


Hope for the High Street

A new model for delivering change

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IN THIS REPORT WE OUTLINE OUR PROPOSALS FOR A NEW KIND OF PUBLIC-PRIVATE PARTNERSHIP ARRANGEMENT TO DELIVER SUSTAINABLE CHANGE TO BRITAIN'S FAILING TOWN CENTRES. THESE PROPOSALS BUILD ON THE FINDINGS OUTLINED IN OUR SEPTEMBER 2013 REPORT, HOPE FOR THE HIGH STREET.

WE BELIEVE THAT OUR PROPOSALS, IF SUCCESSFULLY IMPLEMENTED, WILL DELIVER POSITIVE BENEFITS TO EACH OF THE PRIMARY STAKEHOLDERS IN BRITAIN'S TOWN CENTRES: LANDLORDS, TENANTS, THE LOCAL AUTHORITY AND THE WIDER COMMUNITY.

BACKGROUND

In September 2013, we published a report, *Hope for the High Street*, which highlighted some of the obstacles needing to be overcome to regenerate our failing town centres. Much debate has taken place since that time, but no widely-supported solution to the challenges which we identified has yet emerged.

Town centres are essential hubs for our communities. There remains a strong demand for centrally located places where people can meet, communicate, eat, drink, work and spend time outside of the home. These functions are at the historic roots of all towns and cities. But their current formats – the way they look, the mix of uses, the functions which they offer and the way in which they are managed – require a new vision.

Among other factors, our September 2013 report highlighted:

- There are too many empty or underutilised properties which will struggle to continue as shops;
- The need for a broader use-mix beyond retail, given changing lifestyles and internet growth;
- The difficulty of bringing about change because of fragmented property ownerships;
- The need to engage with the four primary stakeholders – landlord, tenant, local authority and wider community; and
- Voluntary arrangements alone won't succeed without some kind of positive, public authority intervention.

At the core of many town centres, there is an area which continues to work well as a vibrant shopping and community meeting place, but it's smaller than it was. Food, beverage and entertainment uses have gradually displaced

fashion, banks and other services in the mix. However, beyond the core area, there are many under-occupied buildings and streets which no longer work as retail, resulting in neighbourhoods which are run-down, unappealing and, in some cases, unsafe. Some suburban locations and smaller towns provide more extreme examples of this failure

There has been much debate about the kind of Government intervention which would be most effective. Some have proposed blanket compulsory purchase; others have focused on incentives to promote more independent retailers back into the properties. We believe that a different, more joined-up and community-led approach is needed.

Since our paper was published, Government has introduced some welcome measures, including more flexible planning uses in town centres, an enhanced Business Improvement District (BID) model with greater business involvement, and potential reform to business rates, among other proposals. But the fundamental obstacles to lasting change, outlined above, remain with us, and the average level of shop vacancies remains at around 13%, with town centre vacancies approaching 28% in Newport, Stoke-on-Trent and Hartlepool at the end of 2014¹.

We concluded in our 2013 report that a new kind of public-private partnership arrangement was needed as a solution, both to deliver change and to successfully manage the town centre for the longer-term. In this report, we set out our proposed approach, which addresses most of the obstacles previously identified, and which we believe merits further, detailed exploration.

¹ BCSC/LDC Shopping Centre Vacancy Monitor (July 2015)/ LDC Vacancy Report, February 2015.

THE OBJECTIVE

Any solution must be able to harness the four primary constituencies of the town centre – landlords, tenants, the local authority and the wider community. They each have different, often conflicting, objectives, resources and time horizons. No-one seems content with the status quo. So any solution is therefore likely to result in winners and losers. But, on balance, the solution pursued should achieve an outcome which most would be prepared to accept, in order to bring about the prospect of a change for the better.

We set ourselves the objective of creating a partnership vehicle which can bring together the relevant property owners within a failing part of a town centre, which is also capable of being supported by the property occupiers, the local authority and the wider community, and which can provide a sustainable solution to the neighbourhood's longer-term management.

