Agenda Item No:

CARLISLE CITY COUNCIL
www.carlisle.gov.uk

CORPORATE RESOURCES OVERVIEW AND SCRUTINY COMMITTEE

Committee Report

Public

Date of Meeting: **12 APRIL 2007**

Title: **ASSET REVIEW**

Report of: **Director of Development Services**

Report reference: **DS37/07**

Summary:
The Executive considered the attached report CE11/07 on 19 February 2007. The minute from Corporate Resources Overview and Scrutiny Committee of 22 February, CROS.18/07 is also attached. The item is on this Agenda for the Committee to scrutinise the Executive report.

Recommendations:

The Committee is asked to consider and comment on the information in the attached Executive report.

Contact Officer: Catherine Elliot **Ext:** 7502

Note: in compliance with section 100d of the Local Government (Access to Information) Act 1985 the report has been prepared in part from the following papers: None

CARLISLE CITY COUNCIL
www.carlisle.gov.uk

REPORT TO EXECUTIVE

PORTFOLIO AREA: ECONOMIC DEVELOPMENT & ENTERPRISE / FINANCE & RESOURCES

Date of Meeting: 19 February 2007

Public/Private* Public

Key Decision: Yes **Recorded in Forward Plan:** Yes

Inside Policy Framework: Yes

Title: ASSET REVIEW
Report of: Director of Carlisle Renaissance
Report reference: CE 11/07

Summary:

The City Council holds a significant portfolio of assets across Carlisle. This portfolio generates considerable income for the City Council and has an important impact upon the local economy.

In June 2006 a report titled "Asset Review – A Future Strategy (Options Appraisal & Business Cases)" was presented to a workshop of the Corporate Resources Overview & Scrutiny Committee. A copy of that report is included in Part B of the Executive Committee agenda.

This report summarises the key findings and recommendations presented to the Overview & Scrutiny Committee, reviews the current policy context for the Asset Review, and outlines the concept of a Local Asset Vehicle as a mechanism for delivering the objectives of the Asset Review.

Recommendations:

Note: in compliance with section 100d of the Local Government (Access to Information) Act 1985 the report has been prepared in part from the following papers: None

The Executive are recommended to:-

a) Agree to the principle of establishing a Local Asset Vehicle (LAV) as a mechanism for delivering the objectives of the Asset Review

b) Direct the Asset Management Group (AMG) to undertake a detailed investigation into the risks and benefits of a LAV to the City Council and present a report of their findings to a future meeting of the Executive Committee

c) Agree to the release of £100,000 from the Asset Reserve to enable the procurement of such property, legal financial and other specialist advice that may be required by the AMG to undertake this investigation.

Contact Officer: Ian McNichol **Ext:** 7399

1. BACKGROUND

1.1 The City Council holds a portfolio of assets across Carlisle with a book value of over £110m generating income in excess of £5m per annum. It is estimated that over 12,000 people work in property that makes up the portfolio. In 2001 an Audit Commission Best Value Inspection Report of Property Services & Economic Development identified the need for a strategy to rationalise the portfolio, maximise returns and sustain the quality and economic value of the assets.

1.2 In 2003 a report by property consultants Lamb & Edge highlighted that without a change in approach to its portfolio the City Council could see a considerable reduction in income and an increased liability over the long term. Whilst noting the significant role the City Council has in the local property market it concluded that without a change of approach it could be seen to be holding up economic development

1.3 An Asset Review Scoping Report was published in April 2004, setting out the purpose of the review to deliver: -

- Clear and consistent policies for the various elements of the City Council's property portfolio
- A transparent strategy for maintaining and sustaining the City Council's property related income
- Economic development benefits and a framework for investment

1.4 An Asset Management Group (AMG) of City Council officers was established (chaired by the then Head of Property Services) to lead the review and co-ordinate a series of work packages, including liaison with stakeholders and external agencies. Responsibility for steering the review and the work of the AMG was allocated to the Corporate Resources Overview & Scrutiny Committee (CRO&S).

1.5 On 23 January 2006 (PS 02/06) the Executive noted progress on the first stage of the Asset Review to deliver -

- A draft corporate property policy statement
- An assessment of the property portfolio, including liabilities, maintenance, values and income
- An analysis of delivery options including joint ventures, external management, direct development etc.

