

CABINET MEETING: November 2015

REVIEW OF THE NON OPERATIONAL ESTATE

REPORT OF CORPORATE DIRECTOR AGENDA ITEM:

PORTFOLIO: Economic Development

Reason for this Report

1. Following an independent review of the Council's Non Operational (Investment) Estate to seek authority to centralise all income generating property under the management of the Strategic Estates department and to establish a discrete Investment Estate with specific new governance and management arrangements.

Background

2. The Council's Non Operational Estate comprises circa 600 properties which the Council leases to external companies and organisations in the following categories:
 - 84 leased shops on market rents
 - 51 ground leased shops
 - 18 commercial properties (mainly strategic sites in the city centre)
 - 25 pubs and clubs
 - 6 hotels on ground leases
 - 96 industrial ground leases
 - 143 workshop units comprised in 9 separate estates
 - 54 community assets (e.g. community halls, churches and sports facilities)
 - 63 tenancies Cardiff Indoor Market
 - 83 other let properties (e.g. advertising hoardings, electricity substations, agricultural lettings etc.)
3. The Non Operational Estate is managed by the Council's Strategic Estates department on a commercial basis and it produces a total gross income to the Council of £5.2m, before deducting management and maintenance costs. This income is used to support the Council's core revenue budget.

4. The portfolio of this estate is diverse with a mixture of commercial properties at market value and community buildings leased historically at peppercorn rents. At present there are some inconsistencies in terms of how the properties are managed with some still controlled directly by Council service areas and not by Strategic Estates. In addition, the diverse nature of the Non Operational Estate can cause confusion in terms of the purpose for holding an asset and the subsequent processes required for management/disposal.
5. An independent review of the Council's Non Operational Estate was undertaken in January 2015 by property consultancy Jones Lang LaSalle (JLL) and a copy of the report is attached as Appendix 1. JLL made a series of recommendations which are considered in this report. These included rationalising the estate by selling low yielding management intensive properties and to reinvest the capital by acquiring better yielding assets. JLL further advised that reinvestment of capital receipts in the estate is required to retain and improve the asset value.
6. In January the PRAP Scrutiny Committee received a presentation from JLL. The Chairman of the Committee asked that a number of their views be taken into account. These included:
 - That the community and social benefits be taken into account as well as financial considerations.
 - That the community benefits of the market rented shops be taken into account in the decision making process.
 - Where community assets are considered for transfer that sound business cases should be in place and there must be a community capacity to take on these buildings.
 - It was requested that full ward member consultation is undertaken where disposal of assets is proposed.
 - That the Council's strategic sites in the city centre be retained.

Issues

7. At the present time there is no defined rationale or governance to effectively manage the Council's Non Operational estate. As a consequence decisions in terms of lettings, disposals and estate rationalisation can be ad hoc with varied authorities being applied.
8. Given the range of assets currently included in the Non Operational Estate the purpose for holding an asset is not clear.
9. Investment to modernise the estate is sporadic, and maintenance expenditure for the upkeep of the estate is not undertaken on a structured basis. The condition of the estate is variable with some of the more modern properties being in good condition and with some in need of extensive maintenance work. The current maintenance backlog for this portfolio is estimated to be circa £2m. Maintenance work is financed from the Asset

Renewal Programme on a standard prioritised basis each year but this does not address the work needed and is not a sustainable solution.

10. Some properties within the Non Operational Estate are held across service areas and are utilised to support revenue budgets. This results in sub-optimal management of the estate.