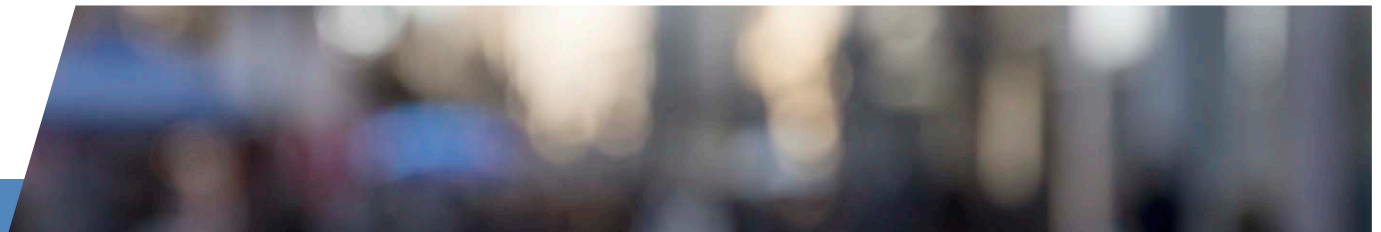
The vehicle would be created to tackle a defined part of the central area of a town, typically adjacent to the core retail area, which is demonstrably struggling. It might, for example, be close to the railway station or a significant civic building. In any event, in order to bring the area back to life, a more flexible mix of uses, including residential, would be needed, together with focused, expert management. The key elements are summarised in our **10-POINT PLAN**:

CORE PRINCIPLES OF THE PARTNERSHIP VEHICLE: A 10-POINT PLAN

- 1 Each property owner within the designated area will be encouraged to contribute his property ownership into the vehicle at its current market value, in return for a proportionate percentage financial interest in the vehicle's pooled portfolio.
- 2 Agreement would also be sought with the occupying tenants in each property, reflecting the current value of their remaining lease, as well as compensation for loss of earnings and disruption. Some of the occupiers, of course, may wish to re-locate within the new development.
- 3 The vehicle's design will draw upon appropriate features from the Business Improvement District (BID), Development Corporation and Elected Business Council models. The precise format needs to be further developed and will depend on local circumstances.
- 4 The vehicle will appoint its own experienced management team to work with the local authority to secure planning consent, raise funding, and deliver change. It will commission a development master plan for its designated regeneration area, ideally to include an appropriate housing product mix (private for sale, private for rent, and affordable), alongside a viable management and financing business plan.
- 5 The vehicle would be able to borrow (secured against the pooled assets) and to raise third party equity to finance its plan, to the extent that additional funding is needed to complete delivery of the project. Third party equity investors would expect to participate in any uplift in capital value and rental income resulting from the scheme, alongside the former property owners who contribute their property assets into the vehicle. All investors will need to be satisfied that the returns available justify the risks involved.



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- 6** To minimise the risk of the project being frustrated, a defined planning framework will be devised in conjunction with the local authority. Alternatively, the vehicle could be granted its own planning powers, within defined parameters.
- 7** The aim will be to secure voluntary agreement for participation by landowners and occupiers, by making a compelling and financially attractive case. Local authority-supported CPO powers will only be used as the ultimate back-stop, where voluntary agreement on properties essential to the project has not proved possible within a defined timetable. This last-resort approach will prevent ransom positions, and will provide a valuation and compensation benchmark to voluntary agreements.
- 8** Following completion of the development works, the vehicle will take responsibility for the long-term estate management of the new neighbourhood, funded by a combination of a service charge or business rate levy on the properties, and appropriate local authority support. Once income-producing, potential exit routes can be explored to provide liquidity to shareholders, for example by injecting long-term institutional investment, or the involvement of a REIT.
- 9** Public sector support (eg, in the form of cash, land, assets, borrowing support) will help the creation of these partnership vehicles, to accelerate change. Such support could be allocated by a competitive process.
- 10** As part of the package, the local authority would commit to improving the surrounding public realm, together with appropriate car parking and traffic management measures to ease congestion and improve longer-term sustainability. The new neighbourhood would become a catalyst for the wider regeneration of the town centre.

The above are, of course, generic principles. They will need to be customised to suit the specific circumstances of a specific town.

MANAGING DELIVERY

A suitable, public-private working group will be appointed in each location to develop an appropriate partnership vehicle and to project manage the concept. As indicated above, the precise design of the partnership vehicle will depend on local circumstances.

The recently enhanced BID format could be used as a potential enabling body for the concept in a particular location, since it offers a proven means of bringing together local business interests and the local authority in considering strategic changes to a town.

Elected Business Councils, already being introduced in some locations, may also have a part to play. Equally, the Development Corporation concept has been successfully used to deliver regeneration in many locations, and, typically, has had the advantage of its own planning powers.