- A draft strategy for operational and non–operational property, surplus property and property acquisition

1.6 At that stage the Executive released funding from the Asset Reserve to engage property consultants to assist with the Asset Review process. In June 2006 (DS 37/06) the Executive approved the draft Asset Management Plan (2006-2011). This was subsequently approved by CRO&S (DS 39/06).

1.7 On 27 July 2006 the then Head of Property Services presented a report titled “Asset Review – A Future Strategy (Options Appraisal & Business Cases)” to a CRO&S workshop. A copy of that report is included in Part B of the Executive Committee agenda. A further CRO&S workshop took place on 5 October 2006, with a presentation by Hyde Harrington, who assisted in the preparation of the original report. .

1.8 This report summarises the key findings and recommendations presented to the Overview & Scrutiny Committee, reviews the current policy context for the Asset Review, and outlines the concept of a Local Asset Vehicle as a mechanism for delivering the objectives of the Asset Review.

2. A FUTURE STRATEGY (OPTIONS APPRAISAL & BUSINESS CASES)

2.1 The report presented to CRO&S sets out proposals for the City Council’s property portfolio, which is divided into a series of 11 different categories: -

a) Main industrial estates
b) Workshops
c) Enterprise Centre
d) Misc. industrial estates
e) Other strategic assets
f) Sustainable commercial assets
g) Sustainable commercial assets with strategic opportunity
h) Sustainable ‘service’ assets with development opportunity
i) Unsustainable ‘commercial’ assets with strategic potential
j) Unsustainable ‘service’ assets with strategic potential or requiring investment
k) Surplus assets

2.3 The report recommends the retention of all assets in categories (e) to (j) and the disposal of all assets in category (k). For the remaining assets the report makes individual recommendations for each asset, either to retain, dispose of or joint venture with a private sector partner. Each recommendation is supported by a business case, which reviews current issues and sets out long term requirements, funding, a possible timetable and a risk assessment.

2.4 The report forecasts that the impact of these recommendations (against a "do nothing" base case), if adopted, would be as follows: -

- An additional increase in annual income of £0.5m within 3-5 years rising to £1m within 10-15 years and £1.5m in 20 years
- An additional increase in the capital value of the portfolio by £20m in 20 years
- A reduction in the portfolio maintenance backlog to nominal levels within 10 years
- A reduction in ongoing maintenance by 50% within 5 years
- A net surplus of £5m capital receipts over a 20 year period.
- An improved supply of business accommodation with associated employment growth

2.5 In the process of preparing the report a number of other options for delivering the strategy were discounted. These were: -

- Establishing a single joint venture into which all non-operational properties are transferred, managed and developed
- The City Council acting as a developer in its own right
- Establishing a strategic property partnership which covers the management and development of both the operational and non-operational assets.

2.6 The first of these options was discounted on the grounds that it may not be appropriate for Carlisle's property market and the size of the Council's portfolio in relation to the organisation, although the report did recommend investigating this option with caution "only if the City Council accepts the potential rental loss implications"

2.7 The second of these options was discounted on the grounds of the risks to and resource implications for the City Council associated with direct development, although the report did recommend considering this approach if private sector partners could not be secured for some or all of the assets where a joint venture approach was proposed.

2.8 The third of these options was discounted on the basis of loss of income, potential negative impact upon the property market and the fact that the City Council's operational property does not have a major maintenance backlog.

2.9 The report suggest that the process of delivering the strategy could be self-financing on the basis that investment in and maintenance of the portfolio is financed by disposals and income growth, but that this can only be achieved if all the recommendations are implemented within the timeframe proposed. The report does not set out a detailed plan for the implementation of the recommendations. Previous work on the Asset Review has been financed from the Asset Reserve but there is currently no provision in the Medium Term Financial Plan (MTFP) to finance the implementation of the recommendations.

3. POLICY CONTEXT

3.1 Much of the rationale for the Asset Review remains as it was at the beginning of the review process: -

- Pressure for public sector spending efficiencies from Central Government
- The need for continuous improvement in the quality of services delivered by the City Council
- The opportunity cost of not investing in the portfolio in terms of reducing returns
- The challenge to effective medium term financial planning associated with reactive property maintenance
- Opportunities presented by the introduction of the Prudential Borrowing Code

3.2 A fundamental issue for the City Council is the degree to which it relies on the income generated from its property portfolio for the delivery of services. Whilst the majority of this income derives from more secure longer term leasehold arrangements, fluctuations in short term property derived income, such as car parking income, have a disproportionate impact upon its budget structure.

