
Executive

13 July 2017

Report of the Director of Economy and Place

Portfolio of the Executive Member for Finance and Performance

Establishing an Investment Budget for a Strategic Commercial Property Acquisition

1. An opportunity has arisen for the council to acquire the freehold interest in a portfolio of properties in the city centre that will ensure the ongoing maintenance of the buildings, support the economic vibrancy of the city centre and generate significant additional income to contribute to the increased budget income target set for the council's commercial portfolio.

Recommendations

2. Executive is asked :
 - (i) To recommend to full council
 - the establishment of a capital budget of £15m, to be financed initially from borrowing, to fund the acquisition of freehold interest in a portfolio of city centre commercial property assets.
 - to agree that any future capital receipts not currently assumed in the Capital strategy, be allocated to fund the purchase, thereby reducing in time the associated borrowing related to the investment. This will be updated in capital monitor reports in the future.
 - (ii) To bring back to Executive a due diligence report prior to completion of the acquisition

Reason: - To ensure the ongoing economic vibrancy of the city centre and increase the income from the council's commercial property portfolio in order to achieve budget targets

Background

3. The council has for many years operated a significant commercial portfolio often purchased in order to conserve either the buildings or promote the regeneration and economic vibrancy of the area. The assets also generate a revenue income stream to support the council's revenue budget. In the last two years, additional income targets have been agreed as part of the annual budget. Significant work has already been undertaken to deliver additional income including the disposal of underperforming assets and the acquisition of property in Hospital Fields Road.
4. The budget report for 2017/18 set out an approach to a 4 year budget and identified the need to consider further property investment opportunities in order to continue this good progress over future years. Given that interest rates are low, property acquisitions perform well when compared to other forms of investment and are capable of delivering higher yields.
5. The council has always focussed its commercial estate in York in order to promote and support economic vibrancy and ensure the preservation of historic buildings. These acquisitions also serve a broader role in meeting social economic and environmental objectives such as regeneration and ensuring the sustainability and vibrancy of the city centre.
6. An opportunity has arisen to make a strategic acquisition of a mixed commercial portfolio in York city centre. The portfolio is on the open market and hence the details are commercially sensitive. Details of the properties are attached as confidential Annex 1, together with a pre-acquisition report at confidential Annex 2, prepared by national and York based commercial agents, which provides a commercial view of the opportunity.
7. The marketing exercise is live now and will close later in July. In order to make an offer for these properties the council will need to agree an overall capital budget for the acquisition. If that offer is then accepted by the vendor then a more detailed due diligence report will be brought back to Executive before the acquisition is completed.
8. The item has been added to the forward plan as an urgent item because a decision is needed by Executive and full Council in July 2017. This does not allow for the item to appear on the forward plan for the usual 28 days. The next full Council meeting is in October which would be too late.

Funding

9. Given the commercial sensitivity of an open marketing exercise, it is proposed that an overall capital budget of £15m is set aside to fund the

acquisition. The detailed due diligence report will set out the actual sale value if the council is successful in securing the assets.

10. The funding will be provided by borrowing from the Public Works Loan Board (PWLB) and will be repaid from rental income.
11. The outline business case in confidential Annex 3 sets out scenarios for a range of eventual purchase prices showing the different returns. Prudent assumptions have been made to make provision for potential voids, the staff costs of operating an enlarged commercial estate and a prediction of the potential increase in income over the next 5 years to indicate how the revenue stream will increase whilst repayment of the capital will stay steady and eventually fall away. The business case is based upon borrowing over 50 years and minimum revenue provision being based on the asset's perceived life.
12. It is proposed that ultimately the financing for the purchase will be paid for from future capital receipts. There are a number of potential significant receipts in coming years, and as these come through it is intended that these will be utilised to reduce the borrowing requirement on the assets within this report. Ultimately that should result in there being no actual debt associated with the investment, incurring no associated borrowing costs. This will be set out in further detail in the next report.
13. In addition to rent each lease has the ability for a service charge to be levied which will ensure the ongoing quality of the assets and pay for the repairs and maintenance liabilities of the property. Given current low interest rates, even with making full provision for repayment of the costs of purchase the rental income will provide an additional source of annual revenue, net of borrowing costs. In addition the value of the asset is likely to increase over time.
14. The investment therefore represents a good opportunity to increase the commercial portfolio rental stream and support city centre economic prosperity

The Council Plan

15. The acquisition will support the following priorities;
 - I. The creation of a Prosperous City for All,
 - II. Be a Council that listens to residents particularly by ensuring that :
 - III. Everyone who lives in the city can enjoy its unique heritage and range of activities.
 - IV. Visitors, businesses and residents are impressed with the quality of our city.

- V. Local businesses can thrive.
- VI. We are entrepreneurial, by making the most of commercial activities.

Implications

Financial – These are covered in the report and in confidential annex 3.

Human Resources (HR) – If the acquisition goes ahead additional resource will be needed to manage the expanded commercial portfolio. This will be funded from additional income.

Equalities – n/a

Legal – Under part 1 chapter 1 of the Local Government Act 2003, a local authority may borrow for any purpose relevant to its functions or for “the prudent management of its financial affairs. The detailed due diligence exercise will consider the detailed legal implications of the acquisition.

Information Technology (IT) - There are no IT implications.

Crime and Disorder – none

Property – All property implications are covered in the report. A more detailed report will set out the results of the due diligence exercise.

Risk Management

- 16. As with all property acquisitions there is a risk that the value of the property may decrease over time. Full provision is made in the business case to pay off the capital cost over the life of the asset.
- 17. There is also a risk that there may be a level of tenancy voids. The business case makes provision for that risk.

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Wards Affected: Guildhall

For further information please contact the author of the report

Background Papers:

Annexes

Confidential Annex 1a –Property Details
Confidential Annex 1b – Property Details
Confidential Annex 2 - Buyers Pre Acquisition Report
Confidential Annex 3 – Outline Business Case

List of Abbreviations

None