy and the necessary borrowing headroom in their April meeting.

An investment Board, a sub-group of the Cabinet, is being set up to make decisions on the investment opportunities and this report recommends the 'investment guidelines' which they would use when reviewing and recommending investments from this fund.

**Proposal** (1) To review and comment on the 'investment guidance' at the end of this report  
(2) To approve the guidance for use by the 'Investment Panel' when reviewing and recommending property investment opportunities

**Action by** Head of Finance – distribute to Investment Board Members and officer advisory group

**Timetable** Immediate

This report was prepared after consultation with:

- Chief Executive
- Strategic Directors
- Head of Legal and regulatory services
- Newport NORSE

**Signed**

## **Background**

### **Establishment of the Council Commercial Property Fund**

As the Council faces on-going financial challenges, the Cabinet considered a commercialisation strategy in their March 2019 meeting. Growing external income as one approach to closing the medium term forecasted funding gap was agreed. Amongst other aspects to this, the Cabinet agreed to the creation of a 'Commercial Property Fund' of £50m which would be used to invest in commercial property and generate a net financial return, after borrowing and other associated costs. Subsequent to that, in April, the full Council agreed the approach in the Council's Capital Strategy and authorised the necessary borrowing headroom to make available the £50m.

Cabinet agreed that investment decisions would be delegated to an 'Investment Panel', a sub-group of Cabinet. The panel would be supported by officers and Newport NORSE and, where required, external advisers.

In line with good governance and to manage the risk in undertaking this activity, Cabinet also agreed that an 'investment criteria' should be established to guide the Board in their review of potential investment and opportunities.

### **Investment Criteria**

The draft 'Investment Criteria' is appended to this report and the Cabinet is asked to review this and adopt / make changes as appropriate.

The criteria stipulates two 'must do/have' criteria, as follows:

- Diversification criteria – set's maximum amount of the fund that should be invested in different property sectors
- All investments should make a positive net financial return, after relevant costs

Beyond these, the criteria is a guide to enable comparison of different opportunities and to build a strong, secure range of investments which provides acceptable financial returns to the Council, as the fund was set up to achieve.

The criteria will not mean that this activity is 'risk-free' and stop 'losses' as there is inherent risk in this activity but should provide a good framework for the panel to assess opportunities and make decisions from a considered position. It will contribute towards the well managed review of opportunities and inherent risks and therefore good governance.

### **Applicability**

The guidance is for use when reviewing/assessing property opportunities to be funded from the Commercial Property Fund. This investment type is one of three in terms of the different investment activities in the Council's Capital Strategy:

- (1) Treasury Investments - those investments which arise from the organisation's cash flows and debt management activity, and ultimately represent balances which need to be invested until the cash is required for use in the course of business. This is managed through the Treasury Management Strategy
- (2) Operational (Service) Investments – those investments held clearly and explicitly in the course of the provision, and for the purposes, of operational services, including regeneration.
- (3) Commercial Investments – investments primarily taken for financial reasons with aim of making a financial surplus for the Council, which could include investment properties as well

as other activities such as shares in subsidiary companies etc. Activities guided by the investment guidance here fall into this category.

There is a degree of overlap between operational and commercial investment types in that operational investments could sometimes generate a financial return or that commercial investment include a regeneration benefit. The differentiation mainly comes down to what is the primary reason for the investment. The draft 'Investment guidance' recognises this and the investment criteria recommended includes the ability of the commercial investment to benefit the local economy/create jobs, with the primary reason to generate a financial return to the Council.

## Financial Summary

The primary reason for the Commercial Property Fund is to make a financial return to the Council. There is no budget target currently included in the Council's Medium Term Financial Projections for this and this will need to be developed.

As the investment guidance says, any net financial benefit is after associated costs, which will include, amongst other things, capital financing charges, direct costs related to that investments and provision for required life-cycle costs where appropriate.

Therefore, the cost of borrowing related to the £50m, when invested, should be recovered through the income generated from that spend.

The Income/Costs associated with this fund will be reflected in the Councils current commercial/industrial service activity area, and structured separately to ensure the Council can report and manage the performance of the fund.

