**SDCT response to:**

**UK Parliament Public Accounts Committee: Local Authority Commercial Investment Inquiry**

**Detail on Government website:**

Local authorities have invested in commercial property for a long time, but there has been a recent step-change in the scale of activity. Estimated commercial property purchases for 2013-14 to 2015-16 were £460m; compared to an estimated £6.6bn for 2016-17 to 2018-19.The NAO’s report ‘Local authority commercial investment’ assesses whether MHCLG has effective oversight of the risks to the financial sustainability of local authorities due to their investments in commercial property.

The report finds that there has been a significant increase in out-of-area commercial property acquisition. There has also been an increase in acquisitions that are outside the acquiring authority’s LEP area. The report also finds that changes made by CIPFA and MHCLG to statutory guidance have not stopped some authorities borrowing large sums, to invest in commercial property. Commercial property acquisition is concentrated in a relatively small proportion of authorities. The NAO conclude that local auditors have raised concerns about the governance and risk management arrangements for investment activity in some authorities. The data MHCLG collects has limited usefulness for monitoring commercial activity and assessing its risks.

The Committee will question officials from the Ministry of Housing, Communities, and Local Government on gaps in commercial skills in local government, and the extent to which the Department formally monitors commercial activity and long-term exposure to risk.

The Committee will also ask officials about the Ministry’s response to COVID-19, and what impact the pandemic has had on local government finances.

The NAO’s February 2020 report on ‘Local authority commercial investment’ assesses whether MHCLG has effective oversight of the risks to the financial sustainability of local authorities due to their investments in commercial property.

**Response**

Responder

Name: Adrian Rowbotham

Organisation: Society of District Council Treasurers

Role: Lead Advisor for Growth and the Commercial Agenda

Reason for submitting evidence: Representing District Council Section 151 Officers

**Background**

1. The Society of District Council Treasurers (SDCT) was formed in 1974 and represents the 188 district council finance functions in England.
2. The Executive Committee of SDCT comprises of up to 26 of the district council chief finance officers (s151) who take responsibility for advising and leading on specific areas relevant to the finance profession.

**District Council Funding**

1. Local authorities **and district councils in particular**, require new and innovative income streams to enable them to continue to deliver statutory services to the high standard required by the public.
2. Many district councils no longer receive any Revenue Support Grant (RSG) from the Government with negative RSG still a possibility in one form or another.
3. Business Rates Retention remains uncertain for the short term and even more so in the long term. The resetting of the Business Rates System will have a significant financial impact to authorities but particularly to those districts who have delivered significant growth. The Fair Funding Review (now postponed) increases the financial uncertainty authorities face.
4. Council tax referendum limits continue to restrict the ability to obtain extra income and many service income streams (e.g. planning) are restricted by centrally set fees or increases.
5. Many authorities have reviewed how their services are delivered and realigned services, however you can only reduce costs so far. This has meant authorities have looked to other income streams which are a necessity if district councils are to continue to operate successfully and property investment is one area that many have gone into. Local authorities are committed to balancing income and financial risks in the delivery of vital services through income which is raised locally from fees and charges or from commercial property investments. Income continues to be a key element of a District Councils budget.
6. Other options include doing nothing which inevitably leads to cutting services. Such an approach is not sustainable in the long term and clearly reduces the level of much needed services provided by the sector. Doing nothing as we approach the financial cliff edge is easy to do from a compliance perspective but s151 officers need to find solutions to divert away from the cliff edge

**Commercial Property Investment**

1. It should be remembered that local authorities have invested in property for many years, this is not new to the Sector and there are legal powers to do this. As an example, S120 of the Local Government Finance Act 1972 contains the following provision:

