

Item No. 20.	Classification: Open	Date: 21 March 2017	Meeting Name: Cabinet
Report title:		Commercial Property Portfolio: Addition of Income Generating Assets	
Ward(s) or groups affected:		All	
Cabinet Member:		Councillor Fiona Colley, Finance, Modernisation and Performance	

FOREWORD – COUNCILLOR FIONA COLLEY, CABINET MEMBER FOR FINANCE, MODERNISATION AND PERFORMANCE

This year the total income receivable from the Council's commercial property portfolio is £11.65m. This is a vital source of income to support council services. However, this income has reduced by £2m over recent years as a number of sites have been either sold to help finance the capital programme or redeveloped to deliver new council homes.

An opportunity has arisen to add to our portfolio by purchasing three commercial properties in the borough. Having carefully assessed the capital value, income yield, financing costs and risks I am recommending the Cabinet approves the purchase of these buildings.

In this period of decreasing government funding for council services, this capital investment will generate much needed additional income into the general fund revenue budget and help support the delivery of our highly valued public services.

RECOMMENDATIONS

1. That Cabinet:

- 1) Note the circumstances leading to the proposed acquisition of the freehold interests in three commercial properties and actions and investment due diligence undertaken by officers and their advisors:
- 2) Approve the acquisition of the freehold interests in the three properties, and all related costs.
- 3) That the cabinet delegate to the Chief Executive, advised by and in consultation with the Strategic Director of Finance and Governance and Head of Property, authority to:
 - a. Complete the purchase of the freehold interests in the assets;
 - b. Agree detailed transactional terms pursuant to the Heads of Terms;
 - c. Agree the financing structure to be adopted to fund the acquisition of the assets.

BACKGROUND INFORMATION

Income from the commercial portfolio

2. Rent from commercial property assets is a crucial funding source for council services. The nature, management and performance of the council's portfolio has been extensively reviewed over recent months; culminating in Cabinet giving its approval for a new Asset Management Plan for commercial property in December 2016.
3. Over the last four years, despite continuing improvement in the underlying rents obtainable from individual assets revenues have fallen by approximately £2 million, or 15%.
4. The cause lies in the release of assets in to other initiatives; to generate capital receipts, or otherwise into regeneration, Southwark Regeneration in Partnership Programme and Direct Delivery schemes to deliver a range of corporate priorities. Other significant reductions are expected to take place in the short to medium term.
5. Although a limited number of new income generating assets may be created through regeneration, appreciating that it is not the primary objective of these programmes to provide new commercial properties, officers have looked for other opportunities to replenish the diminishing asset base and incomes derived from it.

KEY ISSUES FOR CONSIDERATION

6. An opportunity has been identified to acquire an established portfolio consisting of three freehold, multi-let office/studio buildings, situated in the London Bridge area.

Sale process

7. The portfolio has been actively marketed through a competitive process by the seller's agents.
8. The council's offer for portfolio has been accepted in principle by the vendor. This is subject to formal approvals, and subject to exchange of legally binding contracts on or before the 28 March 2017. The vendor has issued completed Heads of Terms and the council and seller have entered in to a period of exclusivity to enable completion of the transaction within the timescale specified, if cabinet is agreeable.
9. Officers have commissioned full due diligence work in the acquisition to commence, including legal and building survey reports.

Financial due diligence and the council's bid

10. In advance of bidding, the investment opportunity and viable bid level was reviewed by independent property advisors who specialise in the acquisition and disposal of Investment property and are advising the council in this transaction.

11. The council's bid is supported by investment valuations undertaken by the council's advisors in accordance with the requirements of the Royal Institution of Chartered Surveyors Valuation Professional Standards ("the Red Book").
12. The purchase will provide a commercial return to the council as part of its property portfolio. The rationale for the council to invest can be summarised as follows:
 - An established income stream;
 - A favourable yield, which will be significantly above financing costs and interest rates for money on deposit;
 - Asset management opportunities to increase rents in the short to medium term;
 - Poorer quality assets released into other initiatives mentioned previously will be replaced by significantly better ones in investment terms.
13. As with any investment there is risk. However the central London property market is perceived to be relatively resilient in times of uncertainty. In acquiring this portfolio there is future investment and strategic potential in an attractive and regenerating location, close to London Bridge Station, More London, Bermondsey Village and Tower Bridge / Butlers Wharf.

Community impact statement

14. In formulating the recommendations of this report the potential impact on the Community has been taken into account, including people identified as having protected characteristics. No specific equality implications have been identified in relation to this report.

Policy implications

15. The holding of investment property to generate income, which in turn is used to fund council services pursuant to agreed policies, is consistent with the new Asset Management Plan for commercial property agreed by Cabinet in December 2016.

Financial Implications

16. The financial implications for the council from this prospective purchase are contained in the closed version of this report.

Consultation

17. In view of confidentiality requirements and commercial sensitivity in relation to this as yet uncompleted transaction external, consultation has not been undertaken. Internal consultation has taken place with all relevant departments, including the provision of advice from Director of Law and Democracy and Strategic Director of Finance and Governance.

SUPPLEMENTARY ADVICE FROM OTHER OFFICERS

Director of Law and Democracy

18. The Council is authorised in accordance with section 120(1), Local Government Act 1972 to acquire any land by agreement for the purposes of (a) any of its statutory functions, or (b) for the benefit, improvement or development of its area. Further, section 120(2) allows the Council to acquire land even though it may not immediately be required for a particular purpose.
19. External legal advisers have been instructed to undertake a legal due diligence report on behalf of the Council and this will be appended to the report. This will comment and advise on contract and title issues, the costs which will be incurred in the purchase and on the transaction generally.

Strategic Director of Finance and Governance

20. The financial implications are contained in the closed version of this report and demonstrate a financial benefit to the council both in the short and longer term from this purchase, regardless of the method of financing the acquisition.
21. This acquisition will allow the council to efficiently utilise existing resources and available external borrowing options to generate a secure source of ongoing funding, without exposing the council to undue risk.

BACKGROUND DOCUMENTS

Background Papers	Held At	Contact
None		-

APPENDICES

No.	Title
None	

AUDIT TRAIL

Cabinet Member	Councillor Fiona Colley, Finance, Modernisation and Performance		
Lead Officer	Eleanor Kelly, Chief Executive		
Report Author	Matthew Jackson, Head of Property		
Version	Final		
Dated	10 March 2017		
Key Decision?	Yes		
CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / CABINET MEMBER			
Officer Title	Comments Sought	Comments Included	
Director of Law and Democracy	Yes	Yes	
Strategic Director of Finance and Governance	Yes	Yes	
Cabinet Member	Yes	Yes	
Date final report sent to Constitutional Team/ Team		10 March 2017	