House of Commons Treasury Select Committee

The impact of Business Rates on business inquiry

Submission by British BIDs

Executive Summary

- There are some fundamental problems in the Business Rates system. The last Business rates review followed a seven-year gap and came into effect last year. It made some very major changes to the cost of businesses; these changes vary greatly across the country, are opaque, are very different for different types of business, are not easily open to appeal, penalise innovation and are difficult for future planning.
- Data from individual businesses show that many have ceased trading; six small independent businesses in one small market town show a 77.3% business rate increase for the businesses as a group and a 139% increase for one business in the past year.
- Business rates are a penalty for creative and innovative businesses, who are penalised for putting more back into their business, with the benefits going to the owner who may be very distant.
- An alternative valuation method -'receipts & expenditure' - is used very often in the public house and food and beverage industries and is a totally different model from the traditional property tax and is applied unfairly.
- While business rates have risen significantly as the proportion of council tax, the asset base of commercial property has a value just one sixth of that of residential property. It is of note that the highest domestic G band annual Council Tax for Kensington and Chelsea is only £2246, based on its capital value in 1991.
- Business rates give a major competitive advantage to online businesses. They generally have property in locations with a low rent per square foot, with a low rateable value and yet have a much higher turnover and compete with 'bricks and mortar' businesses unfairly across the country. Thus, 'bricks and mortar' businesses are being heavily penalised at a time when the role of the high street, experiential retail and curated public space are all being explored and celebrated by local and central government.
- The Appeals system has failed under the pressure and attempts to reform it have mostly been ineffective and the new appeals system is designed to make appealing more difficult.
- Localisation of business rates, more frequent valuations, the ability to better capture the benefits of growth and reducing the inequity between high street and online retailers could all radically improve the existing business rates system in the short to medium term.
- A Local sales tax (implemented with a VAT system) emerges as a potential replacement for business rates, both in terms of working for business and local government.

British BIDs

1. This submission is from British BIDs (Bb) a well-established membership organisation focused on serving the 305 Business Improvement Districts in the British Isles. Bb provides advice, training, conferences, research, accreditation, access to a government loan fund, ballot support, products and services. We have over members across the sector and we have a team of BID practitioners providing information advice and guidance to BIDs across the country.

2. A Business Improvement District (BID) is a business-led and business funded body formed to improve a defined commercial area. The benefits of BIDs are wide-ranging and allow businesses to decide and direct what they want in their area, be represented and have a strong voice in issues affecting their trading area. The BID collects a levy, the money from which is ring-fenced for use only in the BID area. This results in increased footfall and spend, improved staff retention, reduced business costs, and enhanced marketing and promotion activities in the area. A BID is a commercial company, with a Board, that enables businesses to work together with other stakeholders to plan infrastructure, work on pollution, improve traffic flow and movement, give guidance in place shaping vision activities, have powerful networking opportunities with neighbouring businesses, and allow assistance in dealing with the Council, Police and other public bodies.

3. The BID mechanism allows for a large degree of flexibility and as a result BIDs vary in shape and size. The average size of a BID is 300-400 business premises, with some of the smallest having fewer than 50 premises and the largest at over 1,000. Annual spending is typically £200,000-£600,000 but can be as little as £50,000 per annum and as much as £2 million. Currently there are over 120,000 businesses across the country in a BID

4. This submission contains feedback from these members, identifies what some of the current problems are, and proposes some new plans that might help.

The Issues

5. Business rates are clearly a very major issue for BIDs and their members. We had been looking forward to the broad outline of the way both business rates and fairer funding scheme might work, and we understood this would coincide with the spending review that is expected in 2019. The previous Chancellor's commitment to allow local government to retain all business rates by 2020 was delayed when the enabling legislation fell at the end of the last Parliament. The current Government has said it remains committed to the policy on a longer timeframe but is currently only rolling out business rate retention on a pilot basis. The Chancellor has announced that revaluations will take place every three years, but only from 2020 and with no timeframe for moving towards annual revaluations.

6. What many of our members are concerned about is an apparent lack of long-term planning for the future of local government funding. Short term, we know about the changes in business rates and the projections of council tax revenue; however, there is apparently nothing being developed that addresses the disconnect between the funding envelope and the increase in demand for council services.

7. The retention of revenue from the business rates system by local authorities in the future results in many local authorities actively looking for ways to increase rates in their areas, but also raises budgeting problems, as they will have to pick up the bill for refunds after successful appeals, which could take several years to come to fruition.

8. We fully understand that business rates are a property tax, levied on business properties on the basis of their rateable value and the national multiplier. We also understand that the advantages of such a tax are that it is very stable, that because it is linked to property is difficult to avoid and that it has a very important link between raising revenue from a business in a particular locality and local authority and the purposes to which that tax is being put to use. However, we do believe that this is still flawed by the small amount retained in reality at the local level.