## Risks

Risk	Impact of Risk if it occurs* (H/M/L)	Probability of risk occurring (H/M/L)	What is the Council doing or what has it done to avoid the risk or reduce its effect	Who is responsible for dealing with the risk?
Investment Fund makes losses	H	L	Investment Panel with advisers  Investment guidelines, in particular diversification  Appropriate returns providing a margin for any reductions / issues	Investment Panel  Advisers
Investment Panel do not follow guidelines	H	L	Need to refer back to Cabinet if risk occurs  Advice provided in Panel meetings	Investment Panel  Advisers

\* Taking account of proposed mitigation measures

## Links to Council Policies and Priorities

The objective of the Commercial Investment Fund is to make a net financial return which will contribute towards the funding of Council services. Therefore, to the extent services meet Council priorities and policies, this initiative positively contributes towards that.

## **Options Available and considered**

The Cabinet has already agreed to carry out this investment activity. The guidelines here recommend how the investment panel considers opportunities. In that respect:

- Cabinet can approve the draft guidelines appended to this report
- Cabinet can suggest changes, taking advice from relevant officers

## **Preferred Option and Why**

Cabinet need to agree a commercial property investment guidelines and are recommended to approve the one appended to this report, which has been drafted after researching those used by other Councils undertaking this activity.

## **Comments of Chief Financial Officer**

These guidelines have been put in place to clarify the governance arrangements the investment panel need to follow when making decisions on this type of activity.

The key issues and risks from making these types of investment were outlined in the report both to Cabinet and Council where it was agreed to proceed with commercial property investments and the associated investment fund.

## **Comments of Monitoring Officer**

The proposed Investment Strategy is in accordance with the Council's general powers to invest and prudentially borrow for the purposes of discharging its functions and for prudent financial management under of the Local Government Act 2003. The Council also has legal power to acquire land and property assets, both inside and outside its area, under section 120 of the Local Government Act 1972. Any borrowing and property investment must comply with Prudential and Treasury Management Codes and the Council's capital strategy. Full Council has resolved to establish a £50m property investment fund and has approved a revised capital strategy as part of the policy framework under the Constitution. However, any investment decisions will be an executive function for the Investment Board, which will need to be established as a sub-committee of Cabinet, with delegated powers. The draft Investment Strategy sets out a proposed framework and parameters for the Board to take investment decisions, having regard to the security and liquidity of any investments and the appropriate balance of risk and reward. Any investment decisions which fall outside the parameters set by the Strategy will need to be approved by full Cabinet.

## **Comments of Head of People and Business Change**

The proposed guidelines set out a framework in relation to the property investment fund which is intended to create an additional income stream for the Council. Commercial investment income is one of the ways the Council is aiming to achieve financial sustainability over the longer term in order to support core service delivery. In addition to income generation the fund will aim to support the local economy in key sectors which are decided in collaboration with the Newport Economic Network. The guidance sets out governance arrangements which will help ensure a balanced portfolio to reduce exposure to individual sector risk. There are no human resources implications in this report.

## **Comments of Cabinet Member**

The Chair of Cabinet, as Cabinet Member for Strategic Finance and Chair of the Investment Panel has reviewed the guidelines and approved it for consideration by Cabinet.

## **Local issues**

There are no specific issues though the criteria favours Newport property investments over other locations

## **Scrutiny Committees**

N/A

## **Equalities Impact Assessment and the Equalities Act 2010**

N/A

## **Children and Families (Wales) Measure**

N/A

## **Wellbeing of Future Generations (Wales) Act 2015**

The objective of the Commercial Investment Fund is to make a net financial return which will contribute towards the funding of Council services. Therefore, to the extent services meet the requirements of the Act, this initiative positively contributes towards that.

The Investment Fund has been agreed at £50m funded from borrowing and when utilised, will represent a long-term revenue liability for repayment of that borrowing. Therefore, it will be important that the investment themselves make returns above all associated borrowing and other costs and maintained over the long-term. If this is not achieved, the investments will not cover costs and could be a 'cost' on general council finances in the future.

## **Crime and Disorder Act 1998**

N/A

## **Consultation**

N/A

## **Background Papers**

Cabinet meeting March 2019 – recommendation of approach, setting up the Investment fund and Panel

Council April 2019 – approval of the approach and commercial property investment into the Council's Capital Strategy and borrowing facility of £50m

Dated: