

Attachment A

Investment Property Policy

Investment Property Policy

Purpose

The Investment Property Policy (the Policy) sets out the requirements for the management of the City of Sydney's (the City's) Investment Property portfolio. The City requires that all investment activities be exercised with care, diligence and skill and not for speculative purposes.

The policy sets the framework to realise the City's Investment Property revenue objectives which align with broader principles of financial sustainability and enable the City to discharge its functions which include the provision of goods, services, facilities and other activities for the community and the wider public. It reinforces the City's ongoing commitment to maintain a conservative and diversified income base to reduce the burden on ratepayers for funding all of the City's operations.

A diversified income base lessens the significant constraint placed on the City's income by the current NSW rate pegging mechanism. Investment property income, arising through acquisitions and the repositioning of existing assets, is one of the few opportunities available to assist the City in generating significant revenue outside rates and annual charges to enable the City to discharge its functions under the Local Government Act. Augmenting operating income also enhances the City's performance against key metrics set by the Office of Local Government that aim to measure financial sustainability.

Strategic investment in property assets can provide the City with stable income streams over the longer term, while securing the value of funds invested in an underlying asset that has historically appreciated over time. In appropriate circumstances, investment in property offers financial advantage over term (cash) investments placed with financial institutions under the City's Investment Policy.

The policy provides for the investment objectives and actions, whilst recognising that the City's Investment Property horizon is over the long term, reflecting the relatively illiquid nature of Investment Property.

Scope

This policy applies to the City's Investment Property holdings, comprising those properties owned by the City that constitute 'Investment Property' under Australian Accounting Standard AASB140. It applies to all managers and employees who actively manage the City's Investment Property or have responsibility for employees who actively manage the City's Investment Property.

Properties held by the City for its own operations/administration, community purposes or other specific strategic purposes are outside the scope of AASB140 and this Policy. Certain City-owned properties held to satisfy longer term strategic outcome generate rental income on commercial terms in the interim, but are not considered to be Investment Property, as the primary objective for holding the property is not for rental income or capital appreciation.

Definitions

The following definitions are referred to in this policy:

Term	Meaning
AREIT	An Australian Real Estate Investment Trust.
Due Diligence	An investigation of the legal, financial, environmental, and physical nature and characteristics including the entitlements and liabilities to and arising from, a real estate asset or assets, usually for acquisition or compliance purposes.

Term	Meaning
GLA	Gross Lettable Area - used for calculating tenancy areas in industrial and retail properties.
Investment Property	As defined by AASB140, property (land or a building, or part of a building, or both) held by an entity to earn rentals and/or for capital appreciation.
Market Value	Market value is the estimated amount for which an asset should exchange on the date of valuation between a willing buyer and a willing seller in an arm's length transaction and proper marketing, wherein the parties each act knowledgably, prudently and without compulsion.
Net Revenue	Gross Revenue less the costs associated with the source of revenue. In terms of rental property revenue, it is the total rent paid by a tenant to the real property owner less the amounts paid incurred as a consequence of owning the property.
NLA	Net Lettable Area - Used to calculate tenancy areas for office tenants.
Real Property	All the rights, interests, and benefits related to the ownership of real estate. Real property is a legal concept distinct from real estate which is the physical asset.
REIT	Real Estate Investment Trust - business trust or corporation that is usually traded publicly and manages a portfolio of real estate to earn profits for shareholders. Patterned after investment companies, REIT's make investments in a diverse array of real estate assets.
Yield	Measure of revenue on an investment, calculated by dividing the net rental revenue by the book value of the asset. It is usually the derived percentage return of a property assessed from the net revenue and the market value or price.
WALE	Weighted Average Lease Expiry - The weighted average lease term remaining to expire across a portfolio. WALE can be weighted by rental revenue or square meters.

Policy Statement

The City's objectives for the Investment Property portfolio are to:

- ensure a stable source of recurrent income and returns in the long term to enable the City to discharge its statutory functions.
- safeguard and enhance existing property revenue levels and achieve an optimal diversified total investment portfolio taking into account cash investments and Local Government regulatory restrictions on investment.
- optimise income from those assets and long term capital growth.
- undertake appropriate asset renewal and repositioning.
- grow property revenue to support long term financial stability; and
- further diversify and strengthen its revenue base.

These objectives are met through the prudent asset management of the Investment Property portfolio.

Investment property governance and responsibilities

The following governance mechanisms are in place to ensure adequate governance and allow transparent and clear performance measurement for the management, acquisition and disposal of the City's Investment Property:

- Asset Management
- Financial Planning and Cash-flow Management
- Delegated Authorities and Investment Responsibilities

- Land Classification of Investment Property and Accounting Treatment
- Investment Criteria
- Performance Reporting
- Audit Oversight
- Environmental and Social Responsibility

These governance mechanisms are explained in more detail below.