9. We also recognise that business rates raise almost £30bn a year but that, as with any form of tax, there must be a basic right for a taxpayer to ensure they are paying the correct amount. This is facilitated by the ability to appeal against a rateable value

10. The business rates system has been reliable and logical for many years, but as the rate in the pound multiplier has increased (34.8p in 1990 to between 46.6p and 50.4p in 2017), the pressure on the system has intensified as it is often business critical to seek to reduce the rates liability to a more reasonable level.

11. The recent Select Committee report on the High Streets and Town Centres in 2030 https://publications.parliament.uk/pa/cm201719/cmselect/cmcomloc/1010/1010.pdf felt that a property-based tax was no longer fit for purpose; “It [...] was designed and developed in the past.”

12. BIDs and their members across the country similarly have that view and submit in this paper some case study evidence, some research-based options and a request that members of the Select Committee visit some business communities that can offer clear evidence of the problems. Our National BID Advisory Board members include New West End BID, Southbank BID, Worcester BID, Hammersmith BID and Winchester BID. All are keen to engage with the Select Committee, feel that the Select Committee might gain much from visiting a BID and have submitted evidence to this report.

The Problems

13. Feedback from our members suggests that there are some fundamental problems. The last Business rates review followed a seven-year gap and came into effect last year. It made some very major changes to the cost of businesses; these changes vary greatly across the country, are opaque, are very different for different type of business, are not easily open to appeal, penalise innovation and are difficult for future planning.

14. The Bb National Survey last year https://britishbids.info/publications/national-bid-survey-2018 suggested that whilst some business communities had a net reduction of some 22% in their business rates other business communities saw an average increase of 16.8%.

Table 1 Average Business rate changes in BIDs 2018

Reduction	22.43%
Increase	16.82%
Average Net change in business rates	0.21%

15. Whilst we appreciate that the net change appears small, matching the government's desire for 'fiscal neutrality,' the variations across regions and at the individual business level are at times huge and unexpected.

16. Data from individual businesses show that many have ceased trading and a case study spread sheet from six small independent businesses in one small market town shows a 77.3% increase for the businesses as a group and a 139% increase for one unit in the past year. Despite the short-term rates relief, this is unsustainable into the future and two units have now closed.

Table 2 Business rates growth example for six businesses

2010 RV	NEW 2017 RV	% CHANGE IN RV	2016/17 RATES PAYABLE	2017/18 RATES PAYABLE	2018/19 RATES PAYABLE	2019/20 RATES PAYABLE
£24,500	£43,500	77.55%	£11,858	£13,607	£17,033	£20,920
£20,750	£37,000	78.31%	£10,043	£11,524	£14,428	£17,720
£25,000	£59,900	139.60%	£12,100	£14,663	£17,583	£21,548
£13,250	£30,500	130.19%	£6,413	£7,359	£9,303	£11,404
£19,000	£35,000	84.21%	£9,196	£10,552	£13,226	£16,240
£35,500	£38,800	9.30%	£17,644	£18,081	£18,623	£19,182
£138,000	£244,700	77.32%	£67,254	£75,787	£90,196	£107,015

Tenants, owners and innovation

17. Business rates are a cost to the tenant rather than the freeholder owner, and they become a penalty for innovative and creative solutions to refurbishment and building design, particularly for the independent sector. Many BID members feel that this is a penalty for creative and innovative businesses, who are penalised for putting more back into their business, which means any benefits go solely to the owner, who may be very distant.

18. Thus, the system does not encourage businesses to invest in their property to the extent that improvements lead to a rates rise. As the HCLG select committee (op cit) noted last

year: “If you make a capital investment in a pub, you immediately have a ratings officer standing on your doorstep wanting to put up your business rates.”

Receipts & expenditure methodology for public houses

19. Where rents aren’t common or are not at open market levels, an alternative valuation method is the ‘receipts & expenditure’ method, which seeks to identify how much rent could be paid out of the profits of the business. This is used very often in the public house and food and beverage industries and is a totally different model from the traditional property tax and is thus unfair

20. Whilst we have seen turnovers increase over the 7 years between valuation dates, this is often achieved by increased costs, whether it be the cost of goods or management costs required to hit the turnover levels. The Valuation Office does not necessarily have either the time or the ability to look deeper into those costs and therefore the ‘shortcut’ valuation method is often misapplied.

21. The leisure sector has generally been hit hard by the new 2017 revaluation, particularly in the larger towns and cities as the rateable values have increased at a higher level than other commercial properties in those locations

Residential council tax

22. The focus on commercial property taxes in the UK is also particularly challenging.
    - In 2017-18 local authorities collected a total of £28.0 billion in council tax,
    - In 2017-18 authorities collected a total of £24.5 billion in non-domestic rates.

