Leases and town centre regeneration

by Emma Stephen,
partner, commercial property,
Stronachs LLP

THE pandemic has ripped through town centres leaving boarded up shop fronts, dilapidated buildings and deserted high streets in its wake. The trend away from in-person to online shopping and the ramifications of that change are becoming apparent.

Despite the convenience of online shopping there remains a desire to have physical shops, as well as functional and vibrant town centres. As we move away from CV19 restrictions managing this juxtaposition shall be a primary concern of local authorities, property investors, retailers and other business owners dependant on footfall.

The reason behind the demise of the high street is not solely CV19 but reports suggest that it has sped up the process of digitisation of shopping by at least five years. A common complaint is that Union Street in Aberdeen is a shadow of its former self. The pavements are dirty and congested with street furniture and the buildings look dilapidated. Perhaps proposals to pedestrianise parts of Union Street shall have a positive impact but they are unlikely to be successful in isolation.

There are many angles to look at this problem from including planning, taxation, investment, unit size, new shopping centres etc. We shall briefly look at the impact leasing has and how landlords can play their part in regeneration.

Most retail premises will be owned by a commercial landlord and leased to retail businesses. These leases would have historically been long term (upwards of 10 years) and on an FRI (full repairing and insuring) basis. Meaning the tenant is responsible for all repairs as well as paying rent. The landlord collects the rent and has little else to do with the premises. This model works well when tenants' businesses are successful and allows them to invest their capital in the business and not property. However, it is not so effective when the tenants' margins are constantly being squeezed, particularly as in-person shopping is more expensive for retailers.

In this climate tenants struggle to comply with the repairing obligations in their leases (dilapidations costs). In the event of the tenant going into administration or liquidation the landlord can be left with buildings with outstanding dilapidations where no payment shall be forthcoming from the tenant. Even if a dilapidations payment is made (in lieu of works being carried out) the landlord is entitled to keep these sums and not reinvest them in the property if they want to.

At the end of a lease the landlord can decide to invest in upgrading the property or to seek to rent the property in its current condition but at reduced rent (if they can find a new tenant at all). This is frequently done by a lease where the repairing obligation of the tenant is limited by a schedule of condition (a photographic record of the condition of the property). In these circumstances there will be no obligation on either the landlord or the tenant to improve the property and this can lead to a general deterioration of the area.

These issues are not the fault of local authorities but rather the normal leasing market practices. In the challenging conditions both landlords and tenants find themselves in there will need to be a recognition of the importance of investment in properties to ensure that town centres do not deteriorate further. Although only part of a wider picture, ensuring the reasonable condition of these retail properties is a crucial part of city centre regeneration. Aesthetically pleasing streetscapes will improve footfall, which shall in turn improve occupation levels, rents and property values in the long run.