Asset Management of Investment Property

The City's aim in managing the Investment Property Portfolio is to strategically position individual properties to deliver optimal and sustainable investment returns. The City utilises a management model with asset managers overseeing the property and facilities management functions.

Financial planning and cash-flow management

The City's Long Term Financial Plan (the Plan) identifies the City's current and future financial capacity to continue delivering high quality services, facilities and infrastructure to the community while undertaking the initiatives and projects that will contribute toward the goals set out in the Community Strategic Plan, *Delivering Sustainable Sydney 2030-2050*.

Financial modelling that underpins the Plan assists to identify potential opportunities for strategically advantageous investments of accumulated cash balances into commercial property. Where allowances are made for future investment acquisitions, associated increases to rental income are also modelled in the Plan, underpinning the City's Net Operating Result in the long term.

Though the Plan may incorporate provisional allowances for investment property acquisitions, opportunities that result in specific development, acquisition and/or divestment recommendations are brought to Council individually as they arise, for review and consideration.

The City's Investment Policy (and Strategy) focuses on managing surplus funds in the short and medium term, setting parameters for fixed-term investments that aim to maximise interest returns whilst maintaining a maturity profile that allows the City to meet operational liquidity requirements. By contrast, the City's investments in property (as guided by this Policy) take a longer-term view, with the goal of achieving both additional stable rental returns and capital growth in asset values.

Monthly, quarterly and annual financial reporting are utilised by staff to monitor the City's returns from Investment Property, and performance against budget, throughout the year.

Use of Debt

The City presently has nil debt. Any Investment Property income generated through using debt, would be largely offset by the debt servicing costs. Unlike a commercial entity the City cannot derive any tax benefits from the use of debt financing.

The City may strategically use debt for Investment Property transactions. Use may be limited to concluding transactions where required, when permanent funding is imminent from a preferable source.

Delegated authorities and investment responsibilities

Delegations – Acquisition and Divestment

The elected Council is the decision maker in relation to all property acquisitions and divestments, including those related to Investment Property.

To achieve the best value for the City in property investments and divestments, recommendations will consider:

- forecast revenue and outgoings;
- property specific risks;

- tenancy covenant/s and rental returns;
- current and future capital works requirements;
- management requirements; and
- both opportunistic and synergistic acquisitions and disposals.

A minimum of two independent valuations supporting the acquisition/disposal are obtained to verify the appropriateness of the proposed purchase/disposal price.

Delegations – Management

Authority for the management of the City's Investment Property is delegated by Council to the Chief Executive Officer in accordance with the Local Government Act 1993 and the Delegations of Authority from Council to the CEO (as amended from time to time). Transactions which would exceed delegated authority are recommended to Council for decision.

Conflict of interest

Council officials are required to comply with the City's Code of Conduct and Conflicts of Interest Policy and must not engage in activities that would conflict with the proper execution and management of the City's Property Investments. Any real, perceived or potential conflicts of interest should be appropriately disclosed and managed in accordance with the City's Code of Conduct and conflicts of Interest policy.

Land Classification of Investment Property and Accounting Treatment

Land Classification of Investment Property (Local Government Act)

The City's Investment Properties are classified as "operational land" in accordance with Section 25 of the Local Government Act 1993. Under an operational classification, the City has the right to develop the land, create interests through leases, licences, easements and to dispose of the land.

Accounting Classification and Treatment of Investment Property (Australian Accounting Standards)

In accordance with accounting standard *AASB 140 – Investment Property*, the City defines Investment Property for accounting purposes as:

"Property (land or a building, or part of a building, or both) held by an entity to earn rentals and/or for capital appreciation"

In applying this definition, the primary purpose for holding the property is considered. Properties held by the City for its own operations and administration purposes, community purposes or other specific strategic purposes are outside of the scope of this definition and this Policy. Certain City-owned properties currently generate commercial rental income, but are not considered to be investment property, as the primary objective for holding the property is not for rental income or capital appreciation.

Properties may be recorded as investment property at the time of acquisition, or transferred into the asset class at a later date, should the strategy for the property change. Similarly, properties may be transferred out of Investment Property, in cases where the primary objective for holding the property is no longer to earn rental income and/or capital appreciation. Where it is proposed to change the accounting classification of a property, recommendations are reviewed and reported to Council via changes in the Annual Financial Statements.

The City's strategy for the acquisition and holding of Investment Property is to optimise the rental returns and to collect contractual cashflows from the City's Lessees (i.e. rent), rather than to regularly trade assets in order to make a profit.

