CITY OF YORK COUNCIL

Executive Member for Corporate Services and Advisory Panel

10 June 2008

Report of the Corporate Landlord

Review and Strategy for the Commercial Property Portfolio – Future Investment Strategy

Summary

1 Further to the full Review and Strategy Report approved by Corporate Services EMAP on 30 October 2007 and the Executive on the 20 November 2007, Executive resolved that a further report be brought back before the Executive Member for Corporate Services and Advisory Panel outlining the future investment strategy for the Commercial Portfolio. Council then resolved on 21 February 2008 that a report be commissioned to review the Commercial Property Portfolio and made available a budget to enable external consultants to be engaged if necessary.

This report therefore is to combine both aspects ; It reports back on the strategy outlined at Corporate Services EMAP and Executive, and gives options for allocating the budget made available at Council. It suggests two options for Member's consideration;

a. To utilise the additional budget made available at Council in February to contribute towards the strategy outlined in principle at Executive in November , which is the sale of some secondary properties and reinvestment of the receipts, and

b. To utilise the additional budget to appoint finance / property consultants to undertake a wider reaching review , including looking at investing in other than property

Background

2. The Commercial Property Portfolio Review examined the performance of each group of properties with reference to 6 commonly used benchmarks. Properties previously released for sale, in order to support the capital programme, were not affected. It focused on non-operational property, not directly linked to service provision (for example, the Shambles shops), but also made reference to operational commercial properties (example, Waterworld at Monks Cross). A summary of the main statistics is reproduced below, categorised against the approved objectives for holding the non –operational properties;

	REASON/OBJECTIVE	MAIN STATISTICS
A	Generation of Revenue Income	£1.81m pa April 2005 – ie at the last 5 yearly valuation. It is rent net of direct management costs . This equates to a 3.% rise in Council Tax if lost. It gives a 6% return on the capital value.
B	To improve Asset Value and generate capital receipts	Asset value rose 36% 2000 ⇒ 2005 to £30m. Total returns, being capital growth plus rental income, average 80% 2000 – 2005. Inflation was 13% over this period. Benchmarks are 55% industrial and 78% retail for this period. Capital receipts of £1.2m were raised in 2006-07 for £27k pa rent loss. Receipts 2000-5 were £1.6m . £2m of sales are in hand. Commercial property has outperformed gilts and cash deposits – source Royal Institution of Chartered Surveyors Investment Property Report 2005
C	To provide opportunities for small businesses and support the local economy.	The council have a diverse portfolio with many small properties at rents under £15k pa. Fishergate and Parkside business centres are being replaced with a modern facility at Clifton Moor, and a refurbished property at Hospital Fields Road. This category is typically the one where most councils hold their property assets.
D	To provide property for operational needs and partners	- 11 Flats above shops are managed by/for the Housing department. - 29 Castlegate has become a new HQ for the Youth Service. - 5-6 Kings Court is partly used for Environmental Health offices - 5 Silver Street is the City Centre Office Although market rent is payable, and grants obtained separately, commercial properties also support the Citizens Advice Bureau, York Childcare, The Rathbone Training Centre and Housing Associations.
E	To influence land use in the city	For example, retain the character of Shambles, retain Hospital Fields Road (Fulford Industrial Estate) for employment use, to participate in any future development at Layerthorpe Industrial Estate, and to input into Coppergate 2.
F	When it is in the Public Interest to do so	As approved by Members. Eg King's Manor, Shambles

Operational commercial properties are held to;

a) Support service delivery – eg Waterworld

b) Generate revenue - eg Housing Estate Shops, and

c) Keep Property in beneficial use – eg the Museums at Micklegate and Monk Bars

Total Revenue to services from such commercial lettings, excluding education lettings to nurseries etc, is about £1m pa.

3. In respect of the proposed strategy for the non–operational portfolio, to work towards the future investment strategy, it is recommended that the properties be considered in four groups, as follows:-

   a) **Secondary shops**. The portfolio is heavily biased towards secondary shops. As values in some areas may have peeked for the foreseeable future, and in order to attract new investment to the properties and reduce the council's cost of management, some properties could be considered for disposal. The full list of properties under this category is summarised in List A of Exempt Annex 1.

   b) **Ground leases at fixed or low rents**. In the right circumstances, the council could share in the extra value which is realised by merging the freehold and leasehold interests, often linked with development, so these properties could be disposed of if and when the opportunity arises. The full list of these properties is given in List B of Exempt Annex 1.

   c) **Property linked with service use or possible future service potential use.** These properties, for example the Citizens Advice Bureau at Blossom Street and the Youth Service at Castlegate, would be retained, unless subject to further reports. These properties are contained in List C in Exempt Annex 1.

   d) **Prime investment properties and those needed to support local business.** These are properties showing good rental and capital value growth and / or which meet the criteria for supporting employment / small businesses, therefore to be retained. They are given in full in List D in Exempt Annex 1.

4 The intention is that the Commercial Property Portfolio in the future would therefore comprise those properties which most closely meet the objectives for management of the portfolio which were approved in October/November, as given again in paragraph 2 above.

The criteria fit in to the Corporate Objectives to improve the actual and perceived condition of the City Streets and also to improve future employment prospects by retaining small business and employment land.

