Property Portfolio Strategy

Draft Report version 1

4 Feb 2024

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1. Introduction

1.1 Scope and Approach

Avison Young Strategic Advisory have been commissioned by the London Borough of Brent (LBB) to provide Consultancy Services in support of development of a Property Strategy to cover the 'commercial' properties owned by the Council and let to third parties for a range of purposes. This portfolio is summarised in Annex A. The scope of this limited exercise was set out in the Engagement Letter dated 13th July 2023 ('230712AY LBB Engagement Letter').

The aim of the exercise is to provide a strategic framework for investment, divestment and management decisions impacting on financial sustainability, opportunities to deliver social value and maximising rent over the next 5 years. Implementing a step-change in social and financial benefits requires efficient systems, processes and capabilities. This strategy also makes recommendations on the property management arrangements required to implement the strategy.

The approach adopted has consultation at its centre and has sought the views of a representative cross-section of council stakeholders, namely Members, service directorates and central functions. This reflects the role of the property portfolio in realising community, economic development, service delivery and financial benefits. The approach has comprised:

- Structured interviews (August 2023) with:
  - Councillor Muhammed Butt, Leader of the Council
  - Minesh Patel, Corporate Director for Finance & Resources
  - Tanveer Ghani, Director – Property and Assets
  - Alice Lester MBE FRTPI, Director, Regeneration, Growth & Employment
  - Lorna Hughes, Director - Communities and Strategy
- Workshops:
  - Policy & Coordination Group September 2023
  - Senior Leadership Team (SLT) November 2023

The report uses the output of this engagement and leading practice to identify the Council's challenges and opportunities and to make recommendations for performance improvement. The aim has been to ensure the Council is maximising its returns by way of social value, income and cost recovery.

1.2 Objectives of Engagement

The property strategy will enable LBB to develop detailed implementation plans for each property (e.g. including capital maintenance, regears, improving covenant strength, change of use, disposals).

1.3 Sector guidance

The strategy is prepared in the context of RICS guidance on Strategic Public Sector Property Asset Management (3rd Edition). It defines strategic asset management as:

"the activity of aligning property assets with the strategic aims and direction of the organisation and adding both financial and non-financial value to the organisation as a result."

This strategy also draws on the Council's Borough Plan 2023-27 (published February 2023) and the CIPFA guidance Strategic Property Management Framework 2018. This framework lists the benefits of strategic property asset management as:

- Being corporate
- Raising awareness of the importance of property
- Improving service delivery
- Improving financial outcomes and efficiency
- Delivering corporate objectives.

The approach to preparing this strategy (see paragraph 1.1) and its objectives reflect the CIPFA objectives.

2. Strategic context

2.1 Background

LBB's last Property Strategy was for the period 2015-19. Major changes since include:

– Exit of the UK from the European Union (EU – "EU Exit" / "Brexit")

– Global Pandemic

– Geopolitical challenges (War in Ukraine and now Middle East), leading to rapid rises in inflation and interest rates globally – "Cost of Living Crisis"

– Continued and worsening budget constraints at national level (rising cost of National Debt)

– Accelerating net immigration into the UK, particularly from non-EU countries.

These factors have manifested themselves in a number of profound and ongoing changes to demographics, ways of working, market practice, portfolio financial performance and the needs of residents.

The Council's Borough Plan 2023-27 sets out 5 five priority areas:

– Prosperity and Stability in Brent

– A Cleaner, Greener Future

– Thriving Communities

– The Best Start in Life

– A Healthier Brent.

The property portfolio seeks to support the Borough Plan, through providing spaces for communities to meet, facilities from which community activities and services are delivered, as well as workplaces, shops and potential land for housing.

2.2 The importance of the portfolio

The size and shape of the portfolio is outlined in Section 3 (and **Annex A**). The portfolio of circa 100 properties is considered by consultees to be a key Council asset, providing a mix of social, community, economic and financial benefits including:

– Space for the voluntary and community sector (VCS)[1] including socially-trading organisations to provide services that support community well-being, health, employment, safety, stability and prosperity

– Commercial space to support employment and economic activities

– A source of revenue that helps fund council activities in a time of financial scarcity

– Support to core services such as leisure and parks.

– Properties that are part of the heritage and built environment which define the places in which communities live and work

– Land with potential for housing and regeneration.

[1] Also commonly referred to as Third Sector Organisations (TSOs)

2.3 Vision

A vision for the portfolio and its management has been developed through the stakeholder interviews and tested at the workshop with members and senior officers:

*"Our vision is to create a **sustainable**, **compliant** and **diverse** property portfolio which contributes to creating **thriving communities,** enhancing the local economy and improving prosperity."*

The vision is aligned to the Council's priority areas, the Borough Plan and reflects the important role provided by the portfolio.

Retention of the portfolio was challenged during the strategic exercise; a strong policy steer was provided that in general the portfolio should be retained, as opposed to disposal and reinvestment in an alternative asset class, due to the social benefits referred to above. However, this does not prevent churn of the portfolio i.e. judicious acquisitions and disposals which better meet the Borough's needs and Council's priorities, particularly to align with the Council's ambition to make *"Brent a carbon neutral area by 2030"*[2].

2.4 Trends and change drivers

The following trends across the property industry have potential impacts on the strategy and management of the Council's portfolio.

Change driver	Change	LBB Portfolio Impact
Workstyles – hybrid working practices	– Lower demand for office workspace. – Increased demand for "Grade A" / high spec offices in central locations that offer a mixed work, hospitality, leisure, retail experience.	– The trend is not translating into higher demand for space in satellite locations as commentators once predicted. – Longer letting times and lower rental levels for office properties in the portfolio. – Requirement of tenants for greater rent-free periods at the start of leases, prolonging the impact of new leases.
Environmental – net zero	– The Council has set an ambition for "*to be a carbon neutral council by 2030*", and explicitly to "*lead by example by retrofitting and reducing energy usage across our estate and operations*"[3]. – The Minimum Energy Efficiency Standards (MEES) make it illegal, with effect from 1st April 2023, for a landlord to let (or continue to let) any "substandard" property with an Energy Performance Certificate (EPC) rating of less than E. – In time it is likely to become illegal to let any properties rated at less than D or C, and by 2030, less than B. See **Annex C.** – 'Green' building are commanding premium returns in the market.	– LBB portfolio will become obsolete if it fails to invest in retrofits, including renewable energy heat and power sources. – Returns on buildings with low environmental performance are likely to soften in the future.