The Proposed Approach

11. The Non Operational Estate has been assembled over many years and consists of many properties that are a legacy of the Council's previous operational activities. In particular, the estate consists of properties that have good commercial purpose and others that are retained primarily for community purposes. It is therefore proposed to re-categorise the Non Operational Estate and to split the estate to create a new 'Investment Estate', with the residual properties being managed as part of the operational estate.
12. The proposed properties to be included in the Investment Estate are presented in Appendix 2. This will create a portfolio of properties that are held solely for income generation purposes.
13. It is proposed to establish a new governance arrangement to manage decision making relating to the Investment Estate to ensure that the portfolio is managed within a strict framework. This will involve the disposal of poor performing assets in terms of yield (return on investment); re-gearing of some existing arrangements; investment in properties that have the potential to generate further income; and the purchase of properties that will deliver a better yield.
14. To enable this, it is proposed that all capital receipts from the disposal of assets within the Investment Estate are ring-fenced to be reinvested in the Investment Estate with a view to generating increased income.
15. It is proposed to establish a new governance arrangement to deal with the efficient management of the Investment Estate. This will involve a new Investment Board consisting of officers from Strategic Estates, Legal and Finance. Day to day management will be undertaken by Strategic Estates with external advice through an appointed Commercial Agent. Recommendations for disposal, investment, re-gearing and acquisition will be presented quarterly to the Investment Board. Decisions will be reported quarterly to Asset Management Board and subsequently to Cabinet.
16. In the first instance Strategic Estates will build on the initial review undertaken by JLL and for each asset will determine which of the following three actions is appropriate:
 - Retain: good investments, hold as they provide a good return;

- Remodel: consider how existing investments can be improved, i.e. re-gear existing leases on better terms or invest in the asset.
 - Release: the asset does not deliver an appropriate return on investment and should be sold. The capital receipt from this sale is then ring-fenced to either invest in an existing asset or purchase a new better yielding asset.
17. It is also intended that the Investment Board directs facilities management spend in relation to these assets, in particular spend on maintenance/asset renewal.
 18. The residual properties that are currently part of the Non Operational Estate that do not form part of the Investment Estate will be managed as part of the Council's Operational Estate and will be subject to the same decision making processes involving local Member consultation and Cabinet approvals accordingly. This is considered the appropriate approach for the residual properties as they retain an element of local and community interest.

Reason for Recommendations

19. To enable Cabinet to approve the establishment of a governance structure and series of actions to enable Strategic Estates to effectively manage this strategic property asset with a view to creating a more commercial and better yielding investment estate.

Financial Implications

20. The Council's investment properties generate rental income to support the Council's overall budget.
21. The report proposes steps to be taken to ensure all non-operational property is managed by strategic estates, and categorised into commercial and operational. This then with a view to seeking opportunities to increase return where possible and disposing of low yielding and management intensive assets which are not in line with Council objectives. In determining whether properties are retained or not, consideration should also be given to the Council's responsibility for maintenance and whether the Council can afford to undertake such works.
22. The report proposes earmarking of any capital receipts /or lease premiums from the disposal or re-gearing of the commercial estate to new or existing commercial assets with a view to creating new assets or increasing income to offset the loss of income. This can only take place where receipts are not committed for other purposes e.g. in supporting the affordability of the capital programme.
23. Where rents are charged below commercial terms, or where disposal of assets takes place, there will be a detrimental impact on revenue income

unless it results in reduced management and maintenance costs or increased income from re-investment or regearing of existing leases. The report proposes that the impact of this be considered when setting the Council's revenue budget.

Legal Implications (including Equality Impact Assessment where appropriate)

24. The Council has an underlying fiduciary duty to ensure value for money from the acquisition, management and disposal of public assets

RECOMMENDATIONS

Cabinet is recommended to:

- (i) Agree to the principle of all commercial income producing properties to be held corporately, managed by Strategic Estates, with associated budgets to be realigned accordingly.
- (ii) Agree to the establishment of a new Investment Estate as detailed in Appendix 2 and to approve the proposed governance and operational arrangements set out in paragraphs 11-17 of this report.
- (iii) As part of (ii) above to agree to the principle of ring fencing and reinvesting all capital receipts generated from the disposal of assets in the newly formed Investment Estate to improve the yield of existing assets or to purchase better quality and better yielding assets.
- (iv) Delegate authority to the Director Economic Development, in consultation with the Leader of the Council, the Section 151 Officer and the County Solicitor to take all decisions in regard to the management of the Investment Estate and to provide an annual report as part of the Corporate Asset Management Plan.

Neil Hanratty

Director of Economic Development

November 2015

The following Appendices are attached:

Appendix 1: Independent Review of the Non Operational Estate

Appendix 2: Investment Estate Schedule