

Property Investment Policy

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1. Objectives

The objectives of this Policy are:

- To comply with the legislative requirements and regulations relevant to the management of Council's strategy for revenue growth.
- To maximise earnings, through the creation of a diversified Property Investment Portfolio ("PIP"), for the sole purpose of investment, to contribute towards Council's long-term financial sustainability.

2. Policy Statement

Councils face revenue pressures, plus policies of Government, in the charging and receipt of traditional income sources. These pressures include:

- rates pegging;
- reallocations of Section 7-11 and other contributions, towards State Government;
- the ongoing uncertainties of grant funding applications and successful outcomes; and
- global trends - fluctuation in approved Local Government investment returns.

Wingecarribee Shire Council will further diversify its income sources and revenue earnings to:

- enhance income from appropriate "risk adjusted" property alternatives; and
- target income sources which cannot be influenced or reduced by Government entities; and
- reduce proportionate exposures to individual income sources.

The property asset class currently provides the best opportunities for Council to:

- diversify its revenue and exposures;
- increase operational income and general revenue; and
- access attractive returns from low risk, passive investment properties

Revenue generation aligns with a core function of property, in the traditional Council business model.

Property is a "cost of business" not core business. **Its function should be viewed as a means of delivering key business services and facilities to the community, not as a pool of passively managed assets.**

Revenue delivery is a key business service, achieved via an Investment Property Strategy. A Property Investment Portfolio ("PIP") can be created and delivered, through the existing Local Government Legislative Framework.

Policy Framework

Consistent with the need to enhance income, this Policy sets out the Framework and Guidelines to create and then enhance a Property Investment Portfolio ("PIP").

Council will deliver a Property Investment Strategy which will:

- create mechanisms for delivering and maintaining a PIP;

- include strong risk management and guidelines, for portfolio weightings and allocations; and
- recommend an appropriate PIP size and annual income target.

Portfolio construction and delivery will occur via reviewing and recommending opportunities to:

- re-cycle capital from the existing property portfolio, into appropriate passive income properties, either through recommended asset sales (operational land), or internal property development opportunities;
- consider if any balance sheet reserves should be utilised for PIP investment purposes;
- set a benchmark annual return ("hurdle rate") consistent with that achievable from owning passive, income generating property assets;
- acquire appropriately diversified assets that individually meet or exceed the hurdle rate;
- acquire assets in accordance with the Property Investment Policy;
- target low risk internal opportunities to deliver income from the existing portfolio; and
- consider rare opportunities outside these parameters, where the justification is compelling.

Council will apply portfolio construction, risk diversification and similar skills to ensure:

- a diversified property portfolio, with varying lease expiry dates, and tenancy exposures;
- generally smaller investments for diversity, but with individual values often above the family trust investment market, where the hurdle rate is more achievable;
- pre-acquisition due diligence for each asset, with external input and recommendations;
- an independent current market valuation for each asset, as part of the pre-acquisition due diligence;
- associated portfolio due diligence – reflecting the diversification and other benefits that each recommended acquisition, delivers to the macro portfolio; and
- annual reporting on the portfolio performance, income achieved and dividends available.

As the portfolio is assembled Council will:

- provide annual PIP reports and results;
- monitor the Weighted Average Lease Expiry ("WALE") of the individual assets and the PIP as a single entity, plus allocations to each property type;
- formalise portfolio distributions and allocations via recommendations and endorsements;
- include any deliverables or reportable outcomes in Council's Operational Plan; and
- adjust and enhance its Long-Term Financial Plan, and other deliverables accordingly.

As scale exceeds \$100m, the guidelines will be adapted to:

- limit combined lease expiries to a fixed % of total PIP income, in any single year;
- limit single asset and single tenant exposures, to a fixed % of total PIP value; and
- set maximum exposures for individual asset types – eg. industrial, core retail, bulky goods etc.

Council will review the PIP and provide an annual report to Council covering the PIP performance, in accordance with the requirements of the Property Investment Policy. Council will also review the Policy framework bi-annually.

The specified benchmarks within the Property Investment Policy will be reviewed annually.



3. Policy

This policy sets the framework to enable revenue growth from the formation of a Property Investment Portfolio, with the sole purpose of property investment. This investment is intended to represent a significant contribution to the total income of Council.

It is essential that Council has clear policy guidelines in respect of the type of properties purchased for the portfolio, plus appropriate due diligence, and risk mitigation procedures.

Legislative Context

Council is empowered by the operation of Section 186 of the *Local Government Act* 1993 (LG Act) to acquire land for the purpose of exercising any of its functions.

In that regard Section 186 of the *Local Government Act*, 1993 states:

(1) A Council may acquire land (including an interest in land) for the purpose of exercising any of its functions.

While this section is explicit around Council's powers to acquire land, there are nevertheless variations in the types of investment property that can be purchased, which are not explained. This policy aims to clearly define the types of property investments that can be acquired.

The 'Functions of a Council' are detailed in Chapter 6 of the *Local Government Act*, 1993. Section 24 (contained in Chapter 6), states:

(1) A Council may provide goods, services, and facilities, and carry out activities appropriate to the current and future needs within its local community and of the wider public, subject to this Act, the regulations, and any other law.

Principles

- To minimise the potential for loss of revenue and capital value, through the creation of a policy that includes an independent assessment of each property and the combined Property Investment Portfolio's perceived risk.
- To minimise the potential for loss of revenue and capital value from property, through development of clear management procedures and decisions around acquisitions and revenue growth, from the Property Investment Portfolio.
- To establish planning and reporting framework for ongoing monitoring and review of Council's revenue from the Property Investment Portfolio and Policy.
- To confirm delegations and other relevant governance matters, in relation to Council's revenue results and distributions, from the Property Investment Portfolio.

Criteria for Property Selection

The selection of any property targeted for inclusion in the PIP will require a resolution of Council, following confirmation that all of the following selection criteria have been met:

- Projected return on investment for each property to be a minimum of 4.75% net growth per annum on average, over the life of the lease term(s).
- Building age and structural condition presents minimal risk to Council based on consideration of current and future capital investment needs.
- Location of site and its relationship to tenant demand over time.
- The weighted average lease expiry (WALE) is consistent with Council requirements and represents an appropriate level of risk.

Reflecting current asset specific characteristics, types and risks, the minimum WALE for any asset type for inclusion in the PIP is as follows:

Asset Type	Minimum WALE
Commercial Offices	7.0 years
Standard Retail Shops	3.0 years
Retail – Bulky Goods	5.0 years
Industrial	6.0 years
Other – if recommended	Based on independent assessment

In exceptional circumstances, Council’s Executive may recommend a property for acquisition that does not meet all the above criteria, provided the investment logic and the key recommendations are considered compelling and are supported by Council, at Council’s sole discretion.

- Full due diligence review has been performed with respect to:
 - the structural integrity and physical condition of the building,
 - an independently assessed current market valuation of the property, compared with the acquisition price.
 - any land pollutants or encumbrances,
 - each existing lease on the property,
 - any other areas which any independent legal or other specialist advice may recommend.
- Further due diligence has been completed with respect to any enhancements (or deterioration) to the portfolio as a whole:
 - in respect of the property exposures and income diversity of the portfolio,
 - the weightings to the specific asset classes,
 - the general composition of the portfolio and the tenant specific exposures.
- The property has been reviewed by Council’s appointed Property Investment Advisor for the purpose of providing the appropriate property investment advice.



Property Investment Advice

Council's Property Investment Advisor must be suitably qualified by industry standards to provide the necessary advice.

The Advisor must be an independent person who has no actual or potential conflict of interest in relation to investment decisions and the strategy being recommended.

Any property identified through an independent source or any a third-party agency, must be subject to a full review by Council's Property Investment Advisor, who must make recommendations accordingly.

Revenue Allocation

Using the 2022/23 Budget as a baseline for revenue, any additional revenue above this baseline will be allocated as follows:

- 80% to be allocated to the Property Investment Reserve
- 20% to be allocated to General Revenue

All proceeds of sales of that are not bound by legislative provisions (i.e. Roads Reserve and The Roads Act) will be allocated to the Property Investment Reserve.

Review of Investment Portfolio Performance

A report on the performance of the overall investment property portfolio will be presented to Council at the end of each financial year, with monthly monitoring by Council's Executive in a manner consistent with the requirements of Local Government legislation.

The review will contain, as a minimum:

- the actual income performance of each property verses its budgeted performance;
- the combined income from the full portfolio; verses its budgeted performance;
- the reasons for any variances exceeding 5% of budget;
- a summary of actual vacancies, maintenance, or other costs for the relevant financial year;
- all property rent reviews, option renewals or lease expiries are complete, or if not complete then the forecast timing and nature of expected outcomes;
- any other matters considered material, for any single property, and the portfolio as a whole;
- a review of the portfolio asset weightings, the portfolio lease expiry profile, and the WALE, against the approved benchmarks;
- any known or forecast costs or vacancies, for the following financial year; and
- a forecast budget of expected revenue and costs for the coming financial year.

4. Scope

This Policy applies to accumulate a diverse operational Property Investment Portfolio, primarily incorporating commercial, retail and industrial property inside the Wingecarribee Shire Local Government Area.