KEY BENEFITS

This approach has the potential to bring significant benefits to each of the primary stakeholders within a town centre:

Local community – a stronger, better designed and managed, genuinely mixed-use town centre, more relevant to the needs of local people. Additional affordable homes within the town centre will benefit older citizens, as well as younger buyers, and the disadvantaged.

Landlords – landlords (and owner-occupiers) who participate in the partnership should see an uplift in the value of their property, greater liquidity and more sustainable investment growth.

Tenants/local businesses – the opportunity to be relocated to more profitable premises within the new development, or to exit an existing lease liability.

Local authority – pride in regenerating a challenged neighbourhood of the town, creating a more sustainable and relevant town centre, with ripple benefits to the rest of the urban area. A more attractive prospect for new inward investment.

Wider economy – stronger business rate revenues from higher business property values and a more robust economic base. Short-term concessions may be needed to support business re-location, and the change of use from business premises to residential use would switch business rates into council tax. But greater economic activity within the town would further strengthen other tax revenues, eg, VAT and Corporation Tax, as well as boosting job creation and local skills.

PILOT PROJECTS

A small number of suitable pilot projects should be worked up in conjunction with supportive local authorities, to test and demonstrate proof of concept in differing locations and circumstances, prior to a wider roll-out.

Appropriate private sector leadership and management of each pilot project would need to be selected, potentially by competition.



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KEY ISSUES FOR DISCUSSION



What kind of public-private vehicle should be used as the development/management entity? What should be its accountability?

The entity should be some form of partnership vehicle between the participating landowners, capable of acting not only as the developer of the project but also, on the project's completion, as the long-term investor and asset manager on behalf of its stakeholders, reporting to the sponsor.

To what degree should CPO powers be used?

Ideally, CPO should be a last resort, only to be used where voluntary agreement has not been possible. But it is unlikely that the site assembly will be possible without the prospect of it as leverage on value, and as protection against ransom positions. The way in which this is implemented will require very careful consideration, particularly where it affects local businesses which face closure.

The intention could be that CPO would only be invoked where the proposals for a scheme have met with a strong measure of support and commitment from most of the affected landlords and tenants, and have the backing of the local authority.

A BID which includes representatives of landowners and occupiers has a role to play in garnering interest in the initiative, in advance of any CPO, in order to demonstrate local political support, to flush out potentially reluctant landowners/tenants, and to indicate support for the use of CPO powers as a last resort, should this prove necessary.

The threat of CPO – if it is a real threat – should accelerate voluntary agreement, by providing a valuation benchmark, a ceiling on compensation and a backstop timetable for resolution.

What would the timetable for agreement/key project milestones be?

Conditional voluntary agreements could not be sustained indefinitely. Equally, landowners and existing business traders and other tenants need to know where they stand. The potential detrimental impact of 'planning blight' on property value would be an important driver of keeping to a relatively tight timetable. The deadline would potentially trigger CPO powers to secure any remaining essential property interests for which voluntary agreement had not proved possible. Key milestones would be:

- Designation of the area to be considered for a scheme
- Appointment of the vehicle's management team
- Creation of the masterplan vision and public consultation
- Initial agreements with landowners and tenants
- Grant of planning consent
- Finalisation of site assembly and development programme
- Confirmation of funding and commencement of development



Momentum would be important in reaching agreement with key participants and to sustaining confidence. A two to three year deadline from the appointment of the vehicle's management team on the back of an outline proposal, to finalising site assembly, planning and the development programme seems a realistic, though ambitious, target.

How would you overcome landlord and tenant agreement conditionality?

One approach to this dilemma could be to have a threshold of voluntary – albeit conditional – agreements beyond which CPO (or the threat of it) can be used as a lever to deliver the remainder. If uncommitted landowners know that the statutory value/compensation formula is the maximum they would achieve, were CPO to be invoked, there would be less incentive for them to hold out for more.

Some tenants may prefer to wait until the expiry of their lease (and some may have security of tenure rights). But possession of their property may be critical to delivering the desired physical alterations to the neighbourhood. Equally, the arrangement of buildings, their uses and the development's phasing would be vital to its commercial success.

Some tenants may be happy to go early. Others may wish to continue trading within the neighbourhood. Alternative accommodation (eg, a new shop within the development) could be offered, perhaps with a rent concession, together with compensation for temporary loss of trade. But ultimately there would need to be a CPO lever. If so, it would increase the possibility of being offered preferential terms (i.e. better than the

CPO limits) for an earlier, voluntary agreement, if it were commercially viable to do so.

