

CABINET

20 October 2020

Title: Investment and Acquisition Strategy Update	
Report of the Cabinet Member for Finance, Performance & Core Services	
Open Report with Exempt Appendix 2 (relevant legislation: paragraph 3 of Part I of Schedule 12A of the Local Government Act 1972)	For Decision
Wards Affected: All	Key Decision: Yes
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Accountable Director: Philip Gregory, Finance Director	
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Summary: <p>In September 2019 Cabinet approved an updated Investment and Acquisition Strategy (IAS) to support the Borough's growth opportunities and to ensure that the Council, and future generations, benefit by increasing the Council's ownership of long-term income producing assets. The IAS is reviewed annually, with this being the fourth version.</p> <p>An objective of the investment strategy is to generate net income of £5.12m by 2020/21. This report provides an update on the performance of the IAS in 2019/20, outlining the changes that have impacted the strategy over the past year. The report also provides the outturn for 2019/20, provides a forecast of the returns expected over the coming four years and the current position of the IAS reserve.</p> <p>This report highlights the financial constraints and opportunities within the IAS. It stresses the importance of bringing schemes into operation as soon as possible to ensure both the regeneration of the borough and the availability of funding available for subsequent schemes.</p> <p>This report also identifies a number of pressures that there are on the strategy but also to establish a method of managing any impact on the Council's revenue budget. An additional consideration is on the impact of leverage on the strategy and the need to bring a more long-term and measured approach to development that can allow schemes to be built and operational before more schemes are agreed.</p> <p>The report also includes a proposal to increase the size of the loan previously agreed by Cabinet to Robyna Limited in respect of the redevelopment of the site at London Road / North Street, Barking.</p> <p>The report is at a point in time and there are schemes in the pipeline that may change and improve the IAS return but there are also challenges posed by increasing build costs and also from the economic impact that Covid-19 and Brexit may have on the</p>	

strategy. These schemes include Beam Park and the development of the Film Studio site, which are being presented for consideration to Members at this Cabinet Meeting.

The report highlights that the Council is in a relatively strong position with its investment strategy and this could result in a very strong balance sheet position going forward if the IAS performs well.

Recommendation(s)

Cabinet is recommended to:

- (i) Approve the updated Investment and Acquisition Strategy set out at Appendix 1 to the report;
- (ii) Note that the IAS and Borrowing Outturn 2019/20 showed a £0.6m underspend for 2019/20;
- (iii) Note the progress being made in meeting the IAS income target and the impact on the IAS of the delays to schemes being completed;
- (iv) Note the governance and controls in place to manage the IAS;
- (v) Note the increase in gross borrowing costs (£105m) and net borrowing costs (£319m);
- (vi) Note the potential for commercial loans and commercial income to support the investment strategy, especially over the short-term;
- (vii) Note the impact of leverage on the IAS and the proposals regarding life-cycle costs reporting and funding; and
- (viii) Agree that the loan to Robyna Ltd in respect of the North Street / London Road residential-led development be increased from £35m to £44m to take account of the increased units to be developed at the site, on the terms set out in Appendix 2 to the report.

Reason(s)

The proposals in this report will support the regeneration and economic growth of the borough and will help to support the long-term financial sustainability of the Council.

1. Introduction and Background

- 1.1 The Council's first Investment and Acquisition Strategy (IAS) was agreed by Cabinet in November 2016 as part of the Council's response to the unprecedented challenges it faced from Government cuts to public sector spending. The strategy has been subsequently reviewed a number of times, with the last review in September 2019.
- 1.2 The purpose of the IAS is to support the Borough's growth opportunities and to ensure that the Council, and future generations, benefit by increasing the Council's

ownership of long-term income producing assets. The scale of investment within the Borough is significant with in excess of 50,000 new homes to be built over the next twenty years. This will be accompanied by increased demand for employment space and sustainable energy providing the Council with a key leadership and investment opportunity.