5. Responsibilities

Responsibilities for the implementation of this Policy are shared between Councillors, Executive and staff as follows:

Councillors:

- To lead the community in their understanding of, and compliance with, this Policy.

Executive:

- To implement this Policy; and
- To lead Council staff in their understanding of, and compliance with, this Policy.

Director – Corporate, Strategy and Resourcing:

- To implement this Policy;
- To provide guidance to Councillors, Executive and other staff as to the content and implementation of this Policy; and
- To ensure the timely review of this Policy.

All Council staff:

- To comply with this Policy and any associated procedures and legislation.

6. Performance Measures

The success of this Policy will be measured by:

- A clear understanding of Council's Policy in relation to Property Investment.
- No reports of breach of this Policy.

7. Definitions

Property Investment Portfolio

The portfolio of commercial, industrial, retail and other income generating properties, owned and specifically grouped by council, for the primary purpose of generating rental income. The income is generated through securing appropriate property tenants, under medium, or long-term leases.

Investment Property

Council owned operational land/buildings that form part of the Property investment Portfolio.

Passive income Generating Property Assets or Passive Income Properties

Properties delivering income under medium, or long-term leases, which are renewed on expiry for further income generation. For the majority of the property ownership period, council's involvement as owner is limited to the more passive property management functions, such as maintenance and rent collection.

Asset development, re-positioning or similar pro-active management strategies are not targeted and occur only where necessitated, by major lease expires or other significant property changes

Hurdle Rate

The required percentage return on asset cost, calculated as the net annual rental, expressed as a percentage of the asset's purchase price.

The hurdle rate represents the minimum return council will accept, when acquiring assets for inclusion in the Property Investment Portfolio and is based on general prevailing market conditions.

The hurdle rate is reviewed annually or otherwise as considered necessary, by reference to analysis of comparable sales evidence, for assets which would otherwise meet all required prerequisites for inclusion in the Property Investment Portfolio.

Portfolio Lease Expiry Profile

The ranking of all portfolio lease expiries, in date order and also by reference to the proportion of income each tenancy delivers, as a percentage of the total portfolio income.

The combined details provide the proportion of the total portfolio income to expire in the current and every future year.

The portfolio lease expiry profile is a risk management tool for the timely management and actions of future expiries. It is also used to measure overall portfolio diversification, so that significant components of the Property Investment Portfolio do not expire in a single, or a very limited number of years, when likely market conditions for renewal cannot yet be known.

Weighted Average Lease Expiry (WALE)

A measurement of the average time period when all leases in each property, and the portfolio as a whole, will expire.

The WALE reflects the average remaining time period (or security) by rental dollar received and should generally be kept as high as reasonably possible for each passive property, but more specifically, for the combined portfolio.

An example of the calculation of the WALE for a hypothetical property follows, where two tenants have differing rental levels and remaining lease terms. The date used for the example is 31 Dec 2022.

A	B	C	D	E	F
Tenant	Net rent paid	Lease expiry	Remaining Term	Proportion of total rent	Weighting (D x E)
Tenant 1	\$120,000	31 Dec 2029	7.0 years	54.55%	3.82
Tenant 2	\$100,000	31 Dec 2027	5.0 years	45.45%	2.27
Totals	\$220,000			100.00%	6.09

The weighted average lease expiry for this property is 6.09 years.

The calculation occurs for each individual property, then for the portfolio as a whole via including the total income from each property and its individual WALE. An example follows.

A	B	C	D	E
Property	Net rent pa	Property WALE (years)	Rental weighting (%)	Weighting (C x D)
Property 1	\$350,000	3.5	48.6%	1.70
Property 2	\$ 80,000	4.2	11.1%	0.47
Property 3	\$125,000	7.7	17.4%	1.34
Property 4	\$165,000	4.9	22.9%	1.12
Totals	\$720,000		100.0%	4.63

The portfolio WALE in this example is 4.63 years.

8. Related Material

8.1 Related Legislation

The following legislation is related to this Policy:

- Local Government Act, 1993
- Crown Land Act 1989
- Retail Leases Act, 1994
- Conveyancing Act, 1919

8.2 Related Policies, Procedures and General Manager Practice Notes

The following policies, procedures, strategies and action plans are related to this Policy:

- Property Investment Strategy 2022
- Property Action Plan

9. Non-compliance with this Policy


Non-compliance with this Policy should be reported to Director – Corporate Strategy and Resourcing who will investigate and determine the appropriate course of action.

10. Document Control

10.1 Version Control

Version	Adoption Date	Notes
1		

10.2 Superseded Documents



The following documents are superseded by this Policy:

Document Title	Adoption Date	Notes

11. Attachments

1. There are no attachments to this Policy.

Approved by:

WINGECARRIBEE SHIRE COUNCIL

Date: