Administration of business rates in England – a BPF-BCSC response

Introduction

The British Property Federation (BPF) is the voice of property in the UK, representing businesses owning, managing and investing in property. This includes a broad range of businesses, comprising commercial property developers and owners, financial institutions, corporate and local private landlords and those professions that support the industry, including law firms, surveyors and consultants.

The British Council for Shopping Centres (BCSC) is the representative body for all aspects of retail property investment, development and operation, our membership includes major occupiers and owners of retail real estate.

Executive summary

We welcome the opportunity to comment on the government's discussion paper on the administration of business rates in England. Detailed responses to discussion paper questions are set out at **Appendix 1**, but our key points are as follows:

- **The time is right for a fundamental review of the business rates system.** The tax has not been updated since the introduction of the Uniform Business Rate in 1990 despite wide-ranging economic and technological changes. Furthermore, business rates could have damaging implications for future real estate development and investment – hurting the economy in the long run.

- **More frequent revaluations (with a reduced antecedent period), the abolition of the RPI 'escalator' and the restitution of empty rates relief** would dramatically increase the fairness of business rates and the ease of administering the system. We welcome the present administrative review, but feel that an opportunity has been missed to truly modernise the system.

- **The current system of individual property valuation should be retained, and revaluations should take place every year**. Revaluing properties every year would ensure that ratepayers' liabilities always reflect actual rental values. It would drastically reduce the incentive for ratepayers to appeal and means that transitional relief could be abolished - freeing up significant resources at the VOA and local authorities.

General comments

There is a widespread feeling – not just among those in the property industry – that the UK's business rates system is no longer fit for purpose. The tax was designed for an economy whose use of real estate was different from today's in some important respects and business rates have not kept up with developments in the economy and in technology.

In some ways, relatively little has changed about our built environment since the early 1990s. We still have offices, shops and warehouses and they fulfil more or less the same functions they did back then. But the way in which those buildings are used has changed significantly. Office-based businesses have relentlessly pursued space efficiency such that the average office worker now occupies approximately half as much space as they would have 20 years ago.[1] The retail landscape is changing very quickly as internet shopping takes off, meaning retailers are better able to separate storage from sales point. Research undertaken by BCSC concluded that the UK has approximately 20% more retail floorspace than it needs.[2] The logistics world has also changed significantly with increased automation in distribution centres.

The drive to use space more efficiently has resulted in barely any net increase in commercial property floorspace since 2003.[3] Yet the business rates system has not adapted at all to these changes and remains designed to raise a practically pre-determined amount of income based on the economy's use of property in 1990, making it out of date and unfair to ratepayers.

We are also concerned about the potential impact of business rates on real estate investment and development. Economic theory suggests that the burden of business rates ultimately falls on property owners. It therefore follows that the level of business rates is likely to have a direct impact on the overall attractiveness of commercial real estate as an investment and will affect the amount of development activity which takes place in the UK. That in turn will have consequences for economic growth, job creation and importantly much needed investment in town and city centres.

Our main worry in this regard is that while the overall amount of business rates levied by the government increases yearly in line with RPI inflation, it is far from clear that rental growth keeps up. Indeed, IPD rental growth figures suggest that overall commercial property rents have increased by only 8% since 1990. That compares with a 107% increase in the RPI over the same period - see **Appendix 2** for more detail. These figures suggest that the state (through business rates) is taking an increasing slice of the economic rent delivered by commercial property and there might come a point at which business rates become penal, seriously compromising the incentive to invest in and develop new commercial property.

Business rates are also becoming a real deterrent to international investors. Whilst negotiations regularly happen in relation to rents and service charges the proportion of occupancy costs taken up by business rates has in a number of cases prevented deals from happening. This clearly has consequences for levels of inward investment.

In addition, business rates on empty properties continue to punish landlords that despite their best endeavours are unable to let their buildings within the short duration of the current relief. This 'tax

[1] *BCO Occupier Density Study 2013*

[2] *BCSC - The Rise and Rise of Multi-Channel Retailing*

[3] *IPF - The Size and Structure of the UK Property Market 2013: A Decade of Change*

on failure' is deeply unfair. It also adds cost to (re)development activity as landlords are generally subject to empty rates both before development (while tenants vacate the building) and after (as new tenants are found and move in). It is through (re)development and refurbishment that the real estate industry adds most value to the economy, and it is a shame that it is being hampered in its efforts. Consequently, we believe that relief from empty property rates should be reinstated.

Given the above, we feel very strongly that now is the right time to take a close look at how the business rates system works and its impact on the economy. The government's administrative review is welcome in this respect, but it is a shame that its scope is not more ambitious. We understand the fiscal constraints under which the government currently operates, but would urge it to consider the general economic benefits that a more proportionate business rates system would bring. Indeed, as the Chancellor noted in his 2014 Budget speech: *"…when you cut a tax rate that is punitively high, that can increase revenues"*.

The good news is that in our view the business rates system does not need a complete overhaul. Nor need it be abolished. With certain focused changes it could become much fairer and more effective. In particular, we would propose:

i. Carrying out revaluations annually with a one year antecedent valuation date. A transition period from the current five-yearly cycle will probably be required;
ii. Allowing the overall business rates take to fluctuate according to economic circumstances (abolishing RPI-linked annual increases); and
iii. Reinstating the pre-2008 availability of relief from empty property rates (100% for industrial properties, three month grace period followed by 50% for all others).

In addition, improving the transparency of rental information as suggested in our response to 'Checking and Challenging your Rateable Value' would eliminate a large part of the incentive for ratepayers to appeal purely to extract the underlying evidence base of an assessment from the VOA.

The administrative review is a good start to modernising the system and we are particularly pleased that serious consideration is being given to more frequent revaluations. But more needs to be done. Occupiers, landlords and the economy generally would greatly benefit.

We remain at your disposal if you would like to discuss this response in more detail.

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Appendix 1 – detailed responses to consultation questions

Q1: The Valuation Office Agency is currently required to set rateable values that are based on the annual rental value of each property at a certain date. What are your views on this approach whilst recognising that the government believes business rates should continue to be based on rental property values?
We believe that the current system of valuing each property individually for business rates purposes delivers the greatest level of fairness and accuracy. Occupiers are generally familiar with the concept of market rents and it therefore makes sense for rateable values to continue to be set primarily by reference to those rents. However, critical to the success of this property tax is assessment of value that is aligned with economic and industry performance. This reinforces the need for frequent valuations and a shorter period between the antecedent data and the start of a new revaluation period.
Q2: What are your views on a less individualised approach to arriving at a rateable value, such as banding, a system of 'zones', indices, or rolling revaluations, as described above?
We are not convinced that the potential benefits (simplicity, potential reduction of administration burden for the VOA and businesses) of replacing the current basis of valuation with a less individualised approach to rateable values outweigh the loss of accuracy and fairness that would result. Any system of banding or zoning will introduce classification difficulties, particularly for properties at the boundaries of those bands or zones. Inevitably there will be many occupiers who end up dissatisfied with the way in which their premises have been classified for business rates purposes. There may be significant financial incentives to challenge the classification, giving rise to protracted negotiation and potential legal action. It is true that individual rateable value assessments are widely challenged under the current system, but in our view that issue could be relatively easily resolved by increasing the frequency of revaluations. We cannot see any such simple solution to the problem of contested banding or zonal classification. That said there is a strong argument for simplifying the valuation process for properties with a low rateable value (say, lower than £12,000 in today's terms). We understand that uch properties account for 64% of the ratings list but only 6% of total receipts. That means that an inordinate amount of VOA resource is tied up in valuing properties that pay little or no business rates and where obtaining a precise value is therefore of lesser importance. Removing such properties from liability to business rates altogether would instantly free up considerable resource at the VOA, which could be used to carry out more frequent revaluations on those properties which provide the bulk of business rates receipts to government. Individual low value properties would still need to be regularly valued (particularly those close to the liability threshold) but it should be possible to largely automate that process. There would also be significant cost savings at billing authorities who would no longer need to issue rates demands and collect payments from over a million ratepayers. Freeing small business from rates liability would also encourage SME start-ups. However, we recognise that the Exchequer cost of this course of action (approximately £1.3bn) is considerable and would probably have to be met by some combination of the government and remaining rate-payers. Applying a single, nominal, level of business rates to low rateable value properties could reduce that cost while retaining the VOA resourcing advantages outlined above,

albeit at the expense of imposing business rates on many occupiers that currently benefit from small business rates relief.

Q3: Moving from the current system to one where properties were placed in bands would result in bills rising for some ratepayers and falling for others. What would be considered an acceptable variance from current bills?

As noted above, we do not think that a banding system would represent an improvement over the current system of valuation except for those properties with a low rateable value.

