Business Rates Review: Call for Evidence

London First "Improving the business rates system: tranche 2 response" – October 2020

1. Our Organisation

London First is a business campaigning group with the mission to make London the best city in the world in which to do business, for the benefit of the whole UK. We convene and mobilise business leaders to tackle the key challenges facing our capital. We are made up of around 200 leading employers across a wide range of sectors, overseen by a non-executive board of influential business leaders.

2. Executive summary

- We restate our call on the Government to support business through the pandemic by extending the 100% relief for businesses in hospitality, leisure and retail for 12 months beyond April 2021; and extending such support to other sectors similarly hit, such as aviation.
- Given the scale and unprecedented nature of the pandemic the recovery is expected to take several years, therefore business rates simply will not – and cannot be expected to -- deliver their historic stable yield.
- Priorities for reform should aim better to align the system to actual market conditions, incentivise business investment to accelerate the UK's transition to a net zero carbon economy, and remove the regional inequalities in the current system.
- Annual revaluations would allow rateable values to directly track market levels and remove the mismatch between rateable value and rental levels that have been experienced in recent years. Shorter revaluation periods would also remove the need for a transitional scheme.
- As the UK accelerates its transition to a net zero carbon economy it is imperative that any barriers to investment in the required technology are removed. There are a number of anomalies, discussed below, within the existing regulations which require review.
- For the remainder of the 2017 revaluation period (up to 2022/23) and thereafter, the government should freeze the Uniform Business Rate, and therefore not continue to increase it in line with CPI. This would break the link with inflation and mean that yield would fluctuate directly in line with changes in the property rental values.

3. Introduction

In our response to Tranche 1 we focused on short-term measures that could be considered. We would therefore restate our call on the Government to support business through the pandemic:

- The government should extend the business rates holiday from April 2021 for 12 months and review the need for any further continuation in 2022/23 in the light of the state of the economy nearer the time.

- In addition to supporting the hospitality, leisure and retail sector, the Government should consider other sectors were support is equally needed. In particular, the aviation sector has experienced similar catastrophic impacts on footfall through lockdown and continued quarantine rules. The Scottish Government has recognised this and included airports in their rates holiday.

Given the scale and unprecedented nature of the pandemic the recovery is expected to take several years, therefore business rates simply will not – and cannot be expected to -- deliver their historic stable yield at the next revaluation, or indeed 2024.

Priorities for reform should aim to better align the system to actual market conditions, incentivise business investment in accelerate the UK's transition to a net zero carbon economy, and remove the regional inequalities in the current system.

More technically detailed responses have been submitted by our individual members.

4. Aligning business rates to actual market conditions - valuations and transitional relief

One of our key criticisms of the business rates system is that it does not respond sufficiently quickly to changes in the economy, trading conditions and property rental values. We support frequent revaluations coupled with a removal of the requirement for revaluations to be fiscally neutral (see later), through which businesses will experience changes in rates bills which more accurately reflect updated property rental values.

The Government committed to a move to three yearly revaluations in response to previous reviews as announced by Philip Hammond in the 2017 Autumn Budget and later confirmed in the 2018 Spring Statement and subsequent draft legislation at which stage it was proposed the period of the 2017 Revaluation would be reduced from five to four years.

We would consider a move to a three yearly cycle to be achievable in the short term and assuming a revaluation as recently announced from April 2023 we expect that the following subsequent revaluation should be no later than April 2026.

Looking to the future we believe that the aspiration should be that revaluations be carried out on an annual basis. Annual revaluations would allow rateable values to directly track market levels and remove the mismatch between rateable value and rental levels that have been experienced in recent years. Shorter revaluation periods would also remove the need for a transitional scheme.

5. Accelerating investment in the net zero carbon economy - plant and machinery and investment

Net Zero is a statutory target set by the Climate Change Act 2008 for a 100% reduction of UK greenhouse gas emissions by 2050. As the UK accelerates its transition to a net zero carbon economy it is imperative that any barriers to investment in the required technology are removed.

There are several anomalies within the existing regulations which require review. For example, solar PV panels and wind turbines are generally not rateable but are if installed by a ratepayer for their own consumption. This can increase business rates liability by a factor of at least 10 times and completely undermine the investment case.