[2] "Brent is a carbon neutral area by 2030": Brent Borough Plan 2023-27
[3] Brent Borough Plan 2023-27

Change driver	Change	LBB Portfolio Impact
Environmental – circular economy	– Meeting sustainability objectives is weighting the decision to redevelop or renew towards reconfiguring and repurposing existing assets.	– More focus on repurposing and refurbishing existing assets than redevelopment in the future.
Whole life asset management	– The Cabinet Office / Office of Government Property has highlighted the importance of keeping buildings in a good standard of condition and investing in lifecycle replacement. It draws attention to the personal consequences to officers of non-compliance with statutory health and safety regulations, the increased costs of deferring maintenance and the impact on operations.	– Lifecycle replacement works to the portfolio cannot be deferred indefinitely and under-maintenance creates significant reputational and financial risk. – Moreover, the ability to let a commercial property quickly and achieve best returns depends on condition, statutory compliance and increasingly environmental performance.
Technology	– Advancements in technology and data analytics such as artificial intelligence, sensor technologies, the Internet of Things (IoT), building information modelling (BIM), Case Management Systems (CMS) and digital twins create new expectations from tenants and opportunities for owners to improve asset management performance.	– Increasing tenant expectations for digital buildings will erode rental growth and returns from legacy stock for property owners in general. The private sector is realising opportunities for more efficient management of the portfolio e.g. from robotic technologies that read and manage leases, to real-time data on occupancy, incidents and maintenance – At a minimum, the Council will need to prioritise efficient buildings, which are well-maintained and cost effective to run, with strong internet connectivity.
Retail	– The long-term move to online retail shows signs of abating. Retail rents have declined before, during and since the pandemic, but the scale of the declines has eased over the last 12 months. – There is a trend towards new in-store technology that enhances this customer experience – such as self-service checkouts. – Vacancy rates and rents will continue to be challenged as working from home and online shopping combine.	– Retail spaces provide important test beds for local businesses to take their first steps into commercial spaces. – “Meanwhile Uses” continue to be an important cornerstone to any long-term regeneration strategy, and the Council’s approach will continue to be relevant. Where possible, the duration of “meanwhile use” should be limited due to the minimal/ zero rent it brings. – The retail properties held by the Council are unlikely to see significant rental growth in the medium term.

2.5 Problem statement

Given the context of scarce resources, deteriorating condition of some assets (especially long-term voids), environmental obsolescence, market conditions and competing pressures on the Council's budgets, the Council must better balance:

– Meeting community expectations and creating social benefit;

– Financial return; and

– A well-maintained and environmentally future-proofed portfolio, that is statutorily compliant.

The strategy needs to provide a direction and framework to resolve these tensions, which are products of the strategic context in 2024. Section 5 highlights why changes to the management of the portfolio are imperative and no change is not an option.

3. Current portfolio

3.1 Composition of Portfolio

The in-scope portfolio is a complex mix of property types, sizes and tenants. It comprises a significant number of legacy service properties (often former operational buildings). The majority of properties are occupied by VCS organisations, community groups with little income and small local businesses. The portfolio is emotive to many stakeholders and challenging to manage, given the tensions between maximising support for Brent's communities and the legal and financial realities of managing property assets. It is summarised below and in **Annex A**[4].

Source: London Borough of Brent (LBB) Property & Assets Team dataset, Avison Young Analysis

The majority (59%) of the properties are defined as 'community use', with:

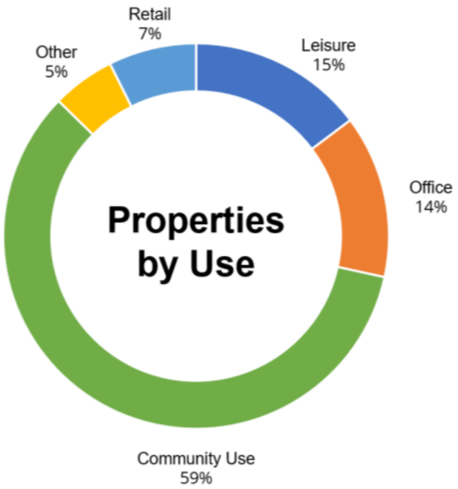
– The next largest asset group is Leisure making up 15%.

[4] The analysis in Annex A is based on data provided in August-September 2023. Subsequent work by the Council's in-house Property & Assets Team has improved the completeness and accuracy of the data held, and increased the number from 95 to 106

– Offices make up 14% and Retail 7% (excluding Cafés).

– We have classified the remainder of the portfolio (c 5%) as 'Other':

- Other properties include builders' yards, education, open storage land and others.



Source: London Borough of Brent (LBB) Property & Assets Team dataset, Avison Young Analysis

A more detailed breakdown of floor area, rent and value (for insurance purposes) is set out in the table below. It shows the significance of the 12 office buildings in terms of floor area and finances, and in particular the Civic Centre.

Use	Units	sq m	Total Rent p/a	Insurance (Total)[5]
Community Use	54	19,110	£528,081	£77,887,000
Leisure	12	10,347	£216,851	£34,226,000
Office[6]	12	33,568	£1,448,382	£179,778,000
Retail (incl. Café)	14	3,462	£47,410	£7,991,000
Other	8	2,205	£83,248	£5,127,000
Veolia contract	6	1,097	£-	£4,157,000
Total:	**106**	**69,788**	**£2,323,972**	**£309,166,000**