Q6: Some ratepayers have suggested establishing annual, 2-yearly, or 3-yearly revaluations instead of the normal 5 yearly cycle. How frequently do you think the rateable value of a property should be re-assessed at a revaluation, bearing in mind possible impacts on the predictability and volatility of bills? Why?

There are strong arguments in favour of carrying out business rates revaluations on an annual basis. In particular, transitional relief could be abolished. This relief is difficult for rates-payers to understand, requires considerable local authority resource to manage and has historically always come at a cost to the Exchequer. Also, annual revaluations would virtually eliminate the incentive for ratepayers to appeal their valuation, freeing up considerable resource at the VOA, Valuation Tribunal and billing authorities. Reducing from two years to one the time between when a revaluation takes place and when it comes into effect would also help.

We think it should be possible to eventually carry out yearly revaluations, especially if small business premises are excluded from liability to business rates and can therefore be valued using largely automated systems (although as noted above more attention would be needed at the margin especially as there would be many appeals on assessment just over the threshold). We understand that there is a cost to the VOA in carrying out revaluations, but the cost is small in relation to the total amount raised by the tax, and should be offset to a considerable degree by the expected reduction in appeals that annual revaluations would likely result in.

Given the likely practical challenges in moving from the current five-yearly system to yearly revaluations it will probably be necessary to stagger the transition. For instance, revaluations could be moved to a three-yearly cycle in the first instance before becoming annual. We understand that the Netherlands progressively moved from five-yearly to annual revaluations over a number of years. While the Dutch property tax system is not directly comparable to the UK's, it is likely that certain lessons can be learned from their transition and the dramatic reduction in the number of appeals means this, and other systems in other jurisdictions, are worthy of a more detailed comparative analysis than has been produced to date.

However, a phased transition is likely to bring its own difficulties. In particular, it is not guaranteed that the number of appeals on a particular revaluation will reduce significantly. Given more frequent revaluations and therefore assessments the overall number of appeals may even increase during transition. During this challenging period, the ultimate goal of annual revaluations – and the likelihood of a substantial reduction in appeals – should be kept in mind.

We do not consider that annual revaluations would lead to a significant increase in the volatility of business rates bills, nor indeed do we think volatility is as important a factor as fairness and accuracy of the system. This may not be the case for SMEs who will probably attach more weight to being able to manage their cash flow with a greater degree of predictability, but as mentioned above we believe there is a case for removing many of these assessments from the list altogether.

In any case, on the whole the rental (and therefore rateable) value of an individual property is

unlikely to vary significantly from year to year and it should be possible for businesses to forecast their rates liabilities with a reasonable degree of confidence. Indeed, probably with more confidence than most other costs that they routinely need to budget for.
Q7: Would your views change if more frequent revaluations meant: ***a. rates bills changed more often i.e. were less stable and less predictable than currently?*** ***b. it were necessary to use a less individualised approach to valuing property than currently which would mean that ratepayers with different rents, who at the moment pay significantly different bills, might pay the same amount?***
As set out in our response to question 6 above, we very strongly doubt that annual revaluations would lead to significantly increased volatility of rates bills. However, we would be interested in exploring with government the situations in which it thinks volatility might increase to unacceptable levels. Our views on using a less individualised approach to valuing property are set out in our response to question 2.
Q8: Do you think ratepayers would be more, less, or just as likely to appeal the rateable value of their property if revaluations were more frequent?
Generally speaking, the more frequently that revaluations take place the less incentive there is for an occupier to appeal the rateable value received. The main reason for this is that the expected financial benefit of appealing becomes smaller (the savings apply for a shorter period of time) and the costs of appealing become relatively higher (as appeals need to be lodged and argued more frequently). There comes a point at which appealing becomes uneconomical. We therefore consider that carrying out annual revaluations would lead to a substantial reduction in the number of appeals, although we accept that a transitional period is probably required to get to that stage. However this question (indeed the entire discussion document) must be read in conjunction with the recent consultation on ‘Checking and Challenging your Rateable Value’. In our response to that consultation we set out support for the provision to ratepayers or their advisors of detailed information behind a rateable value assessment prior to the challenge process. This would be crucial in removing the compulsion for ratepayers to appeal simply in order to get this information. We further support the notion that, under the right terms, the VOA should be allowed to seek additional information from the ratepayer or an agent acting on their behalf to provide more detailed reasoning on why they think a rateable value is wrong. However, the level of information that the VOA was suggesting it would provide, in the form of a Rateable Value Information Sheet (RVIS), and the consequential additional requirements that it is imposing on businesses, shifts too much responsibility for detailed information provision onto the ratepayer. We believe that in order to achieve the objectives set out in the rateable value consultation paper the level of information being provided in the RVIS should be more detailed and made available at the pre-challenge stage. We understand that the VOA is of the view that it is unable to provide more granular information, at an earlier stage, because of provisions in the Commissioners for Revenues and Customs Act (CRCA) 2005. BCSC and BPF do not profess to be experts in the CRCA and cannot therefore comment on the accuracy of the advice the VOA has been given. Nonetheless we would like to further explore this with government as it seems this interpretation is a crucial barrier to its policy objectives being achievable.
Q9: Reducing the time allowed to prepare a revaluation from the current 2 years would also reduce the time available for ratepayers to check their rateable values and prepare for changes to their rates bills. It would also mean the Valuation Office Agency would have less time to collect

