

Committee: Investment Board

Date:

Title: Commercial Strategy Update

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Summary

1. This report attaches the latest version of the Commercial Strategy for consideration by the Board

Recommendations

2. Members consider the revised document and suggest further amendments ahead of the Council meeting on the 16 December.

Financial Implications

3. None.

Background Papers

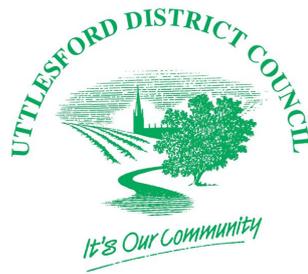
4. The following papers were referred to by the author in the preparation of this report and are available for inspection from the author of the report.

None

Situation

5. Attached as Appendix One is the latest version of the Commercial Strategy. The specific areas that have been updated are
 - a. Paragraphs 3 – 5, reflecting the purpose of the investments
 - b. Paragraphs 16 – 20, setting out the legal framework in which local authority investments are made
 - c. Paragraph 32, clarification that an investment risk register will be maintained and monitored by the Investment Board
 - d. Paragraph 39(b) – reworded for clarity

Appendix One



Uttlesford District Council

Commercial Strategy 2019 to 2023



Prepared by:
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Introduction

1. The Council recognises that as a consequence of reducing government funding there is an increased requirement to generate additional income to underpin the core services provided by the Council to its residents. Traditional ways of generating additional income such as through Council Tax and fees and charges will not be able to absorb the reduction in government funding. By way of illustration, a 1% rise in Council Tax is equivalent to about £55,000 in additional income.
2. This document replaces the Commercial Strategy 2019 to 2023 as approved by Full Council on 8 Octo

Purpose of the Investments

3. To provide a long term income for the council to support the provision of Council services. This income requirement has arisen as a result of reductions in the Council's finance from central government. Government also restricts the ability of councils to raise income from council tax increases.
4. The Council seeks to operate in the most cost effective ways and will look for improvements in its operations which will reduce costs or avoid increased costs. However the scale of reduction in external finance is such that other income sources must be found. Reductions in council services are considered a last resort.
5. The income target for the Board will be guided by the Medium Term Financial Strategy (MTFS). The MTFS forecasts the income and expenditure over a four year period and includes all known factors. It shows the predicted annual net surpluses or deficits. The investment income is sought to cover the forecast significant deficits in each of the years of the MTFS, so as to ensure that existing services can continue to be provided.

Current Portfolio

6. In May 2017 the Council, through its wholly owned subsidiary Aspire (CRP) Ltd, acquired a 50% share in Chesterford Research Park and formed a joint venture with Aviva Investors. As part of the Cambridge Life Science cluster the Park is world renowned, having been in existence for 19 years, with available space to significantly increase the commercial floor space, plus expand the Park into other areas of research to diversify and reduce the risk.

7. The Council gave a loan to Aspire (CRP) Ltd for the purchase of 50% of Chesterford Research Park (£47.25m). The loan was funded by
- a. Phoenix Life – borrowing of £37m for 40 years on a repayment basis @ 2.86% fixed. The first £10m drawdown was 5 July 2017 with the remainder as follows

5 July 2020 - £12m

5 July 2021 - £15m

Whilst this loan is being drawn down the balance will be funded by a mix of local authority and internal borrowing – The amount of each varies during the year dependant on the level of UDC balances available. Average interest rate, interest only, is 0.7%

- b. Use of reserves and balances (£10.25m) funds the balance.
8. For 2019/20 the income from Chesterford Research Park is expected to be £2,130,000 with the cost of borrowing being £400,000. There is also repayment of staff time.

Loans to wholly owned subsidiaries

9. The Council recognises that, to further support the budget ongoing and to ensure the continued delivery of services at the level currently provided, further investment in the expansion of Chesterford Research Park will be necessary. The first set of additional loans relate to the refurbishment of the Newnham Building. To date, the following loans to Aspire (CRP) Ltd have been made

Date	Amount	Term	Rate	Basis	Annual Repayment	Building	Repaid
03/05/2017	£47,250,000	50 years	4%	Interest Only	£1,890,000.00		
27/06/2017	£60,000	10 months	4%	Interest and principal	£61,827.95		✓
26/03/2018	£223,000	49 years 1 months	4%	Interest only	£8,920.00	Newnham	
02/01/2019	£2,518,000	48 years 4 months	4%	Interest only	£100,720.00	Newnham	
20/08/2019	£3,000,000	20 years	4.5%	Interest and principal	£230,630.00	Newnham	

10. In addition there is approval for a further loan of £1.25m for the fit-out of the Newnham Building on an interest and principal basis over 20 years at an interest rate of 4.5%. This will be drawn down during the latter part of 2019/20 as the Newnham Building refit progresses.

The future

11. The Council is committed to investing in the Park. The Council is keen to see existing tenants expand and grow on the Park and for the Park to attract new tenants from a diverse range of research activities. The Park is within the district boundary and investing helps to sustain existing employment, introduce new employment opportunities and generate additional Business Rates. As part of the 2019/20 Investment Strategy, approved by Full Council in February 2019, an in principle agreement to invest up to £20million at the Park over the next three years was approved.