- 1.3 The IAS enables the Council to make investments that have the potential to support economic growth and / or deliver economic regeneration within the borough. In some cases, schemes with lower returns may be considered for strategic reasons. To accelerate the Council's regeneration, a development company, Be First, was created. They have reviewed and reconfigured the development pipeline, have brought new investment opportunities to the Council and have identified new asset classes to support private sector led regeneration.
- 1.4 In line with Government Guidance on Local Authority investment activities, this report provides an update on delivering investment objectives and sets-out the criteria to approve and finance investment opportunities going forward.
- 1.5 In 2019/20 the IAS has come under pressure from scheme delays and an increase in build costs. At the same time, a number of developments have also been accelerated, which has increased the funding requirement of the IAS. The pressures on the IAS has been contained to date from a decrease in borrowing costs and from good returns from treasury investments. The Council holds £326m in cash to fund the IAS, which was sufficient to fund the majority of the long-term financing for the developments agreed as part of the 2019/20 IAS. With the increase in costs and with new schemes being agreed, further borrowing is required for the 2020/21 IAS.
- 1.6 An increase of 1% in the PWLB margin in October 2019 increased the cost of new borrowing and has required the Council to look for alternative sources of financing. While it is possible to obtain external funding as the Council has a strong covenant, it does not come without a cost and additional risk. These risks and costs are outlined in the report, as is the impact of leverage on the IAS.
- 1.7 Covid-19 has had an impact on the strategy, with schemes being delayed as construction work was halted or reduced at some sites. For operational schemes, the impact of reduced rent may only be fully known after the Q3 2020 rental income figures are analysed. The impact on the IAS is mixed as, although there will be a loss of income, it will reduce the immediate requirement to borrow, resulting in lower borrowing costs. The treasury return forecast for 2020/21 is also good and should be able cover the cost of holding the borrowing.
- 1.8 As most of the Council's investments are in largescale, in-borough residential developments, the Council will change its accounting policy on interest payable for funding these schemes, from one which is funded from its revenue budget, to one where the costs are capitalised (added) to the overall development costs and are repaid as part of the overall scheme repayment over 50 years. This option is available for qualifying asset, which are assets that take in excess of two years to get ready for intended use and where expenditure is in excess of £10m. This change will reduce the impact on the revenue budget of borrowing costs for scheme during development but will increase the overall amount that will need to be repaid by each scheme.

2. IAS and Borrowing Outturn 2019/20

- 2.1 For 2019/2, **borrowing costs** were higher than forecast by £0.6m due to an additional £80.0m borrowed from the PWLB as there were opportunities to lock in low borrowing rates towards the end of the financial year. In addition, the sale of the Film studio, forecast for 2019/20, did not occur and therefore additional borrowing during the year was required. Less borrowing was required for the residential schemes due to delays, but more borrowing was required to fund commercial purchases.
- 2.2 **General Fund interest income** was £2.3m more than budgeted due to good treasury returns and interest from loans the Council made to Reside and to its subsidiaries. Treasury have locked in rates at an average of 1.65% for 2020/21 on £280m and this will be used to cover the cost of borrowing but also to fund developments.
- 2.3 **Investment Income** totalled £2.7m compared to a budget of £4.3m, a shortfall of £1.6m. The shortfall is due to Weighbridge and Wivenhoe modular not being operational in 2019/20 and commercial loans for the London Road and Axe street developments being delayed. Going into 2020/21 there have been further delays caused by Covid-19. However, when combined, the treasury and IAS overachieved its target by £57k in 2019/20.
- 2.4 As there is a significant interdependence between the interest budget and the IAS due to a portion of the investment income received via interest charged on loans, the total return for the IAS includes the interest position. Table 1 below shows the IAS and Treasury outturn for 2019/20, showing a small surplus against budget of £57k.

Table 1: IAS and Treasury Outturn 2019/20

IAS and Interest Outturn 2019/20			
IAS Outturn		Interest Outturn	
	000's		£000's
IAS Target	3,733	Interest Expense Budget	(11,769)
Abbey Road 2 MRP	600		
Total IAS Target	4,333	Interest on Long Term Loans	(11,111)
		Interest on Short-term Loans	(1,263)
Residential Surplus Returns		Total Interest Payable	(12,374)
Abbey Road £600k MRP	600	Surplus (deficit)	(605)
Reside Ltd Surplus Rent	242		
Weavers LLP Surplus Rent	317	Interest Income Budget	6,648
Abbey Roding LLP Surplus Rent	358		
Abbey Road 2 Surplus Rental	506	Interest Received	5,058
Reside Management Costs	-316	Commercial Loans	3,851
Total Residential	1,590	Total Interest Income	8,908
Net Commercial Returns	1,029	Net Interest Costs	2,260
IAS Surplus (deficit)	(1,598)	Interest Surplus (deficit)	1,655
Overall Surplus (Deficit)	57		