Changes in Investment Property valuations are shown in the City's Income Statement in the annual financial statements as net gains or losses. These adjustments to book values are only realised at the time a property is sold/divested.

Investment criteria

This section sets out the criteria for investments to be considered for inclusion within the City's Investment Property at time of acquisition. It is noted that the criteria are considered as a whole and are not individually weighted.

Criteria**Scope**

Investments must comply with the legislative requirements and regulations relevant to the City's strategy for revenue growth.

Currency

Property Investments must be denominated in Australian Dollars.

Ownership

Real Property Investments must be held in the name of Council of the City of Sydney. The City does not invest in REIT's or AREIT's.

Synergy

Where applicable acquisition decisions will consider the synergistic benefit to existing assets owned by the City.

Type of Investments and Rental Returns

The City will invest in Property Investments which provides an appropriate commercial return and capital growth potential. The overall mix of assets will be diversified (including type, location and tenancy mix) to generate a balanced source of income which complements the existing investment assets.

Geographic Location

Property Investments are not restricted to the City of Sydney Local Government Area.

Development

The City may engage in development activities in order to generate an investment return. This may be through either new developments or refurbishing and repositioning existing Investment Property.

Market Value Range for Acquisition and Hurdle Rate

The City will target Property Investment with a market value range in the order of \$30m-\$150m. Investment returns, ie Net Yield, from new acquisitions should exceed a hurdle rate of 4% pa.

Performance Reporting

Investment performance is monitored against financial budgets for each Investment Property. The actual revenue received is compared to monthly and annual budgets for a financial year, to facilitate informed asset management decisions and to support accurate financial year forecasting. This enables the financial performance of each Investment Property to be quantified as well and the portfolio as a whole.

The City uses independent valuers to determine the "fair value" of each investment property annually. This allows capital performance to be compared with prior years.

The City will provide a Confidential annual report to Council summarizing its Investment Property performance (post receipt of the annual valuations) which will consider priorities and opportunities for the portfolio in addition to monitoring financial performance. The report to Council will include (but is not limited to):

- the total value of the Investment Property portfolio
- a complete schedule of all property investments within the portfolio
- the net income of the portfolio
- net income for the year versus budget
- the weighted average lease expiry (WALE)
- a summary of current vacancies
- major lease expiries
- commentary on portfolio performance and current property investment environment, and

- any other matters relevant to the portfolio as a whole.

Review of Investment Property Policy

The City will also undertake a review of its Investment Property Policy every four years from adoption. Should there be any significant legislative changes or if the property market conditions change to a degree that warrant an earlier examination, the Policy will be reviewed earlier and brought back to Council for consideration.

Audit Oversight

The City's external auditors will review the annual independent valuations of the City's Investment Property as part of the Annual Financial Reports.

The City's Internal Audit unit will also periodically review the adequacy of the Investment Property Policy and internal controls as part of its audit review program.

Environmental and Social Responsibility

For cash investments, subject to compliance with legislation and investment policy objectives and parameters, the City prefers investment securities and financial institutions that meet our socially responsible investments (SRI) criteria. The criteria for SRI are all preferred and not mandatory requirements.

This philosophical approach is mirrored within the Investment Property Policy when considering new lessees, acquisitions and divestments. Environmental and social responsibility are to be considered on the same basis as other risks and opportunities within the Investment Property Portfolio. The City's preference is to avoid transactions with lessees engaged in the socially and environmentally **harmful** activities listed below:

Environmentally **harmful** activities are considered to be:

- production of pollutants, toxins and greenhouse gases (coal, oil and gas)
- habitat destruction, especially destruction of forests and marine eco-systems.
- nuclear power
- uranium mining

Socially **harmful** activities are considered to be:

- abuse of Human Rights and Labour Rights
- involvement in bribery/corruption
- production or supply of armaments
- manufacture of alcohol, tobacco or gambling products

References

Laws and Standards
<ul style="list-style-type: none">• Australian Accounting Standards• Office of Local Government – Local Government Code of Accounting Practice & Financial Reporting• Office of Local Government Circulars• Local Government (General) Regulation 2021• Local Government Act 1993
Policies and Procedures
<ul style="list-style-type: none">• Investment Policy• Code of Conduct• Conflict of interest Policy• Disciplinary Policy & Procedures• Public Interest Disclosure Policy• Register of Delegations from Council to CEO• Register of Delegations from CEO to Directors and staff

Review period

This policy will be reviewed every four years.

Approval Status

The Council approved this policy on TBA

Approval History

Stage	Date	Comment	TRIM Reference
Investment Property Policy	TBA	Approved by Council	TBA

Ownership and approval

Responsibility	Role
Author	Development Manager
Owner	Chief Operating Officer
Endorser	Chief Executive Officer
Approver	City of Sydney Council