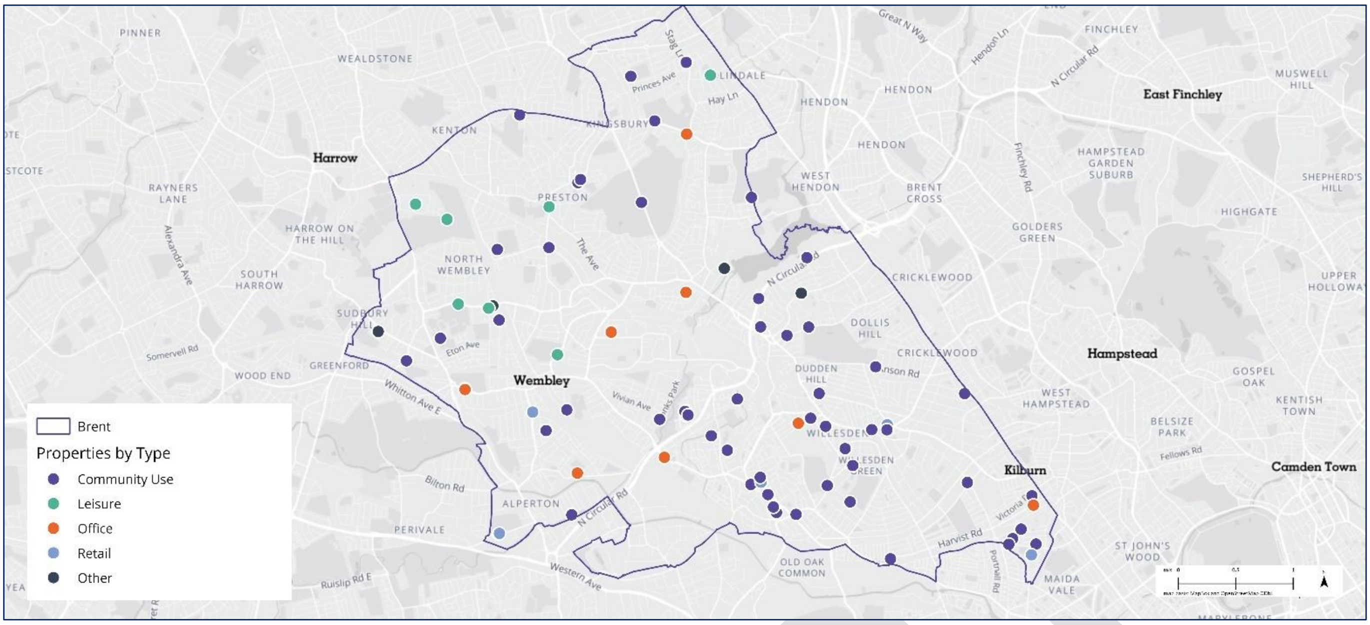
Civic Centre	Office	26,336	£992,288	£136,390,000
Total excl. Civic Centre:	**105**	**43,452**	**£1,331,684**	**£172,776,000**

Source: London Borough of Brent (LBB) Property & Assets Team summary, 'Commercial Properties Status - Rental and Insurance (2), received 19/12/2023

The portfolio is dominated by the Civic Centre in Wembley Park, which comprises almost 40% of the floor space and provides over 60% of the receivable income.

The assets are dispersed around the Borough – future research could explore how well these are aligned to current and future demographics, and market / regeneration opportunities:

[5] NB: Reinstatement Value = estimated Cost of Rebuilding. Open Market Value of the property may be considerably different
[6] Office includes Civic Centre in Wembley Park – see separate row



Source: London Borough of Brent (LBB) Property & Assets Team summary and Avison Young mapping

3.2 Data and Issues

Analysis of the portfolio is produced using the existing and available data. In summary:

– The datasets provided reflect information held in multiple legacy sources. There are therefore a number of variations in these datasets, which makes analysis and reporting challenging.

– The variations in dataset highlights one of the most significant issues for the management of the portfolio, which is the lack of a single comprehensive property asset management system or appropriate Case Management System (CMS).

– The Council's Property & Assets Team has been and is trying to work around this, however it is impossible to ensure consistency of data / analysis without a proper real estate asset management system to:

- "seamlessly link day-to-day asset management tasks with facilities management, project management of works, space management and associated financial management", and

- "*manage, among other things, the life cycle of assets and asset management risks*" [7].

– There are apparent gaps in condition and environmental performance data, which would be costly to obtain - for example:

- Whilst information on individual sites (for example, Energy Performance Certificates – EPCs) can be obtained on a site-by-site basis, it is not possible to record and analyse these on a portfolio level;

- Whilst quinquennial site visits are undertaken (to inspect condition of occupied properties), and occasional *ad hoc* surveys are undertaken (for example, a desktop RAAC review by an independent Chartered Surveyor has been completed recently), the evidence from such regular and *ad hoc* exercises would be much valuable if recorded on a system and readily accessible; and

- Whilst it is understood that significant elements of the estate are aged, ageing, in poor condition and need significant improvement to reach the Council's aspiration "*to be a carbon neutral council*

[7] Source: RICS 3rd Edition Guidance on Strategic Public Sector Property Asset Management – per e.g. ISO 55001 / ISO 55002

by 2030"[8], again evidence on what the issues are and which properties are affected would be more useful if it was stored in such a way it can be easily viewed and analysed.

– Similarly, whilst the Council's Property & Assets Team is managing the portfolio as well as can be expected, better systems, data and processes would enable much easier forecasting, analysis and proactive management of future voids and other material risks & liabilities, such as obsolescence.

  - Buildings are "wasting assets" – they need to be actively managed and maintained if they are to retain value and utility.

  - A lack of investment in the property assets themselves will result in declining rental income and increased risks and liabilities. Some properties have been vacant for considerable periods because they are unlettable in their current condition.

  - Better information, systems and resources would enable the Property & Assets Team to better forecast, model and manage both current and future risks and liabilities, and optimise the portfolio for the benefit of the community.

– The dataset indicates some 20 assets with nil rents, suggesting circa 15,000 sq m or so of void / unrented space, with a potential rental value estimated at up to c £61k to £100k p.a (but subject to investment into remedial works). There are also about 7 unregulated tenancies where no rent is being charged, and these are currently in the process of being regularised and could generate additional income of £26k p.a. once regularised by lease.

In summary, improved systems and resources would enable the Council's Property & Assets Team to better manage these assets, maximise their value, secure additional income streams and contribution to the local community and minimise the risks of exposure to unknown liabilities.

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3.3 Rental Performance – Wilks Head & Eve estimations

- There is an opportunity within the portfolio to increase the rental income. This could lead to a loss of social benefit, attendant with reducing space occupied by the VCS sector on discounted rents.
- There are likely to be issues around the lettability of individual properties and actual rents achievable.
- Rents can only be increased in line with existing terms (such as CPI uplifts) or at lease renewal which will occur at different times for different leases.

An accurate estimate of the total rental discounts provided to the VCS sector is outside the scope of this exercise but is reflected in the potential to uplift rental income to market rates.

3.4 Additional (theoretical) income opportunities and subject to all rents moving to full market rents

This information is included in 'Appendix 2 - Additional Income and Top Development Opportunities' due to containing the following category of exempt information as specified in Paragraph 3, Schedule 12A of the Local Government Act 1972, namely:

"Information relating to the financial or business affairs of any particular person (including the authority holding that information)".

3.5 Top Development Opportunities

This information is included in 'Appendix 2 - Additional Income and Top Development Opportunities' due to containing the following category of exempt information as specified in Paragraph 3, Schedule 12A of the Local Government Act 1972, namely:

"Information relating to the financial or business affairs of any particular person (including the authority holding that information)".