23. Research by the British Property Federation https://www.bpf.org.uk/sites/default/files/resources/Who%20pays%20business%20rates%20research%20%28BPF-BCO-BCSC%29%20Final.pdf shows that in 2015, while business rates rose about 80 percent as much as the tax take of council tax, the asset base of commercial property has a value just one sixth of that of residential property.

24. This appears iniquitous and suggests a very skewed taxation base. It is of note that the highest G band annual Council Tax rate for Kensington and Chelsea is only £2246, based on its capital value in 1991.

Online and e-commerce business

25. In this online world business rates give a major competitive advantage to online businesses. They generally have property in locations with a low rent per square foot, with a low rateable value and yet have a much higher turnover and compete with ‘bricks and mortar’ businesses unfairly across the country.

26. Business rates tend to strengthen the competitive advantage of online retailers as well as the historical cost base of high street shops. The typical London shop is facing a 14 per cent rise in rates, and the average shop across the country a 8.5 percent rise, while online retailers operating from out-of-town warehouses will only pay an extra 2 per cent.

27. ‘Bricks and mortar’ businesses are being heavily penalised at a time when the role of the high street, experiential retail and curated public space are all being explored and celebrated by local and central government.

Appeals

28. The Appeals system has failed under the pressure and attempts to reform it have mostly been ineffective. There are over 275,000 appeals still outstanding from the 2010 revaluation and under the new ‘check, challenge, appeal’ appeals system, that is entirely online, it is not possible to initiate an appeal as the software is not working or available.

29. We believe that the new appeals system is designed to make appealing more difficult. The justification seems to be that more small businesses than ever are exempt from rates now, and all other businesses can afford to not only pay the full (and often incorrect amounts) in the first place, and also to pay for professional advisors to navigate the complex system. This cannot be right.

Some short-term proposals

30. Work by the New West End Company BID, Arup and the LSE (Tax reform technical study. Report for New West End Company, July 2018, Arup) https://cdn.britishbids.info/publications/20180705_NWEC_Tax_Reform_Summary_Report-ZW.pdf?mtime=20180807090204 has identified eight key measures which can improve the design of the tax to support economic growth and provide a fundamentally better source of local tax revenues in the short term
31. Make the system more flexible and responsive
    - Make property value more frequent to make it better aligned to market prices
    - Remove the cap on total business rates yield
    - Devolve Valuation Office Agencies
32. Reward growth of value and floorspace
    - Capture value growth as financial incentive
33. Prevent London’s distortion of national valuations
    - De-couple London’s business rates system from the rest of the country
34. Share rewards and risks within functional economic areas
    - Pooling business rates across functional economic areas (city-regions, devolved authorities)
35. Devolve decision making
    - Devolution of further responsibilities and decision-making to adapt the tax system to respond to local economies and politically accountable decisions, including:
        i. Ability to set their own rates
        ii. Resets and funding baselines
        iii. Needs Assessment
        iv. Qualification criteria and thresholds for reliefs.
36. Adapt equity to modern business models
    - Revise rateable value assessment for online retailers to reduce equity gap

37. All of these propositions have been lobbied for by the London Finance Commission, supported by think tanks (e.g. Centre for Cities, Institute for Fiscal Studies) and are

broadly aligned with Treasury's views on the topic. In the short-term wholesale reform of the business rates system is unlikely, particularly for changes that require legislation, as the Government remains focused on other priorities.

38. The changes to the business rates system suggested could dramatically improve the business rates system in the short to medium term, and could achieve greater benefits, equity and transparency for both businesses and local government funding. Thus, the localisation of business rates, more frequent valuations, the ability to better capture the benefits of growth and reducing the inequity between high street and online retailers could all radically improve the existing business rates system.

Some proposals for full-scale reform

39. These recommendations should be considered alongside proposals for full-scale reform. However, a transformational solution could be envisaged to replace business rates.

40. The UK's over-reliance on property taxes in general and more specifically for funding local government creates substantial inefficiencies in the development of commercial property, the commercial decisions of businesses and the planning decisions of local government. Replacing business rates with a local sales tax could create a system which performs well with regards to tenets of good tax design: ease of collection, ability to fund local services, mitigate against avoidance, equity, ability to pay and the economic impact.

41. Arup was commissioned by the New West End Company to assess two alternative taxes—a turnover tax and a local sales tax—as alternatives to business rates, calling on precedents from other countries.

42. Local sales tax (implemented with a VAT system) emerges as a potential replacement for business rates, both in terms of working for business and local government. This is true so long as the local sales tax is implemented on the same tax base as business rates, not just retailers. It can arguably tackle the challenges of a 21stCentury economy, taking into account the changing nature of high streets, retail and online-businesses.

43. A local sales tax would link business performance to tax liability more effectively, and it could be operated within the VAT system as a tax at final sale. Looking forward, the feasibility of a sales tax and its prospective benefits present a real opportunity to make business taxes work better for government and the British economy.

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