From:	**Gary Cooke, Cabinet Member for Corporate and Democratic Services** **John Simmonds, Cabinet Member for Finance and Procurement** **Andy Wood, Corporate Director Finance and Procurement**
To:	**Policy and Resources Cabinet Committee**
Decision No:	14/00149
Subject:	**The Closure of Property Enterprise Funds 1 & 2 and the Future**
Key decision	**YES –** The properties transferred from the PEF Funds are valued at a total in excess of £1m. In addition the portfolios include properties from across the County of Kent.

Classification: Unrestricted

Future Pathway of Paper: Cabinet Member Decision

Electoral Division: ALL

Summary

The Council established two Property Enterprise Funds, PEF1 and PEF2. Both of which have been largely successful in achieving their original objectives. However given the changing circumstances over the years it is recommended that these are no longer appropriate in their current form. The report therefore recommends that the funds are closed with immediate effect and the assets held be placed in KCC's main Disposal Delivery Programme.

However, the report identifies a need to form a new fund with up to date terms of reference, governance and performance criteria that supports the aims of growing income from property and ensuring that KCC has a future disposal pipeline.

Recommendation

The Policy and Resources Cabinet Committee is asked to consider and endorse or comment on the proposed decision to be taken by the Cabinet Member for Corporate and Democratic Services in consultation with the Cabinet Member for Finance and Procurement to:

1. Approve the closure of Property Enterprise Fund 1 and Property Enterprise Fund 2 and for it to be progressed immediately.

2. Approve the release of assets currently held within the funds to be placed within KCC's main portfolio and where necessary into Kent's main disposals programme and for those capital receipts to be used to support the Council's capital programme.

3. Request the Director of Property and Infrastructure Support and the Corporate

Director of Finance and Procurement to finalise the arrangements for closing the funds.

4. Instruct the Director of Property and Infrastructure Support to consider a business case that supports a decision for a new Property Investment Fund. The objective of the fund being to implement a KCC investment portfolio to support an income return from property assets and grow the property asset base so that KCC has a future disposal pipeline.

1. Background

1.1 The Property Enterprise Funds, PEF1 and PEF2 were set up in 2006 and 2008 respectively.

1.2 PEF 1 was established to create a vehicle whereby the Council could invest in property particularly to enhance existing assets. The fund was also a receptacle for holding disposals which were not straight forward and required a more innovative approach in trying to extract value from them. An example of a PEF1 acquisition would be a purchase of access land to facilitate development and therefore increase value.

1.3 PEF2 was established to ensure continuation of the capital programme and take a longer term view of disposal whilst the property market recovered. PEF2 was successful in allowing the majority of the 2008 – 2011 capital programme to proceed, despite in excess of £100m of this programme having been predicated on capital receipt funding.

1.4 Prior to 2011, Directorates managed their own property portfolio and capital programmes where surplus assets were sold and receipts earmarked for particular schemes. All KCC assets are now the responsibility of the Corporate Landlord and are essentially centrally held. A few specialist / complex asset classes continue to be held within the Directorates pending their move to the centre which is scheduled to complete by March 2015 (with the exception of schools for the time being).

1.5 Capital receipts are now managed as a corporate resource since the introduction of the Corporate Landlord in 2012. Market conditions have also improved since the establishment of these funds. The PEF funds have served their purpose and, given the aforementioned changes, it seems an appropriate time to close these down and move forward.

2. Financial Implications

Summary Position – PEF1

2.1 PEF1 had an agreed overdraft limit of £10m.

2.2 The fund has made some strategic acquisitions, but over the years has also been used for alternative purposes which were considered appropriate at the time. The position on the fund as at 31.03.14 was an overall deficit position of £9.4m.

2.3 There are a number of assets which were originally badged as PEF1 yet to be sold which could return in excess of £15million when they are sold over the next 5 years. One of the key objectives of PEF1 was to tackle assets where value was difficult to extract and consequently progress has been slow or reliant on master planning etc. In addition these “high risk” sites were not attractive to bring forward during the recession years. These properties are already included within KCC’s disposals delivery programme, though presently the receipt is returned into the fund and not the capital programme.

2.4 On closure of the fund the proposal is to use these receipts against the forthcoming capital programme, and to ‘merge’ the remaining debt within our overall borrowing requirement. This proposal is already factored into KCC’s financing calculations and will therefore have no effect on the revenue or capital budget proposals.

Summary Position – PEF2

2.5 PEF 2 was established with the remit of being a not-for-profit making fund with an overdraft facility of £85m.

2.6 Over it’s life PEF2 had a total of 22 properties transferred into it, of which 16 have subsequently been sold. The overall position on the properties sold, taking into account all holding and disposal costs, is a slight profit of £1.8m.

2.7 The 6 properties that have not yet been sold have a holding balance to date of £8.5m, and have prudent forecast sale values of £5.4m. It is envisaged that once these are sold (taking into account further holding costs and changes in sales values) the overall position on the fund will be broadly break even.

