Written Evidence – The British Property Federation (PTC0015)

Introduction

1. The British Property Federation (BPF) represents the real estate sector – an industry which contributed more than £115bn to the UK economy in 2019 and supported more than 2.4 million jobs[1]. We promote the interests of those with a stake in the UK built environment, and our membership comprises a broad range of owners, managers and developers of real estate as well as those who support them. Their investments help drive the UK's economic success; provide essential infrastructure and create great places where people can live, work and relax.

2. The Covid-19 pandemic and the Government's response to it has created unprecedented challenges whose impact will be felt for some considerable time to come. Property owners have been far from immune to this as many of their occupiers have either been prevented from trading or forced to trade at significantly lower than normal capacity due to lockdowns and other restrictions. This has led to much lower rent and service charge collection rates, particularly in the retail, leisure and hospitality sectors. We estimate the rent collection shortfall since March 2020 across all different types of commercial property currently stands at well over £6bn.

3. In addition, the way in which Covid-19 has accelerated an existing trend towards a greater share of retail spend being online, means both that valuations of retail property have fallen dramatically in many areas and that there is a significant reduction in demand for the physical retail space that has traditionally formed the backbone of town and city centres and which will need to be re-purposed to other uses to reinvigorate town and city centres across the country.

4. Covid-19 has also accelerated changes to the office workplace. While there was a pre-pandemic move towards greater use of shared space, shorter, more flexible office leases and people working from places other than their office, this trend was developing slowly and according to ONS data from 2018, only 14% of people "mainly" worked from their homes.[2]

5. It is hard to know at this stage the extent to which the pandemic will have permanently changed where and how people (and office workers in particular) work, but it seems likely that a hybrid approach to working is likely to be far more widespread than before the pandemic. The consequent impact however is hard to predict – on the one hand businesses may consider downsizing their premises to reflect having fewer people in the office at one time. On the other hand, in a recent survey we carried out of large office occupiers, 45% of respondents reported a desire for more adaptable open space and 33% wanted more in-house amenities, both of which suggest that the office of the future may be based on a requirement for more space per person overall than prior to the pandemic.

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[1] https://bpf.org.uk/our-work/consultation-responses/uk-commercial-real-estate-economic-footprint/
[2] Homeworkers by UK region, 2008 compared to 2018

6. In addition, the development of new office buildings has since the 2008-10 global financial crisis been at below long-term historical levels and has lagged growth in demand for that space, resulting in a gradual tightening of availability and an increase in rents and office property values.[3,4] As a result, the impact of downward pressure on office rents may be less pronounced than might be expected.

Long term implications for town and city centres

7. The way in which we use much of the built environment in urban centres is changing and those changes have been accelerated by the Covid-19 pandemic in a way which is placing property owners who not only manage the existing fabric of our town centres but are the source of the future investment needed to reinvigorate them under acute stress as a long-term industry seeks to adapt to massive change.

8. There are clear opportunities – for example to match the need for well-located good quality homes to redundant space in our town centres. Our future town and city centres will continue to have shops, bars and restaurants but will also be a much more eclectic mix of buildings - homes, offices, doctors' and dentists' surgeries, community hubs etc.

9. However there are a number of issues which we believe need to be addressed if the necessary investment is going to be secured to ensure that the Government is going to be able to deliver its levelling up agenda and ensure that inequalities are not exacerbated rather than tackled.

Partnership working – Town Centre Investment Zones

10. To adapt effectively to changing times, places must have a long-term vision for their area that commands strong support from a range of local stakeholders, including local authorities, property owners, community organisations and businesses. However, given the different time horizons and short term pressures each of these stakeholders faces, in practice it can be very difficult to align incentives.

11. To encourage this partnership working, we recommend that the Government introduces Town Centre Investment Zones (TCIZs). In a similar vein to Enterprise Zones, these would be geographically defined areas within which relevant local stakeholders are given additional powers and/or access to additional expertise to support town centre adaptation.

12. However, TCIZ status would only be granted where an area can demonstrate that is has a clear long-term vision and strong local backing. In principle, TCIZs are not that different from Town Deals, but their focus is on enhanced and ongoing local capability rather than one-off allocations of money.

13. The additional policy levers granted under TCIZs could include:

[3] Savills - Spotlight: UK Regional Office Market Report, September 2020
[4] Savills – Development across Central London, February 2020

13.1. **Tax incentives**, such as increased business rates retention for the local authority or the ability for developers to defer National Levy or CIL payments;

13.2. **Planning support**, such as access to a national funding pool for ensuring enhanced planning skills and capabilities;

13.3. **Natural environment measures**, such as assistance to introduce a Clean Air Zone or priority access to Government funding for electric vehicle charge points; and

13.4. Facilitation of **pooled property investment**, which would involve property owners transferring their individual properties into a joint investment vehicle in exchange for a share in that vehicle without triggering capital gains tax or SDLT liabilities.