3. Proposal and Issues

3.1. Funding the IAS (Proportionality)

Although the majority of the Council's investments are for regeneration and are within borough, an assessment of the Council's dependence on profit generating investments and borrowing capacity allocated to funding these, is considered against the lifecycle of the Medium-Term Financial Plan. A four-year net interest forecast has been established by the Council within the Medium-Term Finance Strategy (MTFS), which will support the Council's investments but also at times may act as a limiter to its investment activities. To ensure that the level of borrowing is sustainable, the Council will invest in schemes that provide a positive return after all costs and will also ensure that it invests in a number of different asset classes and assets with different cash flows requirements.

3.2. Additional Funding Requirement

By Minute 33 (18 September 2018), Cabinet agreed to enter into a joint development with Robyna Limited for a residential led scheme at London Road / North Street, Barking. As part of that decision, the Cabinet approved a loan of up to £35m to facilitate the development. The size of the development subsequently increased from 164 units to 196 units and it is proposed to increase the size of the loan to £44m to cover the cost of developing the additional units.

Further details of the funding arrangements for the increased loan are set out in Appendix 2, which is in the exempt section of the agenda as it contains commercially confidential information (relevant legislation: paragraph 3 of Part I of Schedule 12A of the Local Government Act 1972) and the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

Overall, the commercial loan portfolio in the revised IAS has reduced and this loan is currently the only one included in the strategy for 2020/21.

4 Investment Programme Changes 2019/20 to 2020/21

4.1 Be First is the Council's primary delivery agent for the delivery of the current programme and identification of new investments. The IAS relies on profitable schemes becoming operational as this is the main source of its income. Delays in schemes becoming operational has a negative impact on the IAS.

4.2 Table 2 summarises the current development programme. The increase in borrowing in 2019/20, mainly due to an increase in commercial purchases (Welbeck and Restore).

Table 2: Be First Business Plan Summary 2019/20 against actual

Year	Borrowing Forecast	Borrowing Actual	Difference
	£000s	£000s	£000
2019/20	79,794	119,183	39,389
Year	Units Forecast	Units Actual	Difference
2019/20	179	0	(179)

- 4.3 Currently schemes that were due to be operational in 2019/20 and 2020/21 have been delayed. Each scheme, when operational, provides a return to the Council through an interest contribution and also a net return to the IAS. Each delay impacts the IAS target and delays can impact a number of financial years.
- 4.4 Previously, interest incurred during the development stage was charged against the interest budget and any delay or increase in cost resulted in more borrowing costs being charged on schemes that are not earning income for the Council. As the Council will change its accounting policy on large scale developments to capitalise the interest costs, this has reduced the pressure on the interest budget but delays in schemes being built still impacts the IAs return. Table 3 outlines the extent of delays on schemes that were scheduled to be completed by July 2020. Four IAS schemes are due to be operational in 2020/21 delivering 261 units.

Table 3: Schemes by Operational Date at 2018/19 & 2019/20 IAS & Revised Date

Scheme	Units	2018/19 IAS Date	2019/20 IAS Date	Revised Date	Delay period
Weighbridge Modular	92	Jul-19	Nov-19	Jun-20	11 months
Wivenhoe Modular	20	Apr-19	Dec-19	Dec-20	21 months
Becontree Heath	87	Jul-19	Apr-20	Jul-20	12 months
A House for Artists	12	Oct-19	Sep-20	Aug-21	46 months
Sacred Heart	29	Jul-19	Sep-20	Sep-21	50 months
Becontree Avenue 200	19	Jan-20	Dec-20	Jul-21	18 months
Sebastian Court	41	Jul-20	Apr-21	Jul-21	12 months

- 4.5 In 2019/20 Be First started to report increases in build costs due to fire regulation requirements, but also a change in the type of tenure being built, with a decrease in properties that were going to be built to be sold for a profit. The impact of removing sales is to increase the long-term borrowing requirement from the Council but to also remove profit forecast from the sales, from the cashflow.
- 4.6 Table 4 shows the increase in gross borrowing costs for all schemes, excluding the proposed turnkey schemes. The accumulative borrowing requirement to fund the same schemes as outlined in the 2019/20 Be First Business Plan (BFBP) is £105m.