Investment that improves the energy efficiency of a building should not give rise to a rate increase. The regulations need to be realigned with the net zero carbon agenda to support investment in low carbon. We note the scheme operating in Scotland known as the Business Growth Accelerator Relief scheme. This applies 12-month business rates relief to new properties and extensions to existing properties. This is encouraging new investment in Scotland and should be considered in England.

6. Reforms required to the business rates system

The burden of business rates has now reached unsustainable levels, with the tax rate over 50% and increasing. The increase in business rates revenue is largely a consequence of adjustments for inflation, as until 2018 was pegged to relatively higher level of the Retail Prices Index (RPI). While business rates are now tracked to the normally lower Consumer Price Index (CPI), legacy of the link to RPI has resulted in a higher base of tax costs

Since its inception in 1990, the rate of inflation (based on RPI until 2018) has significantly outstripped rental growth which means that despite an intention for revaluations to bring the UBR back down, in reality what has been observed is an upward trend.

This upward trend is expected to continue at the next revaluation, with the Uniform Business Rate (UBR) estimated to reach the highest on record. While the government's decision to postpone the next revaluation was the right one to capture the impact of the pandemic, a recent report by Avison Young and CBI finds that the UBR will increase even further to 51.2p, costing business around £3.2 billion over three years.[1]

The tax burden of business rates should be considered against the cumulative impact of tax in the round:

- Other property related taxes, such as Stamp Duty Land Tax (SDLT), have changed several times in recent years. The UK already has the highest property taxes in the Organisation for Economic Cooperation (OECD).[2]

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[1] CBI/Avison Young (2020), Over-rated Making the case for business rates reform, 2020
[2] DG Taxation and Customs Union, Eurostat; OCED Revenue Statistics Database

- New thematic taxes and regulations proposed (e.g. Deposit Return Scheme, Late Night Levy, tourism taxes) have the potential to increase the cost of doing business by adding financial responsibility for services currently covered by business rates.

In addition, as consequence of the significant differential in property values between London and the rest of England has meant that London business have been disproportionately hit by the 2017 revaluation. A relative increase in London's rateable values leads to an increase in London's aggregated business rates contribution.

Business rates deliver a fixed yield achieved through a variable Uniform Business Rate (UBR). Reductions in rates in some areas are offset but increases in other areas at each valuation.

London represents 16.2 % of all UK rateable properties but more than a third of total business rates. London Councils forecast that London's contribution to total business rates revenue will increase to 60% by 2040 under the current system.[3]

Unlike many other business taxes, companies treat business rates as a fixed cost as it needs to be paid regardless of revenue or profits. The CBI/ Avison Young report also finds that business rates represents an estimated 6% of firms' fixed costs across the economy.[4]This means that any change in business rates has a direct impact on a firm's bottom line, affecting their decision making on important areas such as future investment.

The government should consider whether the current balance of taxation coupled with regional inequality is indicative of a competitive tax regime.

We believe that the business rates should continue to be a property-based tax, but the government should take the following actions to bring business rates in line with actual property values and the economic cycle:

- Revaluations should be undertaken annually (see comments above); and
- no longer be required to be fiscally neutral.

For the remainder of the 2017 revaluation period (up to 2022/23) and thereafter, the government should freeze the Uniform Business Rate, and therefore not continue to index it in line with CPI. This would break the link with inflation and mean that yield would fluctuate directly in line with changes in the property rental values.

For the remainder of the 2017 revaluation period (up to 2022/23), the government should freeze the UBR at 49.9p and therefore not continue to index it in line with CPI. At the start of the 2023 revaluation, the government should freeze total gross receipts from business rates and consider resetting the UBR to a lower rate. Thereafter any business rates revenue growth relates to rateable value growth.

[3] London Councils, Response to Impact of business rates on business inquiry, 2019
[4] CBI/Avison Young (2020), Over-rated Making the case for business rates reform, 2020

We recognise removing the requirement for fiscally neutral will mean that the aggregated tax take from business rates will fluctuate over time. This is likely to have implications for Government finance, and therefore it is prudent that reforms to business rates are considered alongside tax policy in the round; this includes the proposed Online Sales Tax which, correctly designed, would broaden the tax base and create a more level the playing field between online and brick-and-mortar retailers.

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