4. Issues and challenges

4.1 Voice of the stakeholder

The foundation of this strategy is consultation with the communities, elected members and their senior officers. This collaborative approach to asset strategy has highlighted a diversity of voices and views, in keeping with the multitude of outcomes that the portfolio supports.

A number of themes emerge from the consultation, supported by the property data:

– **Financial sustainability** – the estate in its current shape is unaffordable and needs to be reconfigured to arrest a negative circle of decline. Without being put on a financially sustainable footing, the benefits of the portfolio to residents will diminish and policy ambitions such as "carbon neutral by 2030" will be unachievable.

– **Policy refresh** – policies need to be updated and developed to ensure best value decision-making, and this need to be enabled by a highly performing asset management function that has the systems and resource to provide the requisite data and decision-support.

– **Unremitting focus on residents** – changes to policy, processes and properties need to add value to residents and be transparent and fair.

– **Obligations of tenants** – maximising benefit from the portfolio requires a policy shift that strengthens the obligation on tenants to demonstrate social benefit.

4.2 Summary of consultation

Headline phrases are summarised below:

Avison Young and the Property & Assets team have analysed all the inputs and feedback from the structured interviews and workshops, and these have in particular informed the "Issues / Challenges" and "Opportunities" summaries herein, and hence our recommendations:

– A word cloud of feedback from the first workshop summarises some of the keywords raised:

– Copies of the Case Study feedback forms from the Second Workshop are attached to **Annex C**.

4.3 Issues

The following summary of the challenges faced by the Council in achieving its vision for the portfolio are drawn from the portfolio data, interviews, workshops and documentation review. They are challenges faced by councils across the country and all are addressable (see Section 4).

Area	Issue
Governance	– Lack of clarity, evidence and transparency in decision-making, including allocation of space to tenants, rent setting prioritisation of capital. – Decision-making process is not always supported by sufficient data availability. – Challenging to balance competing priorities and weigh Social Value Added / outcomes.
Financial	– Portfolio is unaffordable. – Significant uncollected rent (arrears @ £1.5M) since the start of the pandemic[9], voids / void risks, rents at a discount leading to value leakage. – Inadequate resources to maintain and upgrade portfolio (obsolescence), leading to impairment of future income streams.
Asset Strategy	– Unclear plan for which assets to retain, invest in and dispose of. – Unclear process to prioritise resource. – Risk of non-compliance with health and safety and building regulations; liabilities are unbudgeted.

[9] Rent collection, prior to the pandemic was c.98%.

Area	Issue
	– Risks around expensive, risky, management-intensive assets in portfolio, which absorb management time and scarce resources but provide little return and high liabilities.
Policy and process	– Limited processes for allocating space to tenants or granting rental discounts, leading to issues of fairness and potentially disadvantaging some third sector groups. – Ad hoc, inconsistent treatment of VCS tenants.
Supporting regeneration	– Risk of divergence / "missed opportunities" if regeneration strategy and property portfolio strategy are not well integrated, given role of property in catalysing economic development. – Unclear how well assets are offered to / shared with start-up / seed businesses.
Data & Systems	– There is not a single integrated system –clear MI is required. – accuracy/completeness can be improved. – Significant data gaps e.g. condition, energy performance. – Compliance data gaps (e.g. H&S, RAAC). – Inefficient invoicing system - 1 FTE dedicated per month to raising rental invoices each quarter. • *Costs an estimated £250 to produce an invoice across Council*" - so not worth it for small amounts of money.
Sustainability	– No pathway to fund and reach Net Zero – Gaps in EPC and environmental performance data • The Minimum Energy Efficiency Standards (MEES) make it illegal, with effect from 1st April 2023, for a landlord to let (or continue to let) any "substandard" property with an Energy Performance Certificate (EPC) rating of less than E, and it is likely to become illegal "in time" to let any properties rated at less than D or C, and by 2030, less than B. See Annex B. • It is an offence for a landlord to fail to provide an EPC to any prospective buyer or tenant – the Council could be fined between £500 and £5,000 based on the Rateable Value of the building. – Progressively tigher standards are over time likely to lead to a requirement for significant investment to remain compliant, or erode asset value.

In summary, underinvestment in the Council's 'commercial' property portfolio means that the portfolio is aged, ageing, not well-maintained and increasingly in danger of obsolescence, in particular as regulations around environmental performance of buildings and suppliers continue to tighten.

The challenge is how to fund the changes to the portfolio, governances, policies, processes and systems that are required to achieve the vision to create a sustainable, compliant and diverse property portfolio that helps support communities to thrive and prosper.

5. Opportunities and the case for change

5.1 Opportunities

The opportunities to address the challenges and issues facing the portfolio have been summarised in the table. They are drawn from the practical ideas expressed at the workshops and interviews with elected members and senior officers, along with published best practice guidance and the Avison Young strategy team's experience of public and private sector asset management strategy.

Area	Opportunity to ……
Financial Portfolio is financially unsustainable	– Increase income and reduce overheads by: • collecting arrears and evicting non-paying tenants; • active marketing and leasing under-rented space; • phasing out discounts unless clear benefit; and • selling underperforming assets and reducing the overall size of the portfolio.
Asset Strategy Clear strategy and plans for different asset types to improve value and reduce risk	– Transition over the medium term to a modernised, multi-use, multi-let, flexible, sustainable property portfolio. – Adopt a segmentation approach that sub-divides the portfolio and follows a defined strategy for each segment that maximises the value of properties within that segment. – Develop and drive Asset Level Plans (ALPs) that set out the future for each asset in terms of investment/ divestment and management, in line with priorities and policies.
Policy and process Policies that put residents at their heart and balance financial and social aims	– Improve clarity, fairness and transparency by developing a policy framework that sets out how the Council will allocate and set rental levels to VCS tenants, and how investment/ divestment decisions will be taken. – Develop "Social" lease clauses to oblige VCS tenants to: • equate value of rental discounts to social benefits; • forecast and report actual "Social Value Added"; and • accept mechanisms to enable Council to foreclose if fail to meet KPI targets.
Supporting regeneration Leveraging asset opportunities	– Stimulate economic activity and regeneration, through considering space for start-ups / enterprise incubators.
Sustainability Identifying an investment pathway	– Improve environmental performance and compliance with Net Zero Carbon targets: • collate, record and commission EPC surveys; and • develop roadmap for decarbonisation of buildings.