Table 4: Gross Borrowing Cost increase 2019/20 to 2020/21 BFBP

Year	2019/20 BFBP	2020/21 BFBP	Difference
	£'000s	£'000s	£'000s
2019/20	119,183(actual)	209,125	89,942
2020/21	367,413	422,429	55,016
2021/22	639,717	693,342	53,625
2022/23	809,215	930,307	121,092
2023/24	879,866	1,015,647	135,781
2024/25	952,198	1,052,802	100,604
2025/26	1,003,374	1,108,602	105,228
2026/27	1,054,713	1,160,090	105,378
2027/28	1,060,032	1,165,410	105,378

- 4.7 Table 5 shows the increase in net borrowing costs (after grants and sales), again on a like for like basis. The accumulative net borrowing requirement to fund the same schemes as in the 2019/20 BFBP is £319m, mainly due to the removal of sales.

Table 5: Net Borrowing Cost increase 2019/20 to 2020/21 BFBP

Year	2019/20 BFBP	2020/21 BFBP	Difference
	£'000s	£'000s	£'000s
2019/20	65,917	139,551	73,634
2020/21	241,596	296,480	54,884
2021/22	418,430	518,401	99,971
2022/23	465,760	666,433	200,673
2023/24	371,653	683,024	311,371
2024/25	388,314	700,411	312,097
2025/26	425,653	743,619	317,967
2026/27	460,652	780,040	319,388
2027/28	407,215	726,629	319,414

- 4.8 As at 31 March 2020 the council held long term borrowing still to be invested of £221m (at a rate of 1.97%), £105m in long term borrowing used to fund commercial investment that is scheduled to be repaid over the next three years, and short-term borrowing of £126m and which was sufficient to cover the 2019/20 BFBP and allow flexibility to make opportunistic borrowing decisions as they arose. The 2020/21 BFBP requires an additional £311m of long term borrowing to be sourced by 2023/24.
- 4.9 Delays in residential and commercial schemes completing has resulted in a shortfall in achieving the IAS return target. This improves in 2023/24 as a number of schemes become operational. If schemes, especially ones completing in the next couple of years, improve their net returns then this position could improve, but equally the impact of Covid-19 on rent collection and on delaying some schemes can have a negative impact. Table 7 provides a forecast for IAS income against the IAS target.

Table 7: IAS Income Forecast 2020/21 to 2027/28

Years	Target + £600k for Abbey	Pipeline Schemes	Operat- ional Schemes	Comm- ercial Income	Other Income	Total (shortfall) / Surplus	Accum- ulative
	£'000s	£'000s	£'000s	£'000s	£'000s	£'000s	£'000s
2020/21	(5,725)	388	1,797	800	900	(1,840)	(1,840)
2021/22	(5,725)	1,394	1,962	800	600	(969)	(2,809)
2022/23	(5,725)	1,472	2,174	800	150	(1,129)	(3,938)
2023/24	(5,725)	3,461	2,282	800	150	968	(2,970)
2024/25	(5,725)	4,767	1,357	800	150	1,349	(1,622)
2025/26	(5,725)	4,640	1,400	800	150	1,265	(357)
2026/27	(5,725)	4,986	1,460	800	150	1,671	1,314
2027/28	(5,725)	3,511	1,517	800	150	253	1,567
Total	(45,800)	24,618	13,949	6,400	2,400	1,567	

- 4.10 While the strategy has a reserve balance of £8m as a result of outperformance from treasury, surplus income from Abbey and the non-utilisation of a capital reserve, it is likely that some of this reserve may be required should the shortfalls forecast not be covered by other income. The reduction in borrowing costs due to the delays but also from the capitalisation of interest costs, will likely also improve this position.
- 4.11 Overall there has been a deterioration in the IAS return forecast, caused by delays and costs increases. The above analysis is only on schemes included in the BFBP 2019/20 and does not include pipeline schemes or Turnkey schemes. It also does not include income that may be secured from Film Studio or Welbeck all of which have the potential to improve the outturn.

