

Agenda Item No:	5	
Committee:	Investment Board	
Date:	18 September 2020	
Report Title:	Filtering of Investment Opportunities	

1. Summary

For the Investment Board to agree a filtering process for identifying opportunities in accordance with Parts Two (Commercial Property Investment) and Three (Regeneration and Place Shaping Investment) of the Commercial and Investment Strategy approved by Full Council in January 2020.

2. Key Issues

The investment criteria and process for Commercial Property Investment were approved by Full Council in January 2020 and are attached here as Appendices 1 and 2 respectfully however, a filtering process is needed to narrow down speculative opportunities before this criteria and process are applied. Appendix 3 outlines a draft process for the Investment Board to discuss and approve to manage these opportunities.

3. Recommendation

It is recommended that:

- the Investment Board considers and agrees the draft process for identifying opportunities that are taken forward for full appraisal at future Investment Board meetings;
- the Investment Board note the investment criteria and process agreed by Full Council for the acquisition and disposal of Commercial Property.

Wards Affected	All Wards
Portfolio Holders	Cllr Chris Boden, Leader of the Council and Portfolio Holder for Finance
Report Originator	Paul Medd, Chief Executive Peter Catchpole, Corporate Director and s.151 Officer Carol Pilson, Corporate Director and Monitoring Officer Amy Brown, Chief Solicitor and Deputy Monitoring Officer
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Background Papers	Full Council Report dated 9 January 2020 Approval and Implementation of Fenland District Council's Commercial and Investment Strategy

Appendix 1: Assessment Criteria – Commercial Property Investment: Risk and Return Matrix

Criteria	Excellent	Very Good	Good	Acceptable	Marginal	Notes
Location	Major Prime	Macro Prime	Major Secondary	Macro Secondary	Tertiary	Preference would be given to locations either within or close to Fenland.
	Core and Core Plus approach					
Covenant	Single Tenant, Strong Financial Strength and Covenant	Single Tenant, Good Financial Strength and Covenant	Multiple Tenants, Strong Financial Covenant	Multiple Tenants, Good Financial Covenant	Tenant(s), Average Financial Covenant	The covenant of the tenant(s) is considered in terms of (audited) financial strength and risk of failure.
Lease Length	>10 years	7 – 10 years	4 – 7 years	2 – 4 years	<2 years	Length of lease will determine the fixed term of guaranteed rental income. In most cases, longer leases are more secure although break clauses need careful consideration.
Tenure	Freehold	Long Leasehold 125 years minimum	Leasehold >75 years <125 years	Leasehold <75 years	Leasehold <50 years	Freehold possession is best. Liquidity and marketability of properties are key considerations for leasehold.
Repair Obligations	Full Repairing and Insuring (FRI)	Internal Repairing 100% Recoverable	Internal Repairing Partially Recoverable	Internal Repairing Non Recoverable	Landlord Repairs	There are various levels of repair obligations; impacting structural, external and internal repairs to the property
Net Yield	+8%	5% - 8%	3.5% - 5%	2% - 3.5%	<2%	All investment opportunities must initially provide income (yield) at a positive rate of return after borrowing costs. Acquisition costs may include Stamp Duty Land Tax, agents' fees, legal fees and conveyancing costs.

Given the varied sector dynamics, the criteria for each asset will vary. However, the following core principles should apply in each case:

1. All investments considered must initially provide income (yield) equal to or above the Council's rate of return. This is defined by the cost of capital borrowing for purchase.
2. Individual properties and opportunities will be fully financially and physically appraised using industry standard techniques and the risk/return matrix.
3. To minimise management and risk, preference is for single occupancy investments.
4. Location will be dictated by opportunity to acquire investments that meet the strategy. However, location within the Fenland District or its impact on the economy within the Fenland District will be a deciding factor when all other attributes are equal.
5. Only investments with full repairing and insuring (FRI) terms or FRI by service charge will be considered.
6. Whilst determined by market forces, the aim is to maximise lease length.
7. Market rent should be equal to or above passing rent.
8. Preference will be for market sectors and locations with rental growth and good letting prospects
9. Further performance measures, portfolio analysis and valuation will take place as required during the holding period to allow for buy/sell/hold decision making.

2. Holding Period

It is normal to define a 'holding period' before sale at the time of purchase. This is to counter any significant depreciation eroding value or before the need for redevelopment arises. The holding period will be determined for each individual property at the appraisal stage.

3. Value Add

Value add (vacant or short leases), re-development opportunities or distressed property can reap high capital and yield returns. Whilst such properties can be appraised with the above principles and criteria, they will have different and higher levels of risk. The reasons for considering them must be fully evaluated and understood.

4. Issues not to be overlooked: risks and their management

Market Forces

To limit risk the principles, criteria and full due diligence will be undertaken for all transactions. Changes in demand and supply within the market and wider economy may see the value of investment and income rise and fall. The price of property is not the sole factor that should be considered for making a good investment in the long run.