Area	Opportunity to ……
Data & Systems To support evidenced-back decisions and improve performance through BI monitoring	– Inconsistent, incomplete and inaccurate data about the portfolio reflects a lack of investment in fundamental property asset management systems: • Modern asset management systems and asset level planning approaches can be integrated into financial systems for e-invoicing, receipts / payments, budgeting and evaluating risks and liabilities, and release resources from antiquated management-intensive processes. • A case management system, particularly with bespoke AI / machine learning, would assist in marshalling and analysing key documentation around assets and support driving marketing, leasing and sales of surplus assets, to fund further investment in systems and the portfolio. • Commissioning condition surveys would enable the development of the required “comprehensive plan to be a carbon neutral council by 2030” and thereby “lead by example by retrofitting and reducing energy usage across our estate” [10].
Governance Improve decision support	– Improve collective, evidence-based decision making that balances financial, service, community and regeneration objectives by reconvening a corporate property board to: • Oversee the creation and implementation of corporate property strategy. • Make robust recommendations on asset management to Cabinet and elected members.

5.2 The Case for change

Under a ‘no change’ scenario (medium term) the Council will oversee a degradation in the portfolio that will:

– Reduce total revenue (a real terms decline).

– Reduce the available stock of space as properties are mothballed to avoid unaffordable statutory works and energy performance standards.

– Weaken social benefits as the space available for VCS groups decline and tenancies are awarded without the support of good data and a transparent decision framework.

– Potentially incur reputational damage and financial loss if breaches of statutory compliance occur.

The portfolio is on the verge of entering a spiral of decline, if measures are not taken to improve the condition and energy performance.

Indicative advice about market rental levels suggests that there is significant untapped potential in the portfolio, and seizing this opportunity could secure resources to invest both in the Council’s real estate assets and importantly in the people, processes and systems needed to manage them.

The next section outlines the proposed way forward and recommendations.

[10] As Brent Council has committed to in the Brent Borough Plan 2023-27

6. The Way Forward

6.1 Introduction

This Strategy aims to put the Portfolio[11] onto a sustainable financial footing, with a view to:

– Deliver community and social benefits;

– Achieve Net Zero (/ Carbon Neutral by 2030);

– Minimise the risks of property ownership, including statutory and health and safety compliance;

– Support and enable the Council's corporate strategy and, in time, align the portfolio better to demographic and social need.

The overall aim is a smaller, better, greener estate, financially viable and aligned to Council priorities.

6.2 Summary recommendations

The strategic aims will be achieved by adopting a **more commercial and leading practice asset management approach** that involves:

– Agreeing a set of clear **policies and procedures** for improved clarity and transparency around property asset management, including the allocation of space to community groups;

– Creating and embedding a consistent **framework for decision-making**, in line with the agreed policies;

– Developing and regularly reviewing structured **Asset Level Plans** that set out an evidenced-based rationale for the future ownership, use, management approach and investment (if retained), including expenditure on improving statutory compliance and decarbonising;

– Deploying a **segmentation approach** that categorises and organises properties with similar attributes into distinct segments, with a tailored plan for each segment to optimise the overall portfolio and allocate resources efficiently in line with overall financial and social aims;

– Developing **social impact agreements** and "Social" lease clauses to help ensure that tenants are incentivised or have an obligation to deliver social benefit that is commensurate with the Council's discounted sub-market rents (either through a lease agreement or management agreement).

We recommend that in time, this approach should be applied to the whole Council real estate portfolio through a strengthened **corporate landlord model**. This should be underpinned by the principle that the Council 'owns' property assets and service departments 'occupy' property assets to support service delivery. Strengthening the corporate landlord model will improve performance and value, by facilitating efficient resource allocation, higher utilisation, management efficiencies, improved compliance and risk management, and better BI to support decision making. It will involve a shift in responsibilities away from service departments to the central intelligent client team.

[11] "the Portfolio" as summarised in Annex A and Section 3 above.

6.3 Enablers - data and resources

This commercial and leading practice asset management approach will need to be **enabled by:**

– Increasing investment in people, processes, systems and property assets, paid for by increased income; and

– Improving MI / BI[12] and releasing resources for higher-value-added tasks by investing in better real estate asset management data / technology systems.

A financial case needs to be developed for the investment in people and data, and it is envisaged that it will be funded over time by **increasing net income.** This will be achieved through a combination of:

– Rental subsidy reductions

– More tenancies at market rents

– Active management of tenants leading to reduced debt

– Disposal of loss making or poorly performing properties

– Leveraging asset value through repurposing and strategic redevelopment

– Acquiring higher net return properties over the medium term (taking into account market trends).

Detailed Recommendations

To expand upon these themes, the Council is recommended to:

6.4 Agree clear policies and procedures

The core tenets of the policies are:

– The pursuit of best value for money for taxpayers (with a view to leveraging maximum social, community and financial benefit from the property portfolio).

– Compliance – with statutes, Building Regulations and Council policies.

– Clarity, fairness and transparency.

– Financial prudence and stewardship of taxpayers' assets.

Policies should cover the following areas:

– Acquisition

– Disposal

– Investment

– Maintenance and compliance

– Net zero, decarbonisation and climate adaptation

– Allocation of space to VCS sector

[12] "MI / BI" = Management Information / Business Intelligence. MI reports on current performance of the business (in this case, property assets); BI deals with a broader scope, taking into account different aspects of the business by using technology to deliver further analytics and insights.

– Granting of rental subsides

– Obligations of VCS tenants and the use of social lease clauses

– Measurement of social benefit

– Monitoring tenant performance and rent reviews

– Termination of agreements

The policy statement should include an outline of the policies purpose, objectives, scope, principles, roles and responsibilities, decision processes, compliance and monitoring and review process.

6.5 Develop a Decision-Making Framework

The decision framework should align with the vision and agreed policies and will help prioritise resources to ensure compliance.

– It is a mechanism for supporting the Council consistently apply the policies and make decisions on matters of disposal, retention, redevelopment, investment, change of use/ termination of tenancy.

– The framework should be published to meet transparency and fairness objectives.

– The Segmentation strategy (see below) will draw on the framework to sift properties into the correct segments (see below).

– It will help develop and drive Asset Level Plans and support recommendations e.g. for refurbishment and investment.

– The effectiveness of the decision-making framework is dependent upon the quality of data, including statutory compliance, environmental performance, market valuations, tenancies, financial.

6.6 Implement Asset Level Planning

The purpose of Asset Level Plans (ALPs) is to reach a decision on the future ownership, use, management regime and investment plan for each asset, in line with strategic priorities and agreed policies. The recommendation in the ALP will be based on the formal integration of perspectives from across relevant departments and stakeholders in Council, alongside the professional property and financial view.

The outputs of the ALPs should be consolidated to inform the annual plans, for example:

– Disposal (and potential acquisition) plan.

