Meeting: Cabinet/Council Date: 9 and 18 July 2019

Wards Affected: All

Report Title: Proposal to increase the size of the Torbay Council Investment Fund

Is the decision a key decision? Yes

When does the decision need to be implemented? Immediately

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1. Proposal and Introduction

1.1 The report seeks to increase Torbay Councils investment fund to generate income to help meet the funding gap to provide local services.

2. Reason for Proposal

2.1 The current Medium Term Resource Plan (MTRP) highlights the financial challenges faced by the Council. It estimates that the Council will have to close an estimated funding gap of £18.3m over three years between 2020/21 and 2022/23 based upon existing service demands and “normal” budget pressures including inflation, demand pressures and income assumptions, however it is known that there are increasing cost pressures within Children’s Services which are likely to have further implications for the MTRP.

2.2 An investment fund has been in place for some 20 months, and its current authorisation is for £200m. The purpose of this investment fund is to generate income which can then be used to help fund local services.

2.3 Since the creation of the fund approximately £186m has been committed to acquire a diverse range of investments in a range of different sectors and locations. After the loan repayments and after a contingencies allowance have been made, these investments have generated £2.9m of additional revenue in 18/19, rising to £3.3m in 19/20. Once all of the current commitments are complete and assuming a full year’s income, the fund will generate over £3.5m per annum revenue for the Council to allocate towards local services.

2.4 The proposal is to increase the fund further to £300m. At this level it is projected that this would generate an additional £1.5m of income per annum assuming a

1.5% net return after costs and capital. Eventually this would take the total income from the fund to £5m per annum to help deliver local services. Based on current market conditions it is anticipated that it will take an additional 12-18 months to commit all of the proposed additional £100m.

2.5 The current strong due diligence requirements will remain as outlined in the Investment and Regeneration Strategy along with the change for approvals to be by Cabinet not a specific Committee of the Council.

2.6 The current investment boundary of the Local enterprise partnership footprint, is restrictive and limits the investment opportunities available to the Council. As such it is recommended that the boundary be increased to include the wider economic area.

2.7 The Council will continue to have “regard” to any Statutory Guidance issued by the Minister for Housing Communities and Local Government (MHCLG) that is relevant to the purchase of these properties and any resulting Minimum Revenue Provision.

3. Recommendation(s) / Proposed Decision

That Cabinet recommends to the Council:

3.1 That Council authorise £100m of additional prudential borrowing to enable the Investment and Regeneration Fund to increase to £300m.

3.2 That Council set the investment boundary to the Greater South West peninsula or the Functional Economic Market Area (FEMA), and instruct the Monitoring Officer to make the necessary amendments to the Investment and Regeneration Strategy Policy Framework document.

Appendices

Appendix 1: The Economic interdependency between areas

Background Documents

None included

Section 1: Background Information	
1.	**What is the proposal / issue?** This report proposes that Torbay Council increases the investment fund to £300m to provide additional income to help meet the budget deficit facing the Council, which also provides greater resilience to the fund by increasing its size. Increasing the fund to £300m could deliver an additional £1.5m of income per annum taking the total projected income from the increased fund to £5m p.a.
2.	**What is the current situation?** The investment fund is currently limited to £200m of which £186m has already been committed. With other proposals in the pipeline it is expected that the balance of the fund will be committed by the end of August 2019. Once the fund is fully committed and a full year's income is received then it will provide over £3.5m in revenue for the Council and local services. The Council faces a minimum predicted funding gap of £18.3m over the next 3 years and while a number of measures are being taken to address this, additional income from an increased fund would go some way to help resolve this. Currently the investment portfolio is fully let and a number of investments will see their income increase over the coming years due to specific rent increase clauses in their leases. The predicted rent increases and therefore how the additional financial benefit also increases is carefully monitored. It should also be noted that the borrowing for the fund is based on a full repayment model (on an annuity basis over the asset life up to a maximum of 50 years) and therefore once the loans are repaid the income will increase substantially, and in the meantime it is expected that the capital value of the asset will appreciate. As with all investments there are risks although if the fund is increased then the same level of scrutiny and due diligence will take place to ensure that any risks are identified, mitigated against or quantified. The current investment boundary of the Local enterprise partnership footprint, is restrictive and limits the investment opportunities available to the Council. As such it is recommended that the boundary be increased to include the wider economic area. Economic geography is recognised as complicated. People live, work and undertake leisure activities across a wide geographic area and across