4.12 Pipeline Schemes

To date most of the schemes are from the original 44 schemes, but there is a now significant pipeline of schemes that are being worked on by Be First that potentially need to be funded. Funding these schemes will require a significant direct investment by the council, through increased borrowing or indirectly by providing a guarantee on the rental income. Any funding agreements need to be considered against the current schemes and the future schemes. These schemes are summarised below:

Name	Operational Date	Gross Cost/Dev Cost £'000s	Units
Transport House, New Road	Jan-24	17,492	53
Brocklebank Lodge	Mar-24	19,316	56
Abbey Road	Aug-25	57,735	223
Marks Gate P3	Jul-27	63,087	187
Roding House	Mar-27	99,135	182
Padnall and Reynolds	Dec-26	146,599	389
Gascoigne East P3B 75%	Mar-26	113,322	299
Heath Park	Jan-26	113,918	314
Millard Terrace 75%	Mar-30	197,902	469
Gascoigne East Phase 4 75%	Mar-29	264,965	704
Beam Park	Feb-28	301,191	936
Ibscott 75%	Mar-32	323,624	724
Rest of West 75%	Mar-32	441,936	1,098
	Total	2,160,222	5,634

5. Additional Income and Tenure Mix

- 5.1 The analysis in section 4 shows a deterioration in the short-term IAS return from residential investment and an increase in net borrowing to achieve this return. Additional income streams to the IAS include current Reside schemes, commercial schemes, commercial loans and capital receipts. Some of these have the potential to significantly improve the financial position but can also put additional pressure on the strategy. The main additional income streams are outlined below:
- 5.2 Commercial Schemes provide an immediate return and cover the interest costs. For 2019/20, £1.0m of income was generated. There is potential for some of the schemes already purchased to provide a return to the Council, either directly through an allocation to the IAS or indirectly through a return from Be First or a capital receipt.

- 5.3 Commercial loans: Commercial loans provide a return to the Council and to Be First and help to progress some schemes. The proposed commercial loan portfolio has decreased but any deals will provide the IAS with some additional income.
- 5.4 Capital Receipts: Sales from Shared Ownership (i.e. Kingsbridge) result in a capital receipt. £3m was used to fund transformation, with £500k of profit allocated to the IAS in 2020/21, with a further £500k forecast for 2021/22.
- 5.5 Units and Tenure Mix: Changes in tenure for schemes over the past year have seen a decrease of 450 units from private sales and 141 units from SO, with an increase of 246 in affordable rent. Overall, the percentage of affordable housing provided has increased from 70.6% to 79% The comparison between 2019/20 and 2020/21 is outlined in table 7 below:

Table 7: Tenure split comparison 2019/20 to 2020/21 BFBP

	Private Sale	Private Rent	AR	LLR	LAR	SO	Other AR	Student Acc.	Total	% of Affordable Provided
2019/20	778	298	739	52	797	611	314	68	3,657	70.6%
2020/21	328	389	985	56	746	470	374	68	3,416	79.0%
Change	-450	91	246	4	-51	-141	60	0	-241	8.4%

6. Council's Balance Sheet Position

- 6.1 Below is a summary of a basic balance sheet analysis of what the Council is invested in and what it has borrowed. This analysis does not include grants, reserves, creditors, debtors, pensions or HRA but simplifies the position of the Councils current Investment assets against liabilities.
- 6.2 Over time the loans will increase but there should be a corresponding asset being built or being used. Of the debt, £172m has been spent on other assets that already have sufficient MRP being set aside and cover things from IT, Public Realm etc.
- 6.3 The IAS commercial development (£47m) and IAS residential development (£85m) are assets currently not earning income. While this will grow over the coming years, it is essential that these assets move as quickly as possible to Reside or are sold / developed. The large cash position has locked-in competitive rates to fund developments, with the cost of carry covered by ST debt positions and cash returns.