Acquisition of land by agreement by principal councils.**E+W**

(1) For the purposes of—

(a) any of their functions under this or any other enactment, or

(b) the benefit, improvement or development of their area,

**a principal council may acquire by agreement any land, whether situated inside or outside their area.**

1. However, there has clearly been an increase in property acquisitions for the reasons outlined above. The continuation of reduced levels of funding from central government has led to local authorities wanting to become more self-sufficient. Commercial investments enable the risks to be managed at a local level rather than having to react to ongoing reductions in government funding.
2. Property investments have been made by local authorities for economic regeneration purposes, financial return purposes or a combination of both depending on the circumstances each authority finds themselves in. As an example, local authorities have purchased retail units in order to protect jobs in their areas or are holding them for future redevelopment as part of regeneration schemes. The NAO report does not provide this context or discuss any detailed rationale behind local authority property purchases.
3. It is an authority’s responsibility and that of the s151 Officer to ensure the necessary due diligence has been undertaken prior to making a commercial investment.   This may be internally or in the majority of cases, by using external expertise in a range of fields such as legal, property, tax, treasury etc. S151 officers are also required to be qualified accountants with CPD requirements through their professional body. This ensures skills and knowledge are kept up to date and relevant.
4. Local authorities have clear governance structures in place that include Member approvals where significant expenditure or projects will go through a thorough Member process. Members’ have a wide range of experience which should be used when scrutinising these types of decisions.
5. One benefit of the ‘local government family’ is that it is not a competitive environment and therefore local authorities are much more open to sharing best practice and experience. Bodies such as SDCT act as a conduit to enable this to happen more freely.
6. It is important to spread risk in any investment portfolio and property should be no different. Risk can be spread in a property portfolio in a number of ways such as location, asset category (industrial, office, retail, residential, etc), freehold or leasehold, single or multi-tenanted etc.
7. It should therefore not be surprising, or seen as a bad thing, when property investments are made outside of a local authority or LEP area as local authorities are spreading their risk. It should also be appreciated that the same opportunities do not arise in every local authority area up and down the country.
8. Local authorities by their nature are political organisations and investing “locally” brings emotive issues into the frame rather than pure a commercial mind set.  By investing out of area it means councils can make commercial decisions based on hard facts rather than political demands.
9. The investment into commercial property by local authorities can also strengthen the Public Sector Balance Sheet and it is this point that is often overlooked. Where those investments are generating a positive return, this supports the revenue budget and had been fundamental in maintaining services. Where loans are repaid this reduces the liability, the investment is shown as an asset on the balance sheet and is one that generally appreciates in value and it is these two factors that increase the strength of the local authority’s balance sheet.

**Impact the COVID-19 pandemic has had on local authority finances**

1. The financial returns local authorities have made to MHCLG should highlight the known and potential financial impacts.
2. The financial impacts cover the following areas:
   1. additional expenditure to provide much needed additional services (such as food distribution hubs and increased homelessness demand) to residents and support to businesses.
   2. Reduced income from services such as car parking, planning etc.
   3. Reduced collection rates of Council Tax and Business Rates due to the impact of COVID-19 on residents and businesses leading to cashflow issues and income losses in both the current financial year and 2021/22.
3. The funding provided by MHCLG to date will help to address some of these issues but is likely to be well short of the final cost that local authorities will face. Without further funding, the financial position of local authorities will worsen which will inevitably have an adverse impact on the services provided which have proved to be vital in these challenging times.

**Conclusion**

1. I hope that this response has provided a clear description of why local authorities (especially district councils) have increased commercial property investment and the approach they are taking to address the risks involved to ensure that decisions are taken after suitable due diligence has been carried out. The SDCT believes that Districts have responded positively to the ongoing reductions in government funding and have taken a measured approach to income generation through commercial investments and this has enabled services to be maintained. The Districts have responded well in supporting their communities in these unprecedented times and this has been well evidenced in recent weeks, this in part results from Districts maintaining services and capacity and this has been achieved through being able to generate income locally.
2. The last paragraph in the Inquiry remit states “The NAO’s February 2020 report on ‘Local authority commercial investment’ assesses whether MHCLG has effective oversight of the risks to the financial sustainability of local authorities due to their investments in commercial property.” **It should not be forgotten that there are great risks to the financial sustainability of local authorities if they do not obtain additional income from routes such as investing in commercial property.**