12. Full Council in February 2019 also agreed an in principle sum of £80million for investments outside of CRP. This sum will, in the main, be invested out of area to offset risks of investing in a small geographical area. To minimise risk to the investment the Council will, in the main, concentrate on areas with above average;

- Population growth projections
- Employment growth projections
- Gross Domestic Product (GDP) growth projections

13. The Investment Portfolio may include a mix of

- Multi-let urban industrial
- Offices in dynamic cities
- Single-let long lease
- Convenience retail
- Market rent housing

14. The portfolio will also have a mix of lease lengths again to provide a balance.

15. Evaluation of potential opportunities will be made using a RAG based approach on criteria agreed by the Investment Board.

Borrowing, the Prudential Code and Statutory Guidance on Local Government Investments

16. The Council can rely on a variety of statutory powers to borrow and invest. Where the primary purpose of borrowing and investment is to secure a financial return, the Council has powers under sections 1 and 12, Local Government Act 2003. Section 1 provides that:

A local authority may borrow money—

- (a) for any purpose relevant to its functions under any enactment, or*
- (b) for the purposes of the prudent management of its financial affairs.*

Section 12 states:

A local authority may invest—

- (a) for any purpose relevant to its functions under any enactment, or*
- (b) for the purposes of the prudent management of its financial affairs.*

17. Where the Council proposes to rely on the borrowing powers in Local Government Act 2003 section 15 of the Act makes it a requirement to “*have regard –*

- (a) to such guidance as the Secretary of State may issue, and*
- (b) to such other guidance as the Secretary of State may by regulations specify for the purposes of this provision.”*

The current guidance to which the Council must have regard is:

- Statutory Guidance on Local Government Investments (3rd Edition) issued by the Secretary of State; and
- The Prudential Code issued by CIPFA.

18. The Statutory Guidance contains two paragraphs on what is termed “*borrowing in advance of need. The guidance states:*

46. Authorities must not borrow more than or in advance of their needs purely in order to profit from the investment of the extra sums borrowed.

47. Where a local authority chooses to disregard the Prudential Code and this Guidance and borrows or has borrowed purely to profit from the investment of the extra sums borrowed the Strategy should explain:

- *Why the local authority has decided not to have regard to this Guidance or to the Prudential Code in this instance; and*

- *The local authority's policies in investing the money borrowed, including management of the risks, for example, of not achieving the desired profit or borrowing costs increasing.*

19. The Council will adopt a “case by case” approach in considering whether to depart from the Statutory Guidance and the Prudential Code where the primary purpose of borrowing is to “profit from the investment of the extra sums borrowed”. In reaching a decision, the Council will balance the need to generate additional income to underpin core services to Uttlesford residents against the risks involved in taking on the borrowing and against the risks involved in the investment to be funded by borrowing. It will ensure that investments funded by borrowing in these circumstances are proportionate to the need to make good shortfalls caused by the reduction in Government funding. Given the Council's acute funding shortfall and the likely consequences for Uttlesford residents of not being able to maintain core services without additional funding, the Council is likely to depart from the Statutory Guidance and from the Prudential Code where sound investment opportunities are identified.

20. The Council will set out for each investment the risks associated with the investment, be they specific or industry/sector. These will be monitored on a regular basis by the Investment Board, and where necessary recommendations will be made to the Cabinet. The Council maintains a Medium Term Financial Strategy Reserve which is retained for use in the event of a significant drop in revenue income from an investment.

Key Performance Indicators (KPIs)

21. A suite of KPIs will be developed by the Investment Board for reporting by the Aspire companies on a quarterly basis. These KPIs will be used, as part of suite of information, to inform future investments and disposals and therefore the make-up of the portfolio

Investment Protocol

22. An Investment Protocol will be developed alongside this strategy which sets out the criteria in detail.

Security, Liquidity and Yield

23. As the Council only has a small amount of money of its own to invest, any further expansion of the commercial strategy will necessarily be funded from a mix of external borrowing, from financial institutions, Public Works Loan Board

(PWLB) and other local authorities. The Council will not invest in high yield, high risk opportunities. This will be reflected in yield expectations which are currently 3 – 7%.

24. Investments at Chesterford Research Park will be made by way of loans to Aspire (CRP) Ltd the Council's wholly owned subsidiary. All commercial investments outside of CRP will be undertaken by the Council. Property purchase for letting at market rents will be undertaken through a new wholly owned subsidiary company Aspire (UDC) Ltd.
25. By investing mainly, but not exclusively, in areas of above average population growth, employment growth and GDP growth the risk to the Council investment will be reduced.
26. Financing of acquisitions will be decided on a case by case basis. In almost all cases a mix of repayment and interest only loans will be undertaken, with the split being agreed by Cabinet.
27. The option to liquidate funds is either by selling the investment (or part thereof) or by refinancing the debt.