2.8 In 2009-10 and 2010-11 a total of £9.9m was required for funding “PEF2 projects” in the Education capital programme, for which no suitable properties were found to transfer into the fund at that time. The funding of these projects has been factored into borrowing calculations as discussed below.

2.9 The impact of closing PEF2 has already been taken into account in the borrowing calculations for the forthcoming budget.

2.10 It is proposed that the receipts from the 6 remaining PEF2 properties are used as funding against the forthcoming capital programme, which has already been factored in.

Holding Cost

2.11 Where a temporary use until sale could not be found for assets within the funds, holding costs including security and maintenance were charged to the funds. Once the funds are closed, since there is no revenue budget following the assets, an additional pressure would be placed onto the Corporate Landlord Budget, which has no capacity to absorb such costs. Property and Infrastructure Support are discussing with Finance how this issue and the issue of funding these assets for disposal preparation might be overcome over the short and longer term.

3.0 The Future Position

3.1 When property becomes surplus, up until recently it was standard to apply a limited view on the statutory requirement for local authorities to dispose of assets it no longer had a use for. Consequently, if an operational asset became surplus, it would be sold and the capital receipt reinvested through the capital programme.

3.2 Prior to the Corporate Landlord, Directorates released many of their less complicated sites for disposal and earmarked receipts for reinvestment into their services. In addition, in spite of the Council's 30% portfolio reduction policy, because the "easy to vacate / sell" sites were sold, this target for vacating assets (based primarily on Council revenue saving targets) has been an ambitious one to achieve. Moreover, the Council has not been reinvesting part of its capital income in future disposable assets. Taking this to its logical conclusion KCC's disposal pipeline is likely to dry-up. A significant proportion of the capital programme is funded from capital receipts, this has been even more critical in recent years as we have sought to ensure that the borrowing levels remain within the thresholds set by the Council.

3.3 Whilst the original purpose of the PEF funds have been met and is no longer appropriate, a funding mechanism is necessary to provide: :

- Short term bridging finance to help consolidate the Estate and free up vacant space.
- Strategic purchases.
- Replenishing land for the future.

3.4 The reduction in Local Budgets in recent times has impacted significantly on the affordability of holding property. Part of KCC's response to this is to run property more along the lines of an investment model approach; it has become an ambition to make holding property assets less reliant on Council Revenue Budgets where a greater proportion is needed to ensure statutory services continue to run.

3.5 There are numerous advantages to investing in property and thus progressing an acquisition strategy, including:

- Maximising revenue income and minimising non-recoverable management costs to ensure the best return is generated

- Unlocking and/or influencing future development opportunities

- Promoting regeneration

- Promoting collaborative working and partnership with adjoining owners and developers with a view to maximising value/benefit.

- Supporting economic growth
- Supporting partnering arrangements
- Encouraging inward investment, re-location and business start-up in Kent
- Security; Short, medium and long-term revenue income
- Strategic value; Where a property has strategic value to the Council, some of the above criteria may be relaxed e.g. land capable of development or required to enable development.

3.6 In order to work within the property market, respond to opportunities and grow the investment portfolio, a draw down facility from a fund is required. How this can be drawn down, including a risk assessed business case, will need to be agreed which would then form the basis for the draw down governance arrangement.

3.7 A “Property Investment Fund” (PIF) is therefore proposed for an initial sum of £5m in the first 2 years with a review at the beginning of year 3. This would be part of the Capital Programme should it be approved.

3.8 This report recommends that a business case that supports a decision for a new PIF be brought forward. The primary objective of the fund would be to implement a KCC investment portfolio to support an income return from property assets and grow the property asset base so that KCC has a future disposal pipeline. It should consider governance arrangements, risk appetite, performance requirements etc.

4. Conclusions

4.1 PEF1 and PEF2 have been largely successful in achieving their original objectives. However given the changing circumstances over the years it is recommended that these are no longer appropriate in their current form.

4.2 The funds should therefore be closed and the assets held be placed in KCC’s main Disposal Delivery Programme.

4.3 However, there is a need for a new fund with up to date terms of reference, governance and performance criteria that supports the aims of growing income from property and ensuring that KCC has a future disposal pipeline.

Recommendation

The Policy and Resources Cabinet Committee are asked to consider and endorse or comment on the proposed decision to be taken by the Cabinet Member for Corporate and Democratic Services in consultation with The Cabinet Member for Finance and Procurement to:

1. Approve the closure of Property Enterprise Fund 1 and Property Enterprise Fund 2 and for it to be progressed immediately.

2. Approve the release of assets currently held within the funds to be placed within KCC's main portfolio and where necessary into Kent's main disposals programme and for those capital receipts to be used to support the Council's capital programme.

3. Request the Director of Property and Infrastructure Support and the Corporate Director of Finance and Procurement to finalise the arrangements for closing the funds.

4. Instruct the Director of Property and Infrastructure Support to consider a business case that supports a decision for a new Property Investment Fund. The objective of the fund being to implement a KCC investment portfolio to support an income return from property assets and grow the property asset base so that KCC has a future disposal pipeline.

7. Background Documents

None

8. Contact details

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