3.3 Since the commencement of the Asset Review a series of policy developments have taken place at a local, regional and national level which potentially impact upon the review process and ultimately the delivery of any property strategy, including Carlisle Renaissance, Shared Services, the Local Government White Paper and the sub-national review of economic development and regeneration, which is being carried out jointly by the Department for Communities and Government, HM Treasury, and the Department of Trade and Industry.

3.4 The City Council has committed to play a leading role in the delivery of Carlisle Renaissance, a long term vision for economic, physical and social regeneration. The ability of the City Council to fulfill this role will depend to a greater extent upon its ability to secure investment in regeneration from the public sector and stimulate investment by the private sector. In turn this will determine the scale and pace of the delivery of the renaissance agenda.

3.5 A Development Framework & Movement Strategy (DF&MS) was published on the 30 January 2007. A number of the proposals emerging from the work to date will require public sector funding to deliver. External partners such as Cumbria Vision, the Northwest Development Agency and English Partnerships have already committed investment to this process and have expressed a willingness to invest further funding. The City Council is likely to be required to match this funding from its own resources.

3.6 Other aspects of the renaissance agenda are also expected to require funding from the City Council if they are to proceed, particularly for activities where access to external funding is likely to be limited. Securing external revenue funding for tackling deprivation and delivering interventions to stimulate growth in the local economy has been a significant challenge for the City Council in the past. The area is not eligible for Neighbourhood Renewal funding or any significant European Structural funding and is unlikely to be so for the foressable future.

3.7 The City Council is participating in a Shared Services Property Review with the County Council, which will involve a number of public sector organisations in identifying opportunities for consolidating operational property and improving access to services. A Memorandum of Understanding (MOU) has been agreed by public sector occupiers in the Rickergate area of the City which will consider opportunities for shared property and in parallel the City Council is undertaking an Accommodation Project to assess its own operational property requirements.

3.8 The Local Government White Paper clearly has significant implications for the City Council, including proposals for the restructuring of local government in Cumbria The White Paper promotes the concept of City Development Companies (CDCs) to drive forward economic growth and regeneration, linked to the Government's sub - national review of economic development and regeneration. The Government is now consulting on CDC proposals, including their functions, governance and funding.

3.9 The CDC Consultation Paper makes reference to a number of local authorities looking at the creation of Local Asset Vehicles (LAVs), which combine locally-owned public sector assets and equity from institutional investors to finance and deliver regeneration activities, particularly physical regeneration. Similar approaches have been adopted at a national and regional level by British Waterways, One North East, East Midland Development Agency and the Northwest Development Agency

3.10 English Partnerships (EP) has established an Urban Finance Unit (UFU) to work with public sector organisations and leading organisations in the investment market to facilitate such public private property partnership arrangements, providing both sectors with advice, guidance and practical support. EP has advised the City Council on the LAV concept.

4. LOCAL ASSET VEHICLE

4.1 The Local Asset Vehicle (LAV) concept is based on experience of existing public private property partnerships. It involves the establishment of a special purpose vehicle into which a public sector organisation transfers property assets and the private sector partner contributes cash and other resources. Selection of a private sector partner is by competitive tender.

4.2 The Memorandum and Articles of Association of the LAV set out the aims, objectives and operating rules, and in most instances it is 'deadlocked,' meaning that both partners must agree on strategic issues before any course of action is pursued. This serves to ensure the public sector partner retains a degree of control over the activities of the LAV in relation to the level of risk taken on by the private sector partner.

4.3 The transfer of assets to the LAV could be in one go or phased based on agreed businesses plans, again limiting the level of risk to the public sector partner. The assets transferred could encompass any or a mix of the following: -

- Surplus property
- Investment property
- Sites for development
- Operational assets
- Income producing assets
- Capital from reserves

4.4 Experience from the establishment of previous partnerships is that the actual value the private sector attributes to public sector property portfolios is significantly in excess (by as much as 30%) of their estimated market value. The reasons for this are three-fold: -

- Letting premium - there is a premium associated with the aggregation of assets to form a good-sized portfolio, many investors will pay for the opportunity of buying into such a portfolio
- Marriage value - derived from combining assets which are linked geographically or functionally (i.e. adding to an existing industrial portfolio)
- Securing product pipeline -for institutional investors existing portfolios provide a safe haven for funds on day one and the opportunity to develop these assets to secure income growth

4.5 The selection process is generally based on three stages; expressions of interests, invitation to tender and invitation to negotiate. The public sector organisation is at no stage obliged to enter in to any agreement and the costs incurred by them are typically recouped from any partner selected. Previous partnerships have involved expenditure of up to £0.5m by the public sector organisation to secure a partner and the procurement process has typically taken 9-12 months.

4.6 The principal difference between existing examples of the application of the LAV concept and that which may be applicable to the City Council is the extent to which the City Council is dependant upon the income generated from its property portfolio. For this approach to be of any advantage to the City Council it would need to secure from a private sector partner: -

- A guarantee to maintain the level of income the City Council currently derives from the portfolio introduced to the LAV
- An agreement to share any increase in revenue from the portfolio with the City Council
- Capital to invest in the portfolio
- Revenue to operate the LAV
- A premium (capital sum) to support investment in regeneration projects such as those proposed in the DF&MS.

4.7 This specific approach has yet to be tested in the market place. EP's UFU has indicated its willingness to 'soft' market test this proposition with institutional investors to gauge their appetite. The strength of interest may be determined by the type of assets that the City Council is prepared to introduce to the LAV. This would also determine the range of property related services retained directly by the City Council.

5. CONCLUSION

5.1 The Asset Review reached a significant milestone with the production of the option appraisal and business cases in June 2006. Much of the original rationale for undertaking the review remains but more recent developments in public policy at all levels and experience in the establishment of public private property partnership elsewhere suggests that there is an opportunity to examine in further detail the establishment of a Local Asset Vehicle by the City Council.

5.2 The proposals set out in the report published in June 2006 are within the draft corporate property policy approved by the Executive in January 2006, insofar as they recommend the investment, retention, acquisition and disposal of property in the portfolio and to use public private partnership where appropriate.

5.3 The LAV approach is contiguous with this policy but requires a different approach to that recommended in the existing report. It would involve assembling a package of assets from within the portfolio, including potentially those recommended for retention if appropriate, and selecting a single private sector partner to establish a special purpose vehicle.

5.4 The implications for and risks to the City Council in adopting this approach are potentially significant in legal, financial, operational and governance terms. The first stage of progressing this approach would be though further detailed investigation by which the City Council can determine in detail: -

- Its objectives in establishing a LAV
- The property that would be prepared to transfer to a LAV
- Its preferred corporate structure for a LAV and associated legal implications
- The minimum financial offer it expects from a private sector partner
- The procurement process, including the costs of procurement
- Risks to the City Council and proposals for mitigating these risks
- The degree and nature of interest from the investment market (i.e. market testing)

5.5 This work would be led by the AMG, chaired by the Director of Development Services, with support from EP’s Urban Finance Unit. Responsibility for steering the work would be allocated to the Corporate Resources Overview & Scrutiny Committee (CRO&S).

5.6 It would require the allocation of additional resources from the Asset Reserve to finance property, legal, financial, planning and other such advice that may be required. A budget of up to £100,000 is considered appropriate and the process is expected to take approximately 4 months to complete. Future budget requirements would be determined at that stage.

6. CONSULTATION

6.1 The following have been consulted in the preparation of this report: -

- Strategic Planning Group
- Director of Development Services
- Director of Corporate Services
- Director of Community Services
- Director of Legal & Democratic Services
- Asset Management Group
- English Partnerships Urban Finance Unit
- Northwest Development Agency
- Property consultants

6.2 In addition to the above the following will be consulted: -

- Corporate Resources Overview & Scrutiny Committee
- Department of Communities & Local Government
- Existing public private property partnerships
- Occupiers of City Council property
- Lanes and Market Hall partners
- Trade Unions
- Cumbria Chamber of Commerce
- Government Office for the North West

7. RECOMMENDATIONS

7.1 The Executive are recommended to:-

a) Agree to the principle of establishing a Local Asset Vehicle (LAV) as a mechanism for delivering the objectives of the Asset Review

b) Direct the Asset Management Group (AMG) to undertake a detailed investigation into the risks and benefits of a LAV to the City Council and present a report of their findings to a future meeting of the Executive Committee

c) Agree to the release of £100,000 from the Asset Reserve to enable the procurement of such property, legal financial and other specialist advice that may be required by the AMG to undertake this investigation.