Liquidity







Acquiring and disposing of commercial property can be complex. The process can result in transactional delay and uncertainty which carries risk from market shift, abortive transactional costs and speed of realising a capital receipt.

Active Portfolio Management and Opportunities

Performance of an investment property should be continually monitored as part of an active portfolio management strategy. Qualified in-house or third party auditors should keep up with market trends, manage asset plans, deal with day-to-day issues, examine lease structuring initiatives and protect against loss of income to ensure the investment yield is maximised.

The role of the property professional is to seek out as many opportunities as possible (often in a limited and highly competitive market), build relationships and communicate to the market the Council's requirements and ability to perform.

Appendix 2: Portfolio Acquisition and Disposal Flow Chart

Acquisition (Buying)	Flow	Disposal (Selling)
<ul style="list-style-type: none"> • Appraise property • Offers and counter offers • Agree Heads of Terms • Secure source of funds 	<p>Offer to market – Heads of Terms</p> 	<ul style="list-style-type: none"> • Instruct advisors; formulate asking terms and marketing strategy • Review property information; anticipate information and devise strategy • Procure energy performance certificate
<ul style="list-style-type: none"> • Instruct legal team • Investigate title • Undertake or commission surveys and reports • Negotiate contract 	<p>Pre-contract</p> 	<ul style="list-style-type: none"> • Consider carrying out and providing searches • Make available pre-contract legal pack and access to data • Negotiate contract
<ul style="list-style-type: none"> • Pay deposit 	<p>Exchange contract</p> 	
Parties committed to acquisition		
<ul style="list-style-type: none"> • Pre completion searches • Finalise mechanics for drawdown/transfer of funds for completion 	<p>Pre-completion</p> 	<ul style="list-style-type: none"> • Continue to manage property (in accordance with contract) • Preparation of completion statement • Prepare requisitions on title
<ul style="list-style-type: none"> • Pay completion monies • Assume liability for property 	<p>Completion</p> 	<ul style="list-style-type: none"> • Discharge borrowing liability
<ul style="list-style-type: none"> • SDLT/Land Registry tasks to be completed • Collation of property information • Portfolio management 	<p>Post-completion</p> 	

Appendix 3: Procedure for a Part Two or Three proposal

	Action	Governance
1.	Officers/FFL Directors in discussion with the Leader and members of the Investment Board identify possible opportunities for FDC/Fenland Future Limited to consider.	In principle proposal agreed with the Leader to take forward to the Investment Board. For Part Two opportunities the agreed investment matrix will act as the trigger to decide if any opportunity is worth taking forward.
2.	Meeting of the Investment Board to agree possible opportunity for recommendation to FDC/Fenland Future Limited for consideration. Where agreed, FDC/Fenland Future Limited to be formally requested to consider the proposal.	IB to consider in accordance with terms of reference 1.2.3(i): To oversee the relationships between the Council and the Council's companies and partnerships in accordance with the Council's objectives.
3.	FDC/Fenland Future Limited to draw up an Outline Business Case for approval.	For Part Two opportunities this will be determined by the investment criteria shown at Appendix A.
4.	FDC/Fenland Future Limited to present Outline Business Case to IB for consideration and approval to move to the production of a Full Business Case and any associated funding request.	IB to consider in accordance with terms of reference 1.2.3 (a) (b) and (c): (a) To determine investment appraisals submitted under Part 2 of the Council's Commercial Investments Strategy together with the most appropriate means of delivery; (b) To determine business cases submitted under Part 3 of the Council's Commercial Investments Strategy by the Council's companies and partnerships; (c) To determine the amount and terms of any investments, loans and assets required for the delivery of proposals approved in accordance with paragraphs (a) and (b) above from the agreed budget allocation.
5.	FDC/Fenland Future Limited to draw up a Full Business Case for approval.	For Part Two opportunities this will be determined by the investment criteria shown at Appendix A.

6.	FDC/Fenland Future Limited to present Full Business Case and any associated funding request to IB for approval.	<p>IB to consider in accordance with terms of reference 1.2.3 (a) (b) and (c):</p> <p>a) To determine investment appraisals submitted under Part 2 of the Council's Commercial Investments Strategy together with the most appropriate means of delivery;</p> <p>(b) To determine business cases submitted under Part 3 of the Council's Commercial Investments Strategy by the Council's companies and partnerships;</p> <p>(c) To determine the amount and terms of any investments, loans and assets required for the delivery of proposals approved in accordance with paragraphs (a) and (b) above from the agreed budget allocation.</p>
7.	FDC/Fenland Future Limited to deliver against the agreed business case and funding agreement.	<p>IB to monitor the progress of delivery in accordance with terms of reference 1.2.3(f):</p> <p>To monitor performance and financial delivery in line with the approved business plans.</p>