	different administrative areas i.e. they might live in one area, work in another but principally shop or spend their leisure time in a third or fourth. While for the business community that geographic diversity is broader with functional geographies for businesses that export being genuinely global. Research carried out by SQW in 2010 on functional economic market areas recognised that there is no universally agreed approach to defining Functional Economic Market Areas (FEMAs) and no definitive map or criteria. What is generally accepted is that FEMAs are shaped by a variety of themes that influence economic development which include housing markets, commercial property market areas, commuting patterns, retail catchment, business areas of operation, transport networks and journey times and economic governance & partnership areas (Lichfields). Torbay is part of a layered economy which includes the very local but there is clear evidence that patterns of commuting, in and outbound, from Torbay extend over a wide geography with people travelling to and from Torbay across the South West including the north Somerset and Bristol M5/M4 corridor for work. Under the economic governance and partnership area factor noted above the role of partnerships including Local Enterprise Partnerships is important in helping determine the area. • Torbay is part of the Heart of the South West spanning Devon & Somerset. • Heart of the South West LEP is itself part of a wider group, Great South West, which recognises the interdependence of different geographies including Dorset, Cornwall and Heart of the South West and aligns those areas because of the shared assets, infrastructure and opportunities across that area. • The South West region, including Wiltshire and Gloucestershire, continues to be a recognised designation by Government which reflects the connectivity and relationships across that area. To help inform this position advice was sought from the Councils external auditors on extending the investment boundary and their response was: *‘We have considered your proposed approach for investments properties, which has defined a Functional Economic Market Area (FEMA) using inflows and outflows of labour in Torbay based on 2011 census data. We have noted that the economic note issued by CLG (as it was then) in 2010 on Functional Economic Market Areas comments that the most widely accepted approach to identifying FEMAs is by reference to Travel to Work Areas (TTWAs), but also states that there is no universal approach to defining FEMAs and that there is an argument for analysing census commuting and migration data. We are therefore not minded to challenge this approach, however this is a fast-moving landscape and we therefore reserve the right to come to a different view based on any formal challenge or any emerging interpretations elsewhere.’*

3.	**What options have been considered?** Leave the fund at current level of £200m. Increase the fund but at a lower level than is being recommended. This would see the risk and reward reduce proportionally. Increase the fund to a higher level than is being recommended. This would see the risk and reward increase proportionally.
4.	**How does this proposal support the ambitions, principles and delivery of the Corporate Plan?** A prosperous and healthy Torbay **Principles**: • Using reducing resources to best effect • Integrated and joined up approach **Targeted actions**: • Protecting all children and giving them the best start in life • Working towards a more prosperous Torbay • Promoting healthy lifestyles across Torbay • Ensuring Torbay remains an attractive and safe place to live and visit • Protecting and supporting vulnerable adults
5.	**Who will be affected by this proposal and who do you need to consult with?** All wards will be affected by this proposal as the income delivered will fund services all across Torbay. The Councils Finance department are a key consultee on this issue to ensure that the Councils actions are prudent and at a sustainable level.
6.	**How will you propose to consult?** The proposal has been debated and discussed at an Officer level, has previously been discussed with the Investment and Regeneration Committee when it was in existence and has been discussed with the Cabinet. The report has been circulated to all of the required departments within the Council for specific comment and those comments have been incorporated into the report/