Liabilities £706m			Investments £817m			
£800m						
£750m						
£700m	ST Debt (£126m)	Average Rate 0.85% Average Duration 26 days	Cash (£350m)	Treasury Investment - overinvested to cover refinancing and cost of carry – Average rate of 1.34%		
£650m						
£600m						
£550m						
£500m	Other Debt (£116m)	Average Rate 2.75% Average Duration 30 yrs	IAS Residential Develop (£85m)	21 Investment Properties, some nearing completion		
£450m						
£400m	PWLB (£464m)	Average Rate 2.16% Average Duration 24 yrs	IAS Commercial Develop (£47m)	Film Studio		
£350m						
£300m			IAS Commercial (£59m)	Thames Rd, Welbeck		
£250m						
£200m			Capital Spend MRP (£172m)	Capital spend where direct MRP is charged		
£150m						
£100m						
£50m						
£0m					Company Loans (£33.8m)	LEUK, Be First etc
					Property Reside (£70m)	Abbey, Weavers etc

7 Leverage

- 7.1 Combining the increased borrowing required with lower returns, as outlined in section 4, the net impact is an overall reduction in the rate of return. It must be highlighted that investment returns can improve or worsen and that, for the IAS, returns can be negative if there are significant voids or rental increases are lower than forecast.
- 7.2 Returns are exaggerated through using increased leverage (using more borrowing to receive a similar return). As such, while increasing leverage may provide a £5.1m return for the IAS the risk associated with meeting the cashflow requirements but also in repaying the increased debt, increases.

- 7.3 Table 7 below shows the impact that an increase in borrowing (shown by rent roll), reflected in an increase in rental and borrowing costs, can have should the strategy experience a period of reduced rental income.

Table 7: Rental

Impact on return of a 10% and 20% reduction in return for £31m rent and £3m profit					
Change	Gross Rent	Lifecycle	MRP	Interest 3%	Profit/Loss
Current	31,000	(8,500)	(4,500)	(15,000)	3,000
10% rental reduction	27,900	(8,500)	(4,500)	(15,000)	(100)
20% rental reduction	24,800	(8,500)	(4,500)	(15,000)	(3,200)
Impact on return of a 10% and 20% reduction in return for £48m rent and £3m profit					
Change	Gross Rent	Lifecycle	MRP	Interest 3%	Profit/Loss
Current	48,000	(14,000)	(7,000)	(24,000)	3,000
10% rental reduction	43,200	(14,000)	(7,000)	(24,000)	(1,800)
20% rental reduction	38,400	(14,000)	(7,000)	(24,000)	(6,600)

- 7.4 The impact of increased leverage can also happen without borrowing. This is through lease and lease back arrangements or other options where the Council provides a return guarantee. This may not result in actual borrowing taking place but the effect is the same as leverage. I.e. the cashflows to the funder are guaranteed by the Council but there can be significant risks to the Council from reduced rent or increased management and lifecycle costs.
- 7.5 The impact of leverage can be increased further by using inflation linked returns, both to the lender, where the pressure is to make ever increasing payment to the lender and then modelled for the rental income, where there is pressure to continue to increase rents by the same rate. It is for this reason that the strategy has a preference for fixed rate on all borrowing instruments to fund investments with a significant amount of social housing.
- 7.6 If the trend outlined in section 3 continues, then it may still be possible for the Council to make its £5.1m return based on a set of model assumptions but the level of debt taken to achieve this will be significantly higher than originally considered. This increased leverage will mean that the strategy has less flexibility and margin to cover significant pressures, such as a reduced rents, voids or bad debts.

8. Consultation

- 8.1 The updated IAS was considered and endorsed by the Investment Panel on 22 September 2020.

9. Financial Implications

Implications completed by: Philip Gregory, Finance Director

Development period and long-term borrowing

- 9.1 Due to the scale and timing of the development programme the initial schemes will be funded by borrowing from the Public Works Loan Board (PWLb). As the scale of

development increases funding using institutional funders or bond issuance will be considered to limit the amount of development period exposure to the Council. This approach would allow the Council to limit funding to a defined development programme and to refinance schemes, subject to market conditions, when fully let and stabilised to release capital growth for reinvestment in other projects or elsewhere in the Council.