Viability of town centre investment

14. The UK has some of the largest regional disparities of any major developed economy. In the property investment and development market, these imbalances manifest through relative levels of rent and land value in different areas. For instance, office rents in London are more than twice what they are in Manchester or Birmingham. The same is the case for prime industrial/logistics and retail property.

15. The differential between large cities and smaller cities and towns is even more marked, with commercial rents and land values being lower in smaller cities and towns than in the UK's Core Cities. This means that across swathes of the UK the viability of any new development or regeneration scheme, tends to be marginal at best. In parts of the country, there are many empty commercial properties for which there is no alternative use that it is commercially viable to deliver.

16. These issues will only be tackled with the public and private sectors working together and finding innovative new partnerships to create investible propositions to attract private capital. The most natural source of private sector funding is 'patient capital' – the institutions such as pensions and investment funds that are seeking to allocate large amounts of capital to deliver a secure long-term income stream they can deploy to match against their liabilities.

17. There are a number of factors however that are putting at risk the appetite of such funds to deploy their capital to real estate:

17.1. **Commercial property rent moratoriums**: at the start of the pandemic, the Government restricted a range of property owners' contractual and legislative rights.[5] While the measures were primarily introduced with vulnerable retail, leisure and hospitality occupiers in mind, they apply to all commercial property leases. The property sector was the only sector whose interests were actively legislated against as part of the Government's response to Covid-19.

[5] Namely the right to evict, to petition a court for a winding up order and the ability to use Commercial Rent Arrears Recovery.

17.2. The Government has recently announced a further extension of these restrictions until March 2022. In addition, it is proposing to by-pass the normal resolution path for contract disputes through the Courts and introduce a new binding arbitration scheme for lease disputes linked to rental debt which will be subject to political rather than legal guidelines.

17.3. The Government is proposing these measures notwithstanding that large parts of the tenant base has been unaffected in its ability to trade by public health restrictions, and that BPF research shows that over three quarters of property owners and their tenants have already reached agreement on how to manage and share the impact of Covid-19. Taken together (and with the issues relating to the UK's insolvency regime discussed below) they introduce a significant new element of political risk into UK property investment which undermines the security of income that long-term funds are looking for and potentially makes the investment which will be essential to the physical infrastructure of healthy, more productive and prosperous communities unviable.

17.4. **The UK insolvency regime:** The UK's insolvency framework is recognised for its flexibility and low cost. However, in recent years this flexibility has allowed for an abuse of the Company Voluntary Arrangement (CVA) and very recently, Restructuring Plan (RP) processes that is directly discriminating against property owners as a creditor class and again risks seriously undermining the value and attractiveness to investors of commercial property.

17.5. We support a business rescue culture and we recognise that CVAs and RPs can be useful tools for restructuring when used correctly. We are however extremely concerned by the 'Landlord CVAs' that have been undertaken by major high-street firms over the past decade and very recent 'Landlord RPs'.

17.6. In these property owners are often the only compromised creditors but the CVA is approved by other, largely (sometimes wholly) unaffected creditors. This is possible because the rules allow voting structures to be set up in such a way as to minimise the influence of property owners. While property owners should be an important economic partner to businesses in trouble, CVAs and RPs allow those businesses to treat property owners as "lenders of first resort" without any incentive to meaningfully engage with them to seek mutually beneficial solutions.

17.7. This abuse of the insolvency rules has impacts stretching far beyond property owners themselves: They

- make it riskier to invest in town and city centres, by undermining security of income for property investors;
- distort competition and favour poorly-run businesses, at the expense of better-run or less opportunistic competitors;
- transfer value from UK pensioners and savers to businesses and their (often High Net Worth or private equity) shareholders; and

- undermine property contracts, hurting the UK's reputation among international investors.

17.8. We recommend to the Committee that the Government takes urgent action to work with the property sector to create an investment plan for levelling up and addressing geographical inequalities across the UK which mitigates the impacts of these two measures and restores confidence to the regional UK property investment market.

Business rates

17.9. The issues with the current business rates system are well-rehearsed and not repeated here. However we would ask the Committee to note two issues in particular and to urge the Government to take account of them when it concludes its fundamental review later this year:

17.9.1. The level of business rates is unsustainable and unresponsive to economic conditions – meaning that they are often particularly punitive in areas of greater inequality. This needs to be addressed both by a reduction in the level of business rates and by a more responsive and more frequent valuations system;

17.9.2. The levying of business rates on property owners with vacant properties is a huge disincentive to speculative development yet it is this investment which will be needed if inequalities are to be addressed and investment does not just follow existing success and demand.

1 July 2021