

**Report of: Director of City Development and Deputy Chief Executive**

**Report to: Executive Board**

**Date: 14 December 2016**

**Subject: Design & Cost Report for Acquisition of a Property for the Council's Investment Portfolio**

Are specific electoral wards affected? If relevant, name(s) of ward(s):	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Are there implications for equality and diversity and cohesion and integration?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Is the decision eligible for call-In?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Does the report contain confidential or exempt information? If relevant, access to information procedure rule number: 10.4(3) Appendix number: 1	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No

### Summary of main issues

1. The Council has an opportunity to strengthen and improve the value and performance of its investment portfolio which is brought about from its leading role of stimulating development during the recession.
2. The Executive Board at its meeting on 22 June 2016 approved the purchase of 2 investment assets on the basis that they both stimulated economic investment in the City and also generated a revenue surplus after borrowing costs for the Council. These 2 properties comprised 3 Sovereign Square and Unit 1 Logic Leeds in the Leeds Enterprise Zone.
3. One of the main aims of the Council is to bring about economic regeneration in Leeds. The Council has already been involved in bringing forward the development of the above two buildings at a time when the market was stalling and their acquisition will further the Council's involvement and financial benefits. With the Council's ambition to become the best city in the UK, with an economy that is both prosperous and sustainable, these acquisitions offer the opportunity to further boost the performance of the Council's property investment portfolio with substantial rental income. The acquisitions align with the approved Asset Management Plan which includes enhancing the value of the Council's Investment Portfolio in order to produce further revenue to support the Council's budget position. The proposal also contributes to regenerating places, supporting businesses to grow and invest, creating quality places and spaces and backing innovators and entrepreneurs.

These are unique opportunities which have been offered to the Council to acquire strategic investments which will enhance the quality and performance of the Council's Investment Portfolio.

4. A separate report on Executive Board outlines the Initial Budget Strategy where part of the revenue to support this strategy would be created by the acquisition of further investment assets. The targets in this strategy are to generate additional revenue over borrowings of £2m pa by 2017/18, a further £0.5m pa by 2018/19 and an additional £1m pa by 2019/20. The opportunity exists for the Council to continue its investment in commercial property opportunities and since the acquisition of the above mentioned properties, a number of other investment propositions have been brought forward for the Council to consider. The majority of opportunities would enable the Council to acquire buildings that are let to tenants from which the Council will immediately receive a rental income. The level of rents that are being obtained are sufficient to cover the cost of borrowing to acquire the properties and provide a surplus to support the Council's budgets, to continue to improve services at a time when funding streams to the Council are declining.
5. The proposal also contributes to regenerating places, supporting businesses to grow and invest, creating quality places and spaces and backing innovators and entrepreneurs.
6. As such the Council is seeking to build an investment portfolio that supports the aims of the Best Council Plan to enhance and strengthen the economic growth and access to economic opportunities in Leeds. These opportunities can be unique and enable the Council to acquire strategic investments which will enhance the quality and performance of the Council's Investment Portfolio. Often these property transactions occur off the market and need to be completed in relatively short periods of time. As such the Council needs to ensure that it can respond quickly to these investment opportunities as they arise to meet the revenue targets that have been set.
7. To enable the Council to respond to the opportunities in a timely the Executive Board at its meeting on 22 June 2016 approved that the Director of City Development continues to investigate the acquisition of additional investment opportunities which will further enhance the strength and performance of the Council's investment portfolio in supporting the Council's budget and stimulating economic regeneration and confidence as part of a strategic investment fund. The confidential appendix sets out details of an investment property that the Council can acquire that would generate a net surplus revenue after borrowing costs.

## **Recommendations**

8. Executive Board is recommended to:
  - i) Approve the acquisition of the property on the terms outlined in the confidential appendix;
  - ii) Approve the injection into the Capital Programme, and give authority to spend, the sums detailed in the confidential appendix.

- iii) Authorise the Director of City Development under the scheme of delegation to approve any changes to the recommended terms which may be necessary prior to completion, and to authorise the Director of City Development to complete the acquisition.
- iv) Agree that this report is made exempt to Call-In for the reasons set out in paragraph 4.5.3.

## **1 Purpose of this report**

- 1.1 The purpose of this report is seek approval to the purchase of an investment property that has been offered to the Council generating additional income to support the revenue requirements of the Council as set out in the Initial Budget Strategy. The acquisition will align with the Council's ambition for Leeds to have a strong economy and be a compassionate city with the aim to sustain and accelerate the economic progress the city is making whilst ensuring all people and communities in Leeds contribute and benefit from economic success. The value and strength of the Council's property investment portfolio will be enhanced and make the Council's financial position stronger and more resilient.