- 9.2 Bond rates are at historically low rates and the demand for long-dated, inflation linked returns remains strong from institutional investors

Medium Term Financial Strategy

- 9.3 The Council's balance sheet is currently £1bn in value. To fund the Investment Strategy, the Council will be heavily geared and the debt to asset ratio could be as high as 3:1 during the development period. This ratio will decrease as assets are built and let and are then included on the Council's balance sheet.
- 9.4 In line with the prudential code, the Council will need to demonstrate it can afford to carry the cost of borrowing to fund for both the construction period as well as the initial years before each of the schemes become cash flow positive. All borrowing will be profiled against the individual schemes, ensuring that the cash is available during the construction stage but that the repayment of the debt is included as the schemes generate income from rental and sales over the economic life of the asset. Borrowing will also be made over a period and will be dependent on the requirement but may also be made as and when rates are low.
- 9.5 The Investment Panel will review all schemes and investment proposals individually based on the Terms of Reference previously agreed by Cabinet.
- 9.6 Property acquisitions may be held on the Council's balance sheet or, where more financially advantageous, acquired through a Barking and Dagenham Reside SPV. Acquisitions will be supported by detailed legal and tax advice for each proposal.

10. Legal Implications

Implications completed by: Dr. Paul Feild Senior Governance Lawyer

- 10.1 The Local Government Act 2003 is the key legislation for local authority investment regulation and section 15 of the Act requires that the Secretary of State issues Statutory Guidance on investments the most recent being issued in April 2018. For each financial year, a local authority should prepare an investment Strategy and follow disclosures and reporting requirements specified in the guidance. The Secretary of State recommends that the Strategy should be presented for approval prior to the start of the financial year.
- 10.2 The Council has a wide range of powers concerning borrowing, investment and dealings with property which would empower the Council to pursue its Investment Strategy. Section 1 of the Localism Act 2011, the general power of competence ("GPC") empowers local authorities to do anything that an individual can lawfully do provided that the activity is not expressly prohibited by other legislation. Activities authorised by the GPC can include investment, trading or charging decisions which

may be undertaken through commercial (corporate) vehicles with the primary aim of benefiting the authority, its financial management, its area or its local communities.

- 10.3 Whilst the General Power of Competence will permit the Council to invest in property for a return, such activity is likely to be deemed as '*activity for a commercial purpose*' which cannot be undertaken directly by the authority and must be undertaken through a company structure within the meaning of section 1(1) of the Companies Act 2006 (s.4(2) Localism Act 2011).
- 10.4 Section 12 of the Local Government Act 2003 ("Power to Invest") enables a local authority to invest for any purpose relevant to its functions under any enactment, or for the purposes of the prudent management of its financial affairs. Speculative borrowing to invest purely for profit will not be deemed directly relevant to fulfilling the authority's functions and will not, therefore, be authorised under this power, however, investment in land or property, for example with a view to regeneration, and in line with CIPFA's Prudential Code for Capital Finance would enable the prudential investment of funds borrowed for the purpose of expenditure in the reasonably near future. The CIPFA Code contains detailed recommendations in the context of prudent borrowing practice, which should be considered as individual investment decisions are made. In exercising the power to invest under s.12(b) the Local Government Act 2003 the Council should have regard to the 2018 CLG Guidance on Local Government Investments. The Guidance advocates the preparation of an investment strategy which the Council is expected to follow in decision making unless sensible and cogent reasons exist for departing from it.
- 10.5 Section 1 of the Local Government Act 2003 ("Power to Borrow") provides local authorities with the power to borrow for any purpose relevant to their functions under any enactment or for the prudent management of its financial affairs. The Power to Borrow has similar constraints to the investment power under the 2003 Act. Borrowing primarily to achieve a return is unlikely to be deemed connected to the functions of the Council or prudent financial management. Caution should be exercised in making individual decisions to ensure that new investments financed with borrowing do further the functions of the Council and are consistent with prudent management of the Council's financial affairs.
- 10.6 Section 111 of the Local Government Act 1972 ("Incidental Power") enables a local authority to do anything (whether involving the expenditure, borrowing or lending of money) which is calculated to facilitate, or is conducive or incidental to, the discharge of any of their functions.
- 10.7 Investment and borrowing for the sole purpose of creating a return would not be deemed pursuant to the functions of the authority as required under the above powers. However, the report has clearly set out the primary objectives of the investment activity relate to shaping the strategic growth and economic development of the area to meet the needs of a growing local demographic and to shape local communities. Therefore, investment and borrowing in respect of property assets would be prudent and authorised pursuant to the authority's functions, when used as regeneration tools, alongside other financial measures, to provide a suitable diversified housing mix for the growing local population, to regenerate local areas and to create employment and education opportunities. It is critical that the primary policy objectives of any investment activity, such as building

new homes, regenerating an area or the creation of employment opportunities, are furthered and public funds are not exposed to unnecessary or unquantified risks.