The local authority may also be one of the landowners, so whilst it may have influence in the debate, it would need to be clearly understood how that influence is to be exercised.

Essentially, for both landlords and tenants, there should be a desire to be fair, whilst limiting the prospect of delaying tactics motivated by greed. Landlords may be able to take a more pragmatic investment view than tenants – particularly the smaller independent retailer whose livelihood may be at stake.

It should be recognised that, unless the scheme happens, everyone may become worse off as a result of continuing economic weakness and physical dilapidation, so ultimately interests need to be aligned.

What role should the local authority play within the vehicle, if any?

One option might be for the local authority to take control of the freehold interest of all of the designated land and to grant a long lease to the vehicle with a small share of the resulting income, in much the same way as often happens with the development of town centre shopping centres. This would give the local authority a long-term financial stake in the future of the scheme, provided the governance arrangements are not overly restrictive.

But participating landowners would need to be satisfied that they would not suffer loss of value as a result of the local authority taking a long-term property interest, i.e. their due proportion of the total completed

KEY ISSUES FOR DISCUSSION CONTINUED



development value would still exceed the present value of their specific property, allowing for all relevant costs, loss of rent etc.

A critical factor in the vehicle's masterplan for its designated area is that the vision needs to reflect local needs and be able to attract widespread community support.

If the vehicle were to be given its own planning powers, would the local authority have the right to approve the overriding vision?

It would be important that in matters of planning and development governance, potential tension between the local authority and the vehicle's management are avoided or mitigated. On this the success of the whole venture hangs, otherwise the key players and investors would have no confidence.

So, in selecting the initial pilot projects, it would be important to identify a supportive and experienced local authority, with an appropriate political mandate which could be anticipated for the most critical period of the project, as well as a vehicle management team capable of securing the local authority's confidence and trust.

How far would existing town centre stakeholders be affected by development risk?

Each landowner, by agreeing to participate in the scheme would effectively be putting their property value at risk. If the scheme on completion is not worth what it is expected to be worth, he may lose money in the short-term. There can be no guarantees of commercial success.

The tenants would not carry the same degree of development risk, to the extent that they are receiving compensation for vacating early, or their lease has come to an end, or they are going to be relocated to new premises within the new development at an agreed rent. However, it must be recognised that the position of the sole trader tenant, for whom the business premises represent their livelihood would require sensitive consideration. Relocation may be an option, but it would be regrettable if a specific occupier was able to hold to ransom the entire project for which there was widespread support. Hence the need for CPO powers as the ultimate back-stop.

So participating landlords would be putting their faith in the skill and integrity of the vehicle's management team, and whatever financial incentive that management team may have to deliver a successful result which has support. Hence the landlords would need to have full confidence in the process and the degree to which the inherent risks, including political interference, can be mitigated.



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KEY ISSUES FOR DISCUSSION CONTINUED



How would the project be funded? How far would third party support be necessary?

Ideally, the project would be self-sufficient financially, and the selection of the vehicle management team and the preparation of the masterplan vision should be able to demonstrate this. But there are two areas where third party support may be needed:

First, plan preparation and enabling costs (excluding land costs) for site assembly and other pre-development costs, including tenant compensation. This largely depends upon the timescale and perceived level of risk involved.

- Private sector developers are used to assembling sites over a period of years for large-scale development. But that is usually where the developer is in sole control of the scheme, or possibly working with a local authority partner, not where he has to piece together participations with other landowners, through an (as yet) untested arrangement.
- Developers are always conscious of the 'opportunity cost' of committing to a scheme for a period of time. Hence they would need to be reassured that an adequate level of profit could be made from the development phase, and that an adequate long-term return could be earned from the investment phase.
- The vehicle would have the reassurance of some pre-let agreements with tenants who are to be relocated, and with other occupiers, potentially including residential occupiers, who may be attracted to the scheme. But there would still be

likely to be some degree of speculation. The front-end costs would be speculative and unlikely to be fundable from banks, so these costs would require equity investment.

Second, there may be some projects which are deemed to be essential for wider socio-economic reasons because of the location of the town. There may be much-needed job creation opportunities capable of producing improved local authority revenues.

- In these locations, the economic viability of the project on a strict commercial basis may be weak. So support for the actual development costs – typically the land assembly – may be necessary in order to attract the more substantial private sector commitments.
- In these circumstances, some form of grant or tax incremental funding may be appropriate to help the scheme on its way.