8. REASONS FOR RECOMMENDATIONS

8.1 To progress the work of the Asset Review to rationalise the property portfolio, maximise returns and sustain the quality and economic value of the assets.

9. IMPLICATIONS

- Staffing/Resources – The establishment of a LAV could involve the transfer of staff from the City Council. Other examples of public private property partnership have involved the transfer of public sector employees on full TUPE terms.

- Legal and Financial Comments - The basic premise set out in the report is that the City Council should establish a joint venture limited company or similar special purpose vehicle with a selected private sector partner and the Council will then transfer to the special purpose vehicle a range of its property assets yet to be determined.

It is then proposed that the governance and income sharing arrangements within the vehicle will be structured in such a way that the City Council will receive at least the same income which it does now from the assets to be transferred (presumably with some guarantee for future growth at no less rates than would occur had the property been retained by the City) and that the Council would also look to receive a capital premium as consideration for entering into the joint venture arrangements, as well as the private sector partner undertaking to provide further capital to be invested in the portfolio which the City Council is unable to do. These suggested advantages to the City Council are set out in paragraph 4.6 of the report.

In terms of legal powers, the City Council has power under Section 2 of the Local Government Act 2000 to do anything which it considers is likely to achieve the promotion or improvement of the economic, social or environmental wellbeing of its area. This power is comprehensive and may be exercised in relation to or for the benefit of the whole or any part of the authority's area or all or any persons resident in it. It includes power to incur expenditure and to enter into arrangements or agreements with any person, and co-operate with or facilitate or co-ordinate the activities of any person. In determining whether or how to exercise the power, the Council must have regard to its own community strategy and to any relevant guidance issued by the Secretary of State. On the face of it, the power should be sufficient to enable the Council to establish a joint venture company and enter into an arrangement of the sort described in the report.

The proposals envisage that the Council would transfer the legal interests which it currently holds in the freehold and leasehold of the assets to the special purpose vehicle, which would then become the legal owner. The Council has power, under Section 123 of the Local Government Act 1972, to dispose of its interests in land in any manner it wishes, subject (with the exception of short term lettings) to it receiving the best consideration that can be reasonably obtained. In making any disposal to the special purpose vehicle the authority would be required to ensure that this obligation was complied with.

In addition to identifying appropriate powers to enable it to proceed as indicated in the report, the Council also has to have regard to its overriding fiduciary duty to its Council Tax payers when determining whether or not the course of action proposed is appropriate. This will involve an assessment of the risks and benefits accruing to the authority as a result of entering into the proposed arrangements. Members will be aware that the income stream enjoyed by the Council from its property portfolio underpins the Council's financial base and is critical in maintaining the authority's budgetary position. It is therefore crucial to be satisfied that any arrangements which are entered into do not detrimentally affect this income flow or expose it to unacceptably high risks.

Although there may be examples of similar joint vehicles operating (and it may be useful to examine them in more detail), the point is fairly made in paragraph 4.6 of the report that the level of the Council's dependency on income from its property holdings distinguishes it from other examples of Local Asset Vehicle use. Prior to committing itself to such a course, therefore, the Council needs to be satisfied that its income stream under any LAV sharing arrangement can be guaranteed at a level which is at least equal to that which it currently enjoys, including any future expected growth, for the duration of any joint arrangement, and that the overall benefits of participation exceed any risks arising. Consideration would need to be given in any negotiations as to whether, for example, provisions could be made for the transfer of the assets back to the Council if circumstances so dictated and the Council will need to give detailed consideration to this and other relevant risks and benefits before determining whether to proceed in this way.

.

- Corporate – The Asset Review process derives from the findings of an Audit Commission Best Value Review of Property and Economic Development services. It is identified in the Medium Term Financial Plan as one of a series of service reviews planned or underway.

- Risk Management – A risk assessment was produced as part of the report published in 2006. This will be updated and revised to reflect the risks associated with a LAV as part of the process of further detailed investigation.

- Equality Issues – None

- Environmental – Any LAV established will be expected to operate within the context of the Local Plan and environmental policies adopted by the City Council

- Crime and Disorder – None

- Impact on Customers – Occupiers of City Council property will be consulted during the process of further detailed investigation