- 10.8 Notably, many individual investment and acquisition decisions will be made in implementing the various strands of the Investment Strategy. Individual decisions will be taken by the Chief Operating Officer, advised by the Investment Panel, pursuant to delegated powers in respect of 'corporate and strategic finance, treasury management, investments, and the capital programme...' (Part 3, Chapter 1, paragraph 8.1(g) of the Constitution). To the extent that such decisions are key decisions, or urgent action is taken to acquire land (under paragraph 4, chapter 16, Part 2 of the Constitution) such decisions will be reported or notified to Cabinet in future reports. At all times, full consideration will be given to the Council's powers of investment and acquisition, any relevant guidance such as the CIPFA Code and the overall aims of this Investment Strategy.
- 10.9 The Council's Constitution, Part 4, Chapter 4 sets out the Land Acquisition and Disposal Rules. In accordance with paragraph 2.1, Part 2: Articles, Chapter 6 of the Constitution all key decisions and strategic decisions falling within the Land Acquisition and Disposal Rules as to the use, acquisition and disposal of land and property assets are generally within the remit of the Cabinet.
- 10.10 Formulation of strategic decisions is, at this time, overseen by the Property Advisory Group (PAG) and the Cabinet. Given the creation of the Investment Panel, to the extent that acquisition decisions are taken for investment purposes pursuant to the IAS, the Panel will advise and make recommendations as to such decisions either to COO (to the extent of the delegated powers available) or to Cabinet. Such investment driven acquisition decisions, depending on the value of assets to be acquired may also be key decisions which would be publicised on the Council's forward plan of the decision. Decisions on strategic acquisitions pursuant to the Investment Strategy / IPA would be made by Cabinet or COO, advised by the Investment Panel, in accordance with the Council's Constitution and its Land Acquisition and Disposal Rules and the Scheme of Delegation. For the sake of efficiency, Cabinet is expected to approve an investment programme on a rolling basis (as set out in Appendix 1) and to delegate any necessary authority to the COO, advised by the Investment Panel, to implement individual decisions in respect of individual schemes within the investment programme.

11. Other Implications

- 11.1 **Risk Management** - each potential investment and land acquisition opportunity will be subject to a full evaluation and risk analysis process as part of the IAS approvals process and scheme development Gateway review mechanism. This will be managed on behalf of Cabinet by the Investment Panel. The Investment Panel will be supported by external professional advisors
- 11.2 **Contractual Issues** - sites acquired in advance of planning permission being granted would be acquired under a Call Option arrangement or through outright purchase depending on the commercial evaluation and opportunity provided by each site. Each such proposed acquisition will be subject to the review process set out in Appendix 1.

- 11.3 **Staffing Issues** - additional staff may be required to implement and manage the anticipated level of investment and consequent investment portfolio. Any additional staffing costs would be funded from investment returns.
- 11.4 **Customer Impact** - the proposals in this report would help to achieve the Council's growth objectives and would help to achieve financial sustainability of the Council. In addition, the investment and regeneration programme facilitated by the IAS will underpin the creation of new communities within the borough and will increase housing choices and housing affordability. In turn, this will help to address fuel poverty and help improve household health and educational outcomes.
- 11.5 **Safeguarding Children** - purchase of land in advance of planning permission could potentially lead to the development of additional family housing which could improve help improve the life chances of children through a healthier environment and better domestic space in which to study.
- 11.6 **Health Issues** The provision of new housing has demonstrable health and wellbeing effects for occupants.
- 11.7 **Property / Asset Issues** - the proposals in this report will help the Council increase its affordable housing and income generating asset base. The proposals would also help to address physical and social obsolescence asset management challenges within the Council's existing property holdings and in the private sector

Public Background Papers Used in the Preparation of the Report: None

List of appendices:

- Appendix 1: Investment and Acquisition Strategy
- Appendix 2: London Road Additional Funding (exempt document)