– Capital plan – including major and minor works.

– Annual revenue forecasts.

– Property management plan.

– Decarbonisation plan.

Key characteristics of the process include annual reviews to refresh and refine plans for:

– All larger / higher value properties

– All those with lease events in next 3 financial years

– 20% of the remainder.

A key output will be the categorisation of each property in terms of its future status (aligned to the segmentation approach); for example: "Hold"; "Invest" "Actively Manage", 'Dispose'. As well as informing financial and asset management planning, it will:

– Support regeneration objectives by identifying strategic “hold” and “invest” properties

– Avoid risk of “missed opportunities”, for e.g. start-up / seed businesses

– Stimulate economic activity and regeneration, through considering space for start-ups / enterprise incubators.

6.7 Adopt Social Impact Agreements and Leases

Adopt “Social” lease clauses, with express covenants to require, explicitly, VCS tenants to measure, record and report on actual social benefits delivered. This is to help ensure that VCS tenants are obliged to deliver social benefit commensurate with any discounted rents. To implement, the Council should:

– Develop and agree a corporate assessment methodology for quantifying social, economic and environmental benefit. This will include a combination of ‘input’ metrics such as utilisation, hours open, number of cases processed; and ‘output’ metrics such as changes to employment, reoffending rates and health outcomes, etc.

– Agree the approach to encouraging social benefit through discounted rents:

  - **Option 1:** Move tenants over time to a “market rent” and at the end of the year provide a refund of up to a capped level of the market rent, depending on their performance measured against a number of KPIs, reflecting the specific areas the Council wants to improve. This approach incentivises tenants to maximise social benefit.

  - **Option 2:** Negotiate a social impact agreement and discount the market rent in line with the expected social benefit. Actively manage the relationship, terminating the lease or reducing the discount, should the expected social benefit not materialise. This approach could be viewed as penal.

  - **Option 3:** Flexible revenue share agreements, where the rent charge is proportional to the revenue of the VCS sector, up to an agreed ceiling.

The preferred option should be based on a balance of multiple criteria such as acceptability, deliverability (e.g. legal) and resource costs. (See Section 7.2 Action Plan for timetable for selecting a preferred option.)

6.8 Segmentation Approach

Deploy a segmentation approach that categorises and organises properties with similar attributes into distinct segments, with a tailored plan for each segment to optimise the overall portfolio and allocate resources efficiently in line with overall financial and social aims.

Implementing a segmentation approach involves sifting holdings into the following 4 recommended segments:

1. Dispose	Low prospects of social value or financial return	High management costs; future liabilities high; long term vacant; low prospect rental or capital growth
2. Manage	Active Management Opportunities	Tenant non-compliance with obligations; regearing opportunity; high prospect of improved social or financial return for low capital spend
3. Invest	Investment opportunities, including repurpose	Longer prospects for rental and capital or social value growth but requires significant investment e.g. repurpose, retrofit, redevelop
4. Hold	Strategic	Important to control for longer term place shaping/ economic benefits

For each segment, a strategy should be devised to maximise value for money (see Section 7.2 Action Plan):

Dispose: Low value, high-cost properties with poor growth prospects should be disposed, in order to avoid significant expenditure with poor returns and to raise capital for re-investing in retained assets.

This covers properties with low prospects of social value or financial return and / or low return on investment (i.e. weak net yield) given e.g.:

- High future liabilities (for example, to modernise, maintain, achieve better environmental performance or to bring up to minimum statutory compliance;
- Unduly high management costs (due to time involved in managing secondary tenants);
- Weak links to regeneration / place shaping agenda; and / or
- Long term vacant.

Manage: Active Management Opportunities have the potential to improve performance and secure "Quick Wins", for relatively little investment. They comprise properties that hold the prospect for improved social or financial returns which involve minimal or relatively low capital spend, but they do require professional resource to realise the benefits. Examples of properties:

- Tenant non-compliance with obligations;
- Leasing / sales or lease re-gearing opportunity;
- Planned maintenance regime;
- Repossession for re-marketing; etc.

Invest: Investment Opportunities have the potential to unlock significant upside and meet strategic priorities:

- Longer-term prospects for good rental and capital or social value growth but requires significant investment;
- May require significant investment e.g. developing planning briefs, land assembly, decontamination, refurbishment/ redevelopment due to economic end of life or higher value alternative use;
- May allow Council to acquire sites with potential for significant value uplift due to population growth/ regeneration.

Strategic Hold: This segment comprises properties vital to enable delivery of the Council's priorities and unlikely to be easily replaced:

- Important to control for longer-term place shaping / economic benefits / regeneration;
- Currently delivers or likely to deliver economic and/ or social benefits that would not be provided by market.

It is recommended that there is an initial sift of properties into the segments using a high-level assessment framework. Over time the allocation of properties to segments will be informed by the outputs of the Asset Level Plans (ALPs).

KPIs should be identified for each segment and periodically monitored and reported to Property Board.

6.9 Enabling Data

Improve data, MI and release resources for higher-value-added tasks by investing in better real estate asset management systems, etc., to:

- Obtain, record, update, analyse and report key data / MI on performance / issues / risks;

– Digitise / automate / integrate routine functions;

– Improve ability to invoice and collect income; and

– Enable proactive asset management.

Enhance and improve community / social value impact of portfolio and better integrate with Planning, Development & Regeneration across Borough by mapping and overlaying demographic data against current distribution of property assets, including forecast / modelled future figures for e.g.:

– Population demographics (gender, age, ethnicity, disability);

– Socioeconomic metrics of relative income, wealth;

– Indices for crime, education, social deprivation;

– Other Council and related Public Sector assets such as schools, healthcare, other "frontline" Council and Public Sector delivery outlets.

Implementation starts with a business case for investment in data systems and data management, which should include a systems architecture review of vendor and in-house options.

6.10 Corporate Landlord Model

In time, the above recommendations should be applied as a corporate approach across the Council's property portfolio, including operational properties such as education, leisure, social care and administrative buildings. The benefits of a corporate landlord model are improved allocation and utilisation of all Council property assets by identifying under-used and under-exploited opportunities for increased shared utilisation by VCS groups.

In the medium term the Council should move to a modernised, multi-use, multi-let, flexible, inter-operable and sustainable property portfolio, through applying the segmentation approach.