and analyse rental evidence to prepare valuations. How do you think this would impact ratepayers and local authorities?
Assuming that revaluations take place on an annual basis as suggested in our response to question 6, we do not think that reducing the time allowed to prepare for a revaluation from two years to one would have particularly significant implications for ratepayers. If revaluations take place on a more regular basis any post-revaluation changes in ratepayers' liabilities are likely to be far smaller than under the current five-yearly cycle and therefore there should be less need for businesses to prepare for those changes.
Q10: What is your understanding of how a revaluation affects final business rates bills? Would you like to receive more information from the government on how this works?
It is likely that there is a sizeable lack of understanding among ratepayers both as to the effect of a revaluation on their business rates liability and on how money collected through business rates is actually spent. Regarding the second point, our members report that ratepayers are generally under the impression that – because business rates are collected by local authorities – the money so raised is spent directly on local services. Even under the new system of local government financing that is true only for a proportion of the amounts raised and we consider that there is a case for greater transparency in how business rates revenue is spent.
Q12: There are a number of reliefs available for certain types of property or property use which can reduce the amount of business rates you pay. What do you think of the general level of awareness about the reliefs available?
We have no particular comments about the level of awareness of reliefs. However, the changes announced at Autumn Statement 2013 added to a growing number of reliefs which have arguably made the system more complicated than it needs to be in order to ensure fairness. If the link between business rates and RPI were broken – and the total rates yield allowed to fluctuate – rates bills would generally fall when the economy (and property markets) underperform, obviating to a considerable extent the need for further relief.
Q13: What is your experience, in general, of how the reliefs system is administered?
As noted above, the proliferation of business rates reliefs – while welcome in some ways – has increased the complexity of the system such that businesses now need to engage advisors to ensure that they do not miss out on the reliefs they are entitled to. We would urge government to consider how the rates system can be made fairer without resorting to reliefs.
Q14: Some reliefs are applied automatically to bills and some require ratepayers to request them from their local authority. What are your views on this?
In an ideal world, all reliefs should be treated equally on the grounds of simplicity and fairness. It is probably most efficient for local authorities to apply these automatically to bills in order to save ratepayers the administrative burden of applying for them (and the subsequent claim assessment process). However, that assumes that local authorities are in a position to accurately assess whether a particular property is eligible for a certain relief. If that is not always the case, further consideration should be given as to how that information can be provided to local authorities.
Q17: The government is interested to know whether the following aspects of the current system for billing and collection of business rates present issues for business ratepayers, and if so, how these might be addressed: ***a. Bills are usually issued to ratepayers in paper form***