## **2 Background information**

- 2.1 The Executive Board at its meeting on 22 June 2016 approved the acquisition of 3 Sovereign Square and 1 Logic Leeds. The acquisition of both these properties have added to the Council's investment portfolio by creating a surplus of income over the borrowing costs and therefore supporting the Council's revenue budgets. The Council has intervened proactively to kick-start development and regeneration projects, support businesses to grow and invest, and to help people to work.
- 2.2 At the meeting on 22 June 2016 the Executive Board further authorised the Director of City Development to investigate the acquisition of additional investment opportunities which will further enhance the strength and performance of the Council's investment portfolio in supporting the Council's budget and stimulating economic regeneration and confidence as part of a strategic investment fund.
- 2.3 Since the Executive Board meeting the Council has been presented with a number of investment opportunities. These have been assessed in terms of the regeneration benefits through investment that the Council might be making in that part of the city to opportunities where the Council will secure a strong revenue return over and above its borrowing costs. The opportunity presented in the confidential appendix would provide the Council with a strong rental return and create a net revenue surplus contributing to the Council's budgets.
- 2.4 The Council has brought forward development opportunities in Leeds such as Sovereign Street in the city centre. The Council's promotion of development at Sovereign Street links to the wider development at South Bank, one of Europe's largest regeneration projects. Arising from this development the Council has recently completed the acquisition of the newly constructed 3 Sovereign Square and started marketing of the final plot 2 at Sovereign Square.
- 2.5 The Council also promoted development in the Leeds Enterprise Zone by awarding grants to land owners for site reclamation, and underwriting development risk by agreeing to purchase vacant warehousing if it was not let following construction. The acquisition of unit 1 at Logic Leeds has enhanced further investment in this area and is providing further investment opportunities for the Council to consider.

### **3 Main issues**

- 3.1 In order to continue to acquire investment opportunities an Investment Strategy has been devised that seeks to acquire additional investment opportunities that either provide a strong rental income and/or add to the investment and regeneration of parts of the City. A major element of the strategy is the identification of the suitable property investment properties.
- 3.2 The aim of the investment strategy concentrates on the identification of opportunities with a preference for new build / pre build developments or recently constructed investments or those that are let or pre let to strong financial covenants with secure income flow on full repairing and insuring leases with lengthy unexpired terms.
- 3.3 This principle is one of the ten key proposed actions in the Asset Management Plan; to support the Council's revenues. The investment property detailed in the confidential appendix will sit well alongside other major key investments such as 3 Sovereign Square, Unit 1 Logic Leeds, the Arena, the redeveloped Merrion House, and the Harper Street (Markets) multi-storey car park.
- 3.4 The acquisition will also enhance the quality of the Council's Investment Portfolio and the Council will continue to review its existing property portfolio to determine assets that it can sell.

### **4 Corporate considerations**

#### **4.1 Consultation and engagement**

- 4.1.1 The Executive Member for Regeneration, Transport and Planning and Executive Member for Resources and Strategy have been briefed and are supportive of the acquisition.

#### **4.2 Equality and diversity / cohesion and integration**

- 4.2.1 Equality, Diversity, Cohesion and Integration screening has taken place indicating there are no implications and, therefore, further assessment is not required. The EDCI screening document is attached at Appendix 2.

#### **4.3 Council Policies and Best Council Plan**

- 4.3.1 The ambition for Leeds to have a strong economy and be a compassionate city is set out in the Best Council Plan. The proposals in this report support this ambition and the Council's Best Council Plan 2016/17 priorities around supporting economic growth and access to economic opportunities and the associated breakthrough projects on 'more job, better jobs,' 'strong communities benefiting from a strong city' and 'housing growth and high standards in all sectors'.
- 4.3.2 The proposed acquisition supports the Best Council Plan ambition for the authority to continue to be an efficient and enterprising organisation by seeking to optimise the council's Investment Portfolio and by generating income to support the council's revenue budget. Not only would the acquisition provide a net surplus income at a

time when there is unprecedented pressure on the Council's revenue budget, but would also put strategically located properties in Council ownership.

- 4.3.3 The approved Asset Management Plan 2013 – 17 has, as one of its ten areas of focus, 'making the Council's portfolio work better' undertaking to improve the scale and quality of the Investment Portfolio to assist and support the Council's revenue budget, including strategic acquisition where there is a strong financial case to do so.

#### **4.4 Resources and value for money**

- 4.4.1 The proposed acquisition would provide the Council with a net surplus annual income as detailed in the confidential appendix after allowing for borrowing costs.

#### **4.4.2 Capital funding and cash flow**

- 4.4.3 See attached confidential appendix.