6.11 Financial Case

Implementing these recommendations will require investment in systems, processes and people. A robust investment case should be developed to place the portfolio on a financially sustainable footing. This is based on the opportunity to more than double net income (current rental income is c £2.5M) and cut overheads by driving active management, marketing and lettings / sales of under-used and under-rented or void spaces within portfolio. For example, by focussing and strengthening the team to:

– Collect arrears (i.e. significant uncollected rent @ c £600k) and evict non-paying tenants;

– Phase out discounts unless clear, reportable and trackable social benefit; and

– Actively pursue rental / sales opportunities.

This will generate:

– More income from underutilised and vacant assets by:

 (a) leasing more space at full Open Market Rental Value, plus;

 (b) sharing more space and creating more flexible and interoperable buildings, and

– Potentially one-off capital receipts by selling underperforming assets (if any).

7. Implementation and Next Steps

7.1 Change programme

A change programme should be established to implement the strategy. There are 3 broad phases:

1. Establish the programme objectives, resourcing, funding and governance. It is recommended that a programme scoping document is developed that quantifies the expected benefits, the resource costs, who is responsible, who is accountable and details of the oversight board. Furthermore, the possibility of programme funding through 'quick wins' from asset disposals or rental increases should be identified with the aim that its implementation is cost neutral.

2. Having set up the programme, the next phase is to develop the policies, decision frameworks and plans that are described in the recommendation section above.

3. The implementation phase refers to the delivery of the plans, which will involve disposing of some assets, undertaking prioritised capital works including statutory compliance and energy efficiency improvements, and major investment in selected assets e.g. repurposing. In parallel there will be active management of the core long-term hold assets to improve financial return and social benefit.

Creating the benefits case to justify the appropriate resourcing levels is an essential first steps. As is setting up the governance to oversee and monitor the programme. Quick win financial benefits should be sought to fund the resourcing required to set up the programme and design the changes.

7.2 Action plan

Recommendation	Actions	By When
Develop and approve draft property strategy	– Obtain approval of property strategy and adoption by Cabinet – Set up programme	May 2024 July 2024
Quick Wins to maximise rent and regularise tenancies	– Identify opportunity for regularising occupation, rent reviews and lease renewals and initiate legal notice or lease negotiations (timeline may be constrained by statutory notice periods).	Current – March 2025
Corporate property board	– Develop terms of reference and agree membership of a new corporate property board to support cross-department collective decision making on property acquisitions, disposals, capital investment, change of use and management. – The board should be responsible for implementing this strategy, including developing new policies and	September 2024

Recommendation	Actions	By When
	processes. This will involve overseeing the activities below.	
Policies	– Confirm policy areas. – Draft policies and framework.	October 2024 Actioned (see Appendix 2)
Asset Management Plans	– Design a process for asset management planning, including objectives, outputs, standardised templates or workbooks, responsibilities, dependencies and roll-out programme. – Run a pilot, learn lessons. – Roll-out across the portfolio in tranches (the speed will depend on resource capacity).	December 2024 January 2025 – October 2025
Decision-making framework	– Agree objectives, scope and outputs. – Design and build the framework. – Pilot and refine. – Go Live.	May - July 2024 July - November 2024 January 2025
Corporate Social Benefits Assessment Methodology	– Agree objectives, scope and outputs. – Agree priorities to measure. – Identify KPIs and data sources. – Pilot. – Go live.	November 2024 December 2024 July 2025
Social Impact Agreement Leases and Rent	– Agree approach to encouraging social impact through discounted rents (undertake an options appraisal) and take to Council for a decision. – Create model social impact lease clauses. – Communicate and provide training to socially trading organisations and VCS groups. – Roll-out new agreements.	May – September 2024 Autumn 2024 January -June 2025 January 2025
Implement Segmentation approach	– Undertake Initial Sift. – Agree strategy for each segment. – Develop a plan per segment for 2024/25 quick win and priority initiatives. – Progress reports to Corporate Property Board. – Prepare 2025/26 plan based on asset level plans.	May- Nov 2024 December 2024 January 2025 August 2025

Recommendation	Actions	By When
Data and processes	– Identify data gaps and improve quality and analysis of property data.	Current – April 2024
	– Carry out health and safety checks and prepare risks assessments for all assets managed.	Current – April 2024
	– Specify high level information management and reporting requirement (KPIs).	Current – October 2024
	– Review current system against requirements and market options and develop a business case for upgrading data and systems in collaboration with Finance and IT.	
	– Develop a business case for data and systems.	Sept-Dec 2024
	– Lease renewals	Current – March 2025
	– Rent reviews	
	– Health and safety compliance (high priority)	-“-
	– EPC	-“-
	– Accessibility audit (high priority)	-“-

7.3 Seed funding

The change programme can be seed funded by realising quick win opportunities to increase rental income and reduce rental arrears in 2024.

This will require an additional commercial property consultant team reporting to the Head of Property for 9 months with the target to deliver £0.36M of additional revenue and £0.7M of one-off capital receipts, in 2024/25.

The table shows that a resource investment of approx. £0.25M could generate £2.6M of revenue over 2 years:

FY	24/25	25/26	Total
Additional revenue	£366,000	£732,000	£1,098,000
Additional capital	£700,000	£1,050,000	£1,750,000
Consultant costs	(£129,600)	(£115,200)	(£244,800)
Net income	**£936,400**	**£1,666,800**	**£2,603,200**

The underpinning high-level assumptions for the figures above, are as follows:

- For all ‘lease expired properties’, a conservative assumption that 50% of the uplift (£0.2m) between the current total rent passing and the ‘minimum’ market rental that may be achieved (refer to Section 3.4), can be realised in 2024/24. It is assumed 100% (£0.4m) of this uplift may be cumulatively realised in 2025/26.

- For the ‘void’ properties, where current total rent passing is zero, and the ‘minimum” market rental is £0.7m, a conservative assumption that 12.5% of this amount (£0.1m) may be realised in 2024/25 and 25% of this amount (£0.2m) in 2025/26.

- For the remaining (non-expired and non-voided) properties, total rent passing is currently £1.0m, while the 'minimum’ market rent' is £2.4m; a conservative assumption is that 5% (£0.1m of this uplift may be realised in 2024/25 and 10% (£0.2m) in 2025/26.

- Total capital receipts of £1.75m may be achieved; comprising of £0.7m in 2024/25 and £1.05m in 2025/26. This is based of the ‘minimum’ rental value of the ‘void’ properties (£0.7m) with an applied net investment yield of 20%; and a further conservative assumption that half (50%) of this figure may be realised over the next two years.

7.4 Enablers of strategy implementation

The recommended enablers to support implementation of the programme are summarised below:

- **Data** – accurate data on the portfolio, and expected costs and benefits.