b. Format of bills may vary across billing authorities, though core content should be the same ***c. Each property is separately liable for rates and so ratepayers receive a separate bill for each property they occupy*** ***d. Changes to the rateable value of a property can lead to an additional, amended bill being issued to the ratepayer***
A change to annual revaluations would supersede the need for (d).
Q18: It can be difficult for the Valuation Office Agency to identify promptly changes to a property that may mean its rateable value should change, particularly if these changes cannot be seen from outside the property. When the change is finally identified, this can result in backdated bills for the ratepayer. To what extent do you think this is an issue for business ratepayers? What could all parties reasonably do to limit the number of situations where this happens?
We have no views on how great an issue this is for ratepayers. One way of ensuring the VOA is kept up to date with changes to a property might be to require ratepayers to complete a simple form on an annual basis on which they self assess whether there have been any changes to the premises, the rents payable or to the rental terms. Armed with such information the VOA could probably do away with its right to backdate bills. That said, we recognise that this might prove an unwelcome administrative burden for ratepayers, particularly if it is not clear what changes need to be notified. Also, the VOA would need to trust ratepayers to be honest (although such trust is the basis of all self-assessed taxes in the UK). Perhaps a better alternative would be for the VOA to make greater use of the planning register to monitor material changes to premises and develop better links with the planning departments at local authorities.
Q19: Changes to rateable values can be made within the life of the rating list, and up to one year after the next list has been compiled. Most backdated bills or refunds are backdated to the date when the change to the rateable value of the property came into effect. What are your views on this?
A change to annual revaluations would supersede this.
Q20: Currently, the Valuation Office Agency collects rental information from ratepayers using forms of return sent by post. What is your experience of completing forms of return? Do you have suggestions for improving the way that you are asked to provide information to the Valuation Office Agency?
It seems incredible that the VOA still relies on written forms to capture the information it requires for valuation purposes rather than using an online system. The VOA could substantially reduce its data entry administration and ensure greater accuracy by asking ratepayers or their representatives to populate their information systems directly via the internet.
Q23: There are currently legal constraints that apply to the data which the Valuation Office Agency can share with ratepayers. Greater sharing of data could help the system run more smoothly. How do you think this could be achieved?
As noted above, we understand that the VOA considers the provisions in the Commissioners for Revenues and Customs Act (CRCA) 2005 to be a barrier to greater sharing of information with ratepayers. Regardless of the accuracy of that view (and we are aware of many who disagree with it) we would like to further explore this issue with government as it seems this interpretation is a crucial barrier to its policy objectives being achievable.

Appendix 2 – rental growth and inflation

Business rates are a property-based tax that has lost touch with the property market and wider economy. In real terms, commercial property rents (predominately retail, offices and factories) fell by about 50% between 1990 (when the regime was introduced) and 2012. On the high street (the focus of much current debate) rents have held up better but still fell by 40% between 1990 and 2012. This divergence between rents and rates is significant and widening, and means that real estate businesses are able to invest in fewer and fewer areas of the UK.

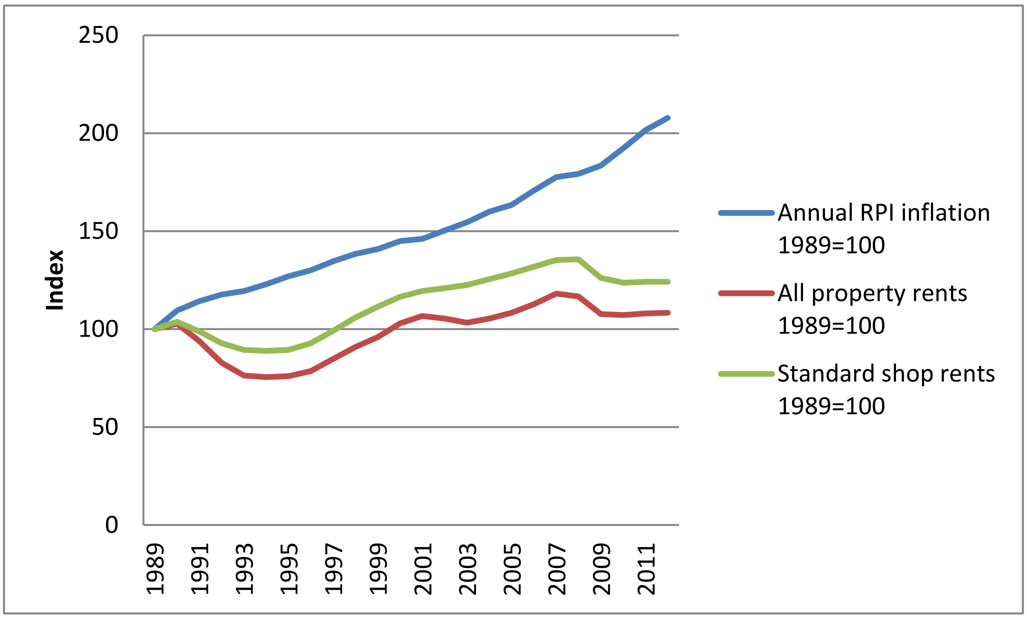

Table 1: While commercial property rents are cyclical, non-domestic rates are not (source ONS, IPD).

There is no mechanism in place to ensure that business rates can respond to wider economic conditions. They have therefore continued to increase in line with inflation, despite the recent decline in GDP and the longer-term declines in consumer spending, commercial rents and businesses' physical need for space.