Risks

28. Each investment must be considered independently and only those viewed as having a positive expected yield and an acceptable risk profile will be taken forward for consideration by the Council.
29. The Council takes advice from its professional advisers at all times. For example, with the purchase of the 50% share at Chesterford Research Park the Council engaged
 - Arlingclose as its financial advisers who project managed the funding tender
 - Cushman and Wakefield who undertook all of the purchase negotiations and due diligence
 - Hogan Lovells for Legal due diligence
30. For Aspire (CRP) Ltd the Council has appointed two non-executive directors to serve on the Board and bring independent challenge and support. The new delivery company, Aspire (UDC) Ltd, will also have two non-executive directors on the Board.
31. The Aspire companies will use a range of specialists which will vary between investments. This will ensure the continued professionalism and sector knowledge.

32. A risk register will be maintained for each investment and these will be monitored by the Investment Board on a regular basis.

Proportionality

33. The aim of the Commercial Strategy is to generate income to underpin the Council's core budget, to invest in other income generating opportunities and also good causes for the district.

34. The Council's main investment at Chesterford Research Park comprises eleven core buildings and circa twenty tenants. For the income to be below the interest repayment amount three of the five largest tenants would be required to default on their tenancy agreement at the same time. Even with this relatively low risk it is important to attract different types of research business to the Park.

Capacity, Skills and Culture

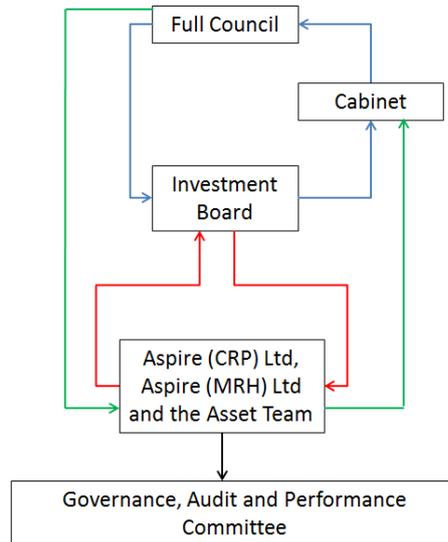
Investment Board (IB)

35. The IB will operate in accordance with the Commercial Strategy which is adopted annually by Full Council. Cabinet will delegate to the Leader; Portfolio Holder for Finance and Budget and the S151 Officer (or Assistant Director of Resources for Aspire investments) to conclude investments where authorisation has been given by Full Council.

36. Constitution of the IB

- a. The IB is a Working Group of Cabinet and membership will be determined by the Leader of the Council
- b. In addition there will be two independent members to supplement the skills of the elected Members.

37. The investment decision making and monitoring process is as set out overleaf



38. Democratic Process (blue line)

- a. As part of the annual budget setting process, Cabinet develops the Commercial Strategy in consultation with the IB. Cabinet recommends to Council the adoption of the Commercial Strategy.
- b. Council adopts the Commercial Strategy.
- c. The IB develops a protocol to implement the Commercial Strategy which will be approved by Cabinet.
- d. The Cabinet will receive from the IB quarterly updates, including KPIs, on the performance of the portfolio.
- e. For new investments, the IB reviews the business cases and if appropriate supports a recommendation to Cabinet for the acquisition.
- f. Cabinet reviews the investment and if satisfied recommends to Council that funding is made available. Given that the IB will be constituted by members with a knowledge of commercial investment, supplemented with external training as necessary, and supported by industry expert independent people, it is acknowledged that Cabinet will not, without good reason duly considered, reject opportunities presented by officers that are supported by the IB.
- g. Ahead of the Council meeting, the IB Chairman, along with officers, undertakes an all-Member briefing session to set out the investment and the reasons for its recommendation.

39. Internal Process (red line)

- (a) The IB provides the two Aspire companies with a Commercial Protocol and sets out in detail the type of new investments it is seeking. Aspire (CRP) Ltd looks after developments at Chesterford

Research Park, whilst Aspire (MRH) Ltd is responsible for residential housing to be let at market rents. The Council's Asset Team will manage all other non-CRP commercial investments.

- (b) Depending on the category of investment sought, Aspire (MRH) Ltd, Aspire (CRP) Ltd or the Asset Team, working with professional advisors, will identify investments which meet the protocol set out by the IB. They will prepare investment business cases for consideration by the IB. The IB will review and consider the cases in detail and if suitable will make the recommendation to the Cabinet to proceed. Approval by the Boards the Aspire companies is also required prior to submission to the IB.
- (c) The Aspire companies, along with the Asset Team, prepare the quarterly KPI and other information for submission to the IB.

40. New Investments (green line)

- (a) At an Extraordinary Meeting of Council a decision is taken on whether or not to allocate the funding.
- (b) If the investment is agreed, funding will be made available to the relevant Aspire company or to the Asset Team to enable the purchase to be made.
- (c) The Aspire companies report annually to the Cabinet as the shareholder board of the Council.

41. Governance, Audit and Performance Committee (GAP) (black line)

- (a) A report on annual performance of the Aspire companies is taken to the GAP Committee. A similar report will be presented by the Asset Team.

Joint Working

- 42.** The Council recognises the benefits of working with other parties, be they local authorities or private sector. Joint Working mitigates risk and has the potential to enable the Council to consider new commercialisation opportunities in markets that alone they would not be able to do so.