Section 2: Implications and Impact Assessment	
7.	**What are the financial and legal implications?** Section 120 Local Government Act 1972 permits a Council to acquire by agreement any land, whether situated inside or outside of their area, where it is for the benefit, improvement or development of their area. Case law demonstrates that property acquired solely for investment purposes is not sufficient to demonstrate compliance in this respect, and the Council's approved Investment and Regeneration Strategy therefore requires any acquisition to deliver multiple benefits. The Strategy recognises that the demand for Council services can be reduced by delivering economic growth, tackling inequality and creating change in the area. The financial implication of this recommendation is significant and when making the decision the total borrowing commitments of the Council should be considered. The risks and rewards of a significant level of borrowing are outlined in the Capital Strategy that was approved by Council in February 2019. It is recommended that members review this document and the impact of an increase of this level on the Council's total borrowing position, whether the level of borrowing is proportionate and is affordable and understand the potential risks and rewards of purchasing properties. It should also be noted that the Council owns over 600 assets locally on which there are no loan charges. As such if you were to spread the total investment fund over all of the assets the Loan to Value level would be significantly reduced. As of the end of 2018 those assets were valued at £235m. All investments are dealt with on a full repayment basis (on an annuity basis over the asset life up to a maximum of 50 years) which certainly reduces the risk to the Council, which will further diminish over time as the loans are repaid. The borrowing associated with these assets will comply with the Prudential Code of Practice 2017 which states: "..the responsibility for decision making and ongoing monitoring in respect of capital expenditure, investment and borrowing, including prudential indicators, remains with full Council". The management of these assets will comply with the Treasury Management Code of Practice 2017 which includes these assets as "Non Treasury Investments". There continues to be a level of comment from central government and public sector bodies such as CIPFA over the increased level of commercial activities in Councils and the resulting higher risks. As a result MHCLG issued Statutory Guidance in 2018 on both Investments and Minimum Revenue Provision. The

	National Audit Office is currently undertaking a review of Councils' commercial activities and will report later this year. This may result in further clarification or restriction around Councils 'borrowing. The Council will continue to "have regard" to any Statutory Guidance issued by the MHCLG relevant to these Investments in particular to ensure that each investment has a multiple objective: Statutory Guidance on Investments is as follows: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/678866/Guidance_on_local_government_investments.pdf A clarification document of the changes in the Statutory Guidance is as follows: https://www.gov.uk/government/consultations/proposed-changes-to-the-prudential-framework-of-capital-finance/prudential-framework-of-capital-finance-qa The MHCLG clarification document states: "…..we are proposing that all local authorities disclose the contribution that each investment makes towards the core objectives of the local authority. The proposals also make it clear that borrowing solely to fund yield generating investments is borrowing in advance of need. Local authorities will be able to borrow to fund investments that have multiple objectives, including generating yield. The positive financial implications are that the income achieved from the increased fund will make a considerable contribution towards the budget deficit.
8.	**What are the risks?** All investment carries a degree of risk. What is important is that appropriate processes and procedures are in place to ensure that these are identified as part of the decision process and then are further investigated and mitigated against through a robust due diligence process. It is also worth noting that information obtained as part of this due diligence process has seen the Council withdraw from three separate approved investments since the fund was created. Robust information supported from a variety of surveys and experts ensures that decisions are well informed. Furthermore the Council always seeks an independent view on the value and quality of the investment prior to proceeding. In terms on obtaining the right number and quality of investments, if the fund were to be increased then the most prominent risk associated with this is the potential rise in interest rates and the potential rise in investment prices. This risk is mitigated against in that each investment is considered on its own merits and if

	the right balance of risk and reward is not there then the Cabinet would not proceed.
9.	**Public Services Value (Social Value) Act 2012** Not applicable.
10.	**What evidence / data / research have you gathered in relation to this proposal?** Medium Term Financial Plan Data and information from within the Investment Dashboard.
11.	**What are key findings from the consultation you have carried out?** The robust process that has happened to date should continue with Cabinet and that the quality of investments should not be compromised as a result of the reduced boundary. On this basis the fund should be increased.
12.	**Amendments to Proposal / Mitigating Actions** n/a