5 It is suggested that receipts from sales in Lists A and B could be reinvested into more suitable property, ie

   a) Modern, low maintenance, energy efficient and with good income and the prospect of future growth.

   b) Mainly in use classes B (office/industrial), C (hotel) or D (Leisure) in order to balance the portfolio, which is now mainly retail.

   c) Property that will support service provision in the future , having regard to Service Plan objectives and Area and Service Asset Management Plans.

   d) Property with future development potential, having regard to the Local Development Framework.

Purely investment property need not be situated within the City of York. Prudential borrowing could add to the available funds when the repayments are adequately covered by the rent receivable or costs saved.

Option for a wider review

6 Following the Council resolution on the 21 February 2008, the review can be widened to include looking at alternative investment strategies. Properties are capital assets, and a wider review would give a comparison between various ways of maximising the returns. To scope this wider review, council officers, including from accountancy and planning , have met with external financial consultants, and further options that are available to the council could include:-

a) Sale of some properties and investing the receipts in cash, by shares or on financial markets – ie akin to Treasury management.

b) Seeking a private sector partner and setting up a joint venture company or companies to undertake development. Existing properties with development potential could be included plus cash from any sales. Such a strategy could also have regard to planning objectives.

c) Putting resources in to a property development syndicate or other investment vehicle.

d) Sale of some properties and utilising the receipts as an additional venture fund, inviting bids from all departments for resources that will give a payback in future savings or additional income.

e) Sale of some properties to invest the receipts in property or other assets more focused on the council's Corporate Objectives and policies.

A summary of the advice from external financial consultants is at Exempt Annex 3

7. It has been confirmed that it is not possible for the council to utilise the asset value to make pension fund contributions, as government consent would be needed and this is not available under current policy.

Consultation

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- Executive Member for Corporate Services and Advisory Panel 30 October 2007
- Executive 20 November 2007
- Corporate Management Team 28th May 2008
- Treasury Management Consultants. A summary of their comments is at Exempt Annex 3.

Options and Analysis

9 The options available for Members are recommended as follows:-

A) To carry on with the position approved in autumn 2007 and adopt the categorisation of the properties in Exempt Annex 1 giving delegation to sell and reinvest to the Director of Resources, subject to consultation , with the exception of the properties contained in the second part of list B and those in lists C and D. The consultants budget approved at Council on 21 February can be partly utilised on a property by property basis for sales advice and acquisitions, condition surveys and other expenses.

Advantages;

- this can be pursued straight away
- existing Framework Partners can be used

Disadvantages

- other possible options are not fully considered

B) To put the process in sub-paragraph A above on hold pending a wider review by suitably qualified firms of finance and property consultants, which will include alternative investment strategies, including those options listed in paragraph 6 above.. The names of three organisations that could be approached for quotations to give this wider range of advice are listed in Exempt Annex 2. The selection of a consultant would be based both on the price and quality of their service.

Advantages;

- Allows a wider review to take place
- Makes full and immediate use of funding now available

Disadvantages;

- The time taken to commission and consider the report
- Use of funding in reporting rather than implementation

10 **Corporate Strategy 2007 – 11**

The measures proposed in this report would assist the following to priorities in particular:-

a) To improve the actual and perceived condition and appearance of the city streets – by releasing some properties for investment by owners/occupiers and focusing resources on retained properties.

b) To improve future employment prospects – investment in more B1 in particular will secure property for new and existing businesses.

Implications

Financial Implications

11 Full Council agreed on 21st February 2008 to invest money from revenue reserves to conduct a review of the commercial property portfolio. The funding has been

earmarked to be spent in 2008/09 financial year. The financial implications of the outcome of the review will be dealt with when the review reports its findings.

Human Resources

12 There are no HR implications. It is, however, intended to reduce the amount of time spent on day to day Property Management matters, to allow more time to be spent on Service and Area Asset Management Plans and their implementation.

Equalities

13 There are no equalities implications.

Legal

14 Any agreed sales of property can be delayed by the absence of title deeds in many cases, and the time taken to register title as a result. Several transactions at once may result in Framework Partners being used, and the costs thereof will need to be a charge against the project.

Crime and Disorder

15 There are no crime and disorder implications.

IT

16 There are no IT implications. All transactions will feature in the council's new Technology Forge Property Management Database currently being developed.

Property

17 Property implications are included within the report.

Other

18 There are no other implications.

Risk Management

19 The council's approach to this will be a key part in forming the eventual strategy. As with our Treasury Management, external consultants have advised that the returns from the council's property portfolio are fair and reasonable given that the council does not directly invest in risk taking development. Higher returns can be obtained from investments, both financial and property related, which involve the greater risk but this does mean that there is the chance that one or more investments may fail. The council's financial management is required to be "prudential".

Recommendation

20 That the Advisory Panel advise the Executive Member that the report be noted and Option B in paragraph 8 be approved, and that any surplus from the revenue allocation for the review be utilised towards the implementation.

Reason

21 So that the council's Commercial Property Portfolio may be modernised, made more efficient and may be aligned more closely to Corporate Objectives and service property needs for the future in response to the budget approved by Council.

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Report Approved ✓ **Date** 8th May 2008

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Resources

Wards Affected: **All** ✓

For further information please contact the author of the report

Background Papers

The report to Executive on 20 November 2007.

Annexes

Annex 1 – Property Schedules
Annex 2 – Recommended Property & Financial Consultants
Annex 3 – Summary of Initial Advice given by Consultants regarding the Commercial Property Portfolio