- **Leadership** – strong and consistent leadership to ensure recommendations are delivered.

- **Governance** – effective cross-service working and strong programme management through a Corporate Property Board.

- **Integration** – closely integrated asset management decision-making and action across the entire portfolio, including with Finance, Communities.

- **Strategies and policies** – a framework for decision-making encompassing social benefit.

- **Rules** – clear protocols on, for example, the allocation of space at discounted rents, lease agreements, KPI, and the responsibilities of tenants as occupiers of space.

- **Challenge** – a robust process whereby the retention of all assets is subject to review and challenge.

- **Communication** – a strategy to effectively communicate the action plan to implement the programme, its costs and benefits, and the roles of stakeholders in shaping and contributing to the success of the programme.

7.5 Skills required to implement the strategy

The following skills will be required to implement the recommendations and rebalance the portfolio:

- **Asset management strategies** – to prepare a commercial segmentation approach and to lead the preparation of asset level plans.

- **Market knowledge** – to identify optimum assets for acquisition and disposal and deliver the investment strategy.

- **Conveyancing/legal support** – to assist with delivery of the strategy and support acquisition and disposal processes.

- **Management consultancy (real estate)** – to design and implement policies, processes, governance and to develop a business case for investment in systems and data.

– **Programme management** – to ensure the change programme hits milestones, meets budgets and delivers a high performing portfolio supported by a high performing management model.

Many of these skills are available within the current team, however, a skills audit is required to identify gaps

Annex A: Scope – Summary of Portfolio Considered

The portfolio in scope comprises primarily the non-owner occupied "commercial" property portfolio owned by the Council, i.e. income generating or potential income generating:

Description	Approximate Numbers[13]
Community Use	54
Leisure	12
Retail (incl. Café)	14
Office	12
Other[14]	14
Grand Total *Excluding individual units in multi-let buildings*	**106**

Rent per annum:

Total Properties:	95
Total Rent:	£2.3M
Ground Rent (HRA):	£0.5M
Total rental income	**£2.7M**

Reinstatement value:

13 Analysis per dataset provided by LBB's Property & Assets team (P&AT) in August 2023 and analysed by Avison Young September-October 2023. Ongoing work by LBB's P&AT continues to develop and refine the understanding relating to this portfolio, with an expanded list of now 106 property assets.

14 "Other"= Builders Yards/portacabins; Education (within scope); Open storage land; WC; other (blank or pending).

Insurance Valuation (FIV):		
Reinstatement Value:[15]	£309.2M	*See Footnote*
Total Area shown:	69,800	sq m GIA

[15] NB: Reinstatement Value = estimated Cost of Rebuilding.
Open Market Value of the property may be considerably different.

Annex B: Implications of Minimum Energy Efficiency Standards

These are excerpts from Private Investors' Paper, re: implications of Minimum Energy Efficiency Standards (MEES), published 19th June 23.

As set out in HMG's regulations, in general a landlord must provide an Energy Performance Certificate (EPC) if:

– Renting out or selling the premises; or

– Finishing a building under construction; or

– Making changes to the number of parts used for separate occupation, which involve providing or extending fixed heating, air conditioning or mechanical ventilation systems.

As solicitors Addleshaw Goddard have set out:

*"landlords can no longer ignore the impact of the Energy Efficiency (Private Rented Property) (England and Wales) Regulations 2015 (**MEES Regulations**). From 1 April 2023 it is now unlawful for landlords to **continue to let** a commercial property with an F or G EPC rating (known as "sub-standard" properties under the MEES Regulations), even if the lease was granted prior to the MEES Regulations coming into force in 2018 (subject to certain exemptions). See here for the implications and commercial considerations.*

"In 2022, the government estimated that around 18% of commercial properties in the UK were F or G rated. Some of these may have been brought up to standard to meet the 1 April 2023 deadline. However, it does seem likely that there will still be a large number of properties out there where there will be tensions between landlords and tenants as each party grapples with being green in their own way and determine where the risk and compliance with MEES should sit in commercial leases."

Regulations setting out Minimum Energy Efficiency Standards (MEES) are making it increasingly unlawful to rent properties that do not meet the minimum Energy Performance Certificate (EPC) requirements, bar some exemptions, with landlords facing serious sanctions for non-compliance. This means lenders will also have to navigate the changing regulatory landscape and consider ESG criteria when deploying capital.

Currently, non-domestic buildings in England and Wales need an EPC rating of E or higher to be viable for lease. From April 2030 rented property will be required to have at least a B rating. This poses a significant challenge for the real estate sector given that the vast majority of existing commercial stock in England and Wales – around 64% – falls below the B threshold for energy performance[5]. In real terms, over half a million individual assets need to be compliant with MEES within the next seven years[6].

[Note that] lenders may consider excluding inefficient real estate assets as defined by the Sustainable Finance Disclosure Regulation – such as those with an EPC of C or below if built before 31 December 2020 – where proceeds of the loan are used to improve energy efficiency and the asset is expected to meet the relevant criteria upon completion of the renovations funded by the loan, then these assets will no longer be deemed inefficient. Once the relevant works are complete, they may even qualify as "green buildings" should they meet specific eligibility criteria.

When funding existing buildings that do not currently meet energy requirements, lenders can hold borrowers accountable by ensuring loan documentation includes specific clauses on energy performance obligations. This will typically require the borrower to improve overall energy efficiency and/or aggregate green building certification as well as meet specific thresholds such as EPC B or above, LEED Gold or above or BREEAM "Excellent or above".

[3] European Parliament, "Energy performance of buildings: climate neutrality by 2050", (europarl.europa.eu), 9 February 2023.

[4] UK Government, "Rigorous new targets for green building revolution", (gov.uk), 19 January 2021.

[5] UK Government, "Energy Performance of Buildings Certificates Statistical Release: January to March 2023 England and Wales", (gov.uk), 27 April 2023.

[6] Gerald Eve, "Energy Performance in Non-Domestic Buildings", (geraldeve.com), July 2021.

“The value of investments will fluctuate, which will cause prices to fall as well as rise and investors may not get back the original amount they invested. Past performance is not a guide to future performance. The views expressed in this document should not be taken as a recommendation, advice or forecast.”

Annex C: Case Studies from 2nd Workshop

Case Studies from 2nd Workshop 30th November 2023

This information is included in ‘Appendix 1 Annex C - Case Studies 1-4’ due to containing the following category of exempt information as specified in Paragraph 3, Schedule 12A of the Local Government Act 1972, namely:

“Information relating to the financial or business affairs of any particular person (including the authority holding that information)".

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