It would be essential to formulate an indicative financial appraisal for a potential pilot project at an early stage, to test these funding challenges in more detail.

How would the long-term management of the redeveloped neighbourhood be approached?

The long-term management of the redeveloped neighbourhood would be critical to its commercial, social and financial success. The buildings and surrounding landscape would need to be well-maintained, the use and tenant mix kept relevant and refreshed as necessary, and a mutually supportive relationship with the rest of the town centre sustained.



What form should these long-term management arrangements take, who should be involved, and what relationship should there be between the ongoing management of the designated area and the wider management of the whole town centre?

The stakeholders in the vehicle may prefer the properties within their ownership to be managed independently, but would have regard to the wider plans for the town centre which the local authority may wish to see implemented. If the local authority were to own the freehold interest in the redeveloped neighbourhood, this may give them greater direct influence, but such influence would need to be exercised in a partnerly manner.

It is likely that the ongoing management of the completed properties within the scheme would be funded by some form of service charge levied by the vehicle on the occupiers, which would be reflected in the rent that is paid.

More substantial future capital expenditure (eg, on any substantial alterations to the properties) would be borne by the vehicle's then investors. However, grants might become available, if such alterations were for the wider benefit of the whole town centre, or in response to an adjoining or nearby development which the local authority might wish to encourage, but were uneconomic on their own.

Equally, it may be necessary for the local authority to make commitments to certain improvements to the areas surrounding the designated area, and to the wider town centre (eg, car parking, traffic management etc.) in order to give confidence to the potential participants in the vehicle to make further investment.

These issues beg the wider question of the longer-term management of town centres which are to be improved by the application of these arrangements.

What should the role of Central Government be?

Primary legislation should be a last resort, but Government would have an enabling role to play, particularly in supporting the creation of the partnership vehicle, encouraging the commitment from the local authority and engagement with the wider community.

If a BID is already in place, this could act as the initial enabler, but may itself lack all of the resources and powers required to promote the initial planning and viability assessment.

NEXT STEPS

In this report we have outlined our proposals for a new kind of public-private partnership arrangement to address the key issues which have to date prevented sustainable change to Britain's failing town centres. The realisation of these proposals would potentially provide lasting improvement and significant economic impact, re-vitalising the town centre as the hub of the local community, and a place where people want to be.

The proposals should be implementable at no net cost to the Exchequer. In practice, we anticipate, the Exchequer should ultimately make a net gain from the lasting impact on the town centre's local economy.

This report represents the first stage in a much longer journey to bring the initiative to life. We see the key next steps as including:

- Government should be encouraged to respond and to consider these proposals in more detail, potentially with the help of a suitably qualified public-private working group. Relevant industry and community bodies will need to be consulted and commercial market soundings taken.
- Review the other initiatives which have been tabled to date, in the light of now greater understanding of the issues and the mechanisms which are most needed to deliver change, in order to ensure that the preferred solution design is the most relevant and capable of being delivered successfully.
- A suitable pilot project or projects should be identified and planned, in consultation with the relevant local authority, to include a properly prepared business case, financial appraisal and an assessment of the expected socio-economic impact within the local area.
- Appropriate public sector support mechanisms, whether potentially of assets, financing support or grants (including relevant competitive allocation processes, if necessary)

should be explored and the principles agreed upon, with appropriate leadership and accountability being put in place.

- An indicative timetable and programme plan for the initial pilot scheme(s) should be prepared, together with a pipeline of potential follow-on projects, in order to begin to demonstrate the overall 'size of the prize', not least in terms of socio-economic benefit, additional housing, employment and tax revenues.

As a result, a much clearer understanding will emerge of:

- The generic principles of the partnership design and sponsorship;
- The workability of voluntary agreements between landowners and occupiers;
- The degree of public sector support, in some shape or form, which is needed to deliver the initial projects, and how this should be provided and managed;
- Specific pilot projects to prove the concept and the preferred implementation process; and
- A longer pipeline of potential projects for which there is market appetite, subject to a detailed business case;
- Other, alternative solutions to tackle the critical issues, as a result of wider consultation and debate.

KPMG INTENDS TO PLAY AN ACTIVE PART IN SUPPORTING THE FURTHER DEVELOPMENT AND PROMOTION OF THESE AND OTHER IDEAS, IN ORDER TO DELIVER THE SUCCESSFUL REGENERATION OF BRITAIN'S TOWN CENTRES.

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