#### **4.5 Legal Implications, access to information and call in**

- 4.5.1 Section 120(1) of the Local Government Act 1972 authorises local authorities to acquire any land for their functions, and for the 'benefit, improvement or development of their area.' Leading Counsel has advised that the Council can safely rely on this power given that the acquisition of the Properties will be for the "benefit" of the Council's area by improving the Council's financial position generally, and for the "improvement" and "development" of the Council's area by facilitating and enabling regeneration projects, in that the surplus generated will contribute to the funding of the Economic and Regeneration Service and its activities, to support economic growth and regeneration in the area.
- 4.5.2 In addition, Leading Counsel has advised that in these circumstances, the power to borrow for any purpose relevant to its statutory functions under Section 1(a) of the Local Government Act 2003, is available to the Council, given that "functions" embraces all powers and duties of the Council, including the power to acquire property mentioned above.
- 4.5.3 The terms provisionally agreed for the property in the attached confidential appendix have been concluded on the basis that contracts are exchanged before the end of December 2016. This particular property was put to the Council very recently and discussions regarding its purchase were only concluded after the date when the List of Forthcoming Key Decisions was issued. Should the Council seek to delay the consideration of the acquisition to next year it is likely that the seller will offer the property to other parties. Also should the sale not complete within the above timescale the Council would be at risk of the sale and the purchase price being re-opened for negotiation in open competition with other parties. For this reason it is proposed that this purchase is exempt from Call-in.
- 4.5.4 The above has been discussed with the chair of Scrutiny Board (City Development) to explain the reasons why the matter is considered to be urgent and cannot reasonably be deferred. The chair of Scrutiny Board (City Development) has

agreed that the exempt part of the report can be considered at the Executive Board for the above reasons as set out in paragraph 4.5.3.

4.5.5 Due to the timescales involved it was not possible to include the decision in the List of Forthcoming Key Decisions for a period of 28 days prior to making the decision. By the time terms had been agreed the deadline to publish the acquisition had passed and with the next Executive Board meeting not being until February 2017 there is a risk that this transaction may be withdrawn from the Council .

4.5.6 The information contained in Appendices 1 is exempt under Access to Information Rule 10.4(3) as it contains information relating to the financial or business affairs of a particular organisation and of the Council. The property has been offered to the Council to acquire on a one to one basis off the market rather than being put to the open market. It is considered that the public interest in maintaining the content of the appendix as exempt outweighs the public interest in disclosing the information due to the impact that disclosing the information would have on the Council and third parties.

## **4.6 Risk management**

4.6.1 The Council will borrow to fund the acquisition. Currently, interest rates remain at historically low levels and the rental income will more than adequately cover the borrowing costs, and provide a substantial surplus to assist other revenue budgets. Interest rates would have to increase substantially before the rental income was fully exhausted covering the borrowing costs. The Council has the opportunity to fix long term borrowing at significantly low interest rates.

4.6.2 There may be times in the future when the buildings, or parts of them, become vacant. Should this be the case then the Council is likely to have been given lengthy notice of a proposed vacation which will provide time in which a new tenant could be sought. The Council's property investment portfolio contains many letting properties and it is quite normal to experience void periods and to seek new tenants.

4.6.3 As part of the acquisition of an investment property the Council is taking external advice from firms of Chartered Surveyors who act on behalf of the Council to negotiate the terms of the acquisition of the property. This external expertise provides the Council with a level of due diligence that ensures that the acquisition represents value for money ensuring that the Council will obtain a good rate of return. If required a building condition survey is undertaken prior to the purchase of the property. Separately prior to the acquisition of an investment property, a financial assessment is undertaken based on the rental levels that could be achieved set against the Council medium/long term borrowing costs and due diligence is also undertaken based on the covenant strength of the individual tenants occupying the building. The acquisition of these properties will be proactively managed by the Council and where appropriate the Council will secure external property advice.

## **5 Conclusions**

- 5.1 In conclusion, the Council has an opportunity to strengthen and improve the value and performance of its investment portfolio. The Council is being offered a number of investment opportunities and in order to meet the additional revenue targets needs to acquire further investments. The terms for the acquisition of this particular property are recommended for approval and detailed in the confidential appendix.

## **6 Recommendations**

- 6.1 Executive Board is recommended to:

- i) Approve the acquisition of the property on the terms outlined in the confidential appendix.
- ii) Approve the injection into the Capital Programme, and give authority to spend, the sums detailed in the confidential appendix.
- iii) Authorise the Director of City Development under the scheme of delegation to approve any changes to the recommended terms which may be necessary prior to completion, and to authorise the Director of City Development to complete the acquisition.
- iv) Agree that this report is made exempt to Call-In for the reasons set out in paragraph 4.5.3.

## **7 Background documents<sup>1</sup>**

- 7.1 There are none.

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<sup>1</sup> The background documents listed in this section are available to download from the Council's website, unless they contain confidential or exempt information. The list of background documents does not include published works.