CBI response to the structural review of business rates.

June 2015

1. The CBI welcomes this opportunity to respond to the structural review of business rates. Non-domestic rates represent a significant proportion of the tax burden faced by businesses – 16 pence in every pound of tax paid by business is in rates. The CBI therefore fully supports efforts to reform the business rates system over the longer term with the aim of reducing the burden faced by those hardest hit by the cost of business rates, ensuring greater transparency and responsiveness, in order to make the system simple, fair and competitive for all.

The CBI's recommendations for business rates reform, in the short term, include:

- More frequent revaluations with a shorter implementation lag.
- Switching the indexation of business rates from RPI to CPI.
- Removing businesses with a rateable value below £12,000 from business rates.
- Removing downward transitional relief to give immediate tax relief in depressed regions where property values have been in decline.
- Re-examining over £3 billion per annum of expenditure on business rates reliefs and exemptions in light of current policy priorities.
- Modernising the billing and collection of business rates.

2. The CBI has made an effort to cost the reform proposals we set out in this paper, based on the data we have access to at this time. The total cost of our reform package involves a fiscal giveaway relative to baseline of less than £3 billion per year. However, in terms of the business rates contribution to the exchequer business will continue to make a greater contribution through this tax compared with 2015/16 in all years other than 2017/18 and as has been mentioned, the current baseline is neither fair, competitive nor representative of economic conditions. **Annex 1** sets out the cost of adopting the CBI's recommended reforms in more detail.

3. The CBI recognises the preference, set out in the terms of reference, for a broadly fiscally neutral outcome from this review. We believe that the system can operate much more effectively with the resources already available to the relevant government agencies, departments and authorities. Several of the suggestions in this response might imply an increase in cost, but they can be achieved with improvements to the process and more efficient use of data.

4. While there are changes that can be made within the scope of this consultation in the short term, ahead of the next revaluation, that will significantly improve the current system, business feels that in the longer-run further reform will be necessary to achieve a simpler,

fairer and more competitive system. The CBI's response to this review will therefore highlight the need for continued reform over the course of this parliament, beyond the parameters of this review. To make the system simpler, government should take advantage of modern technology to deliver a one-stop shop, self-service web portal to ease compliance. To create a fairer tax system, government should look at the disproportionate impact of the business rates system on property-based businesses. To create a more competitive system, government should consider the impact that business rates has on UK investment and growth. It is the CBI's opinion that further reform can be paced in line with the government's existing fiscal consolidation plan.

5. It is important to note the CBI supports the current use of a property based tax upon which to base business rates. Tax research indicates that well designed taxes on immovable property are less distortive than other taxes. It is likely that reform of business rates rather than a replacement with a non-property tax will improve UK tax competitiveness. However the government should keep an open mind when considering any viable alternative to the current system.

Business agrees government should reform now to take the sting out of business rates…

Increasing the frequency of revaluations will make business rates fairer and more reflective of economic conditions.

6. There are compelling reasons to adopt more frequent revaluations. The fact that businesses are paying against April 2008 valuations undermines the principle that business rates are related to the value of property. During the market crash property values declined markedly from their peak, in some property sectors by over 40% yet over this period business rates bills have risen. A plan to introduce more frequent valuations should be one of the main objectives of this review.

7. Introducing more frequent revaluations would deliver two key benefits to businesses and government:

   a. Increasing the frequency of revaluations will mean business rates become more responsive to relative changes in rents, improving the fairness of this tax.

   b. More frequent revaluation cycles will reduce the number of appeals across the system, as businesses appreciate that changes to their business rates bill better reflect economic conditions and property values of the local area. Fewer appeals of this nature will allow the Valuation Office Agency (VOA) to reassign resources from appeals to valuation, further benefiting rate payers.

   c. With more frequent re-evaluations companies could expect their bills to change more often, but to a smaller degree, which would be seen as a welcome reduction in the degree of volatility currently experienced. With a shorter re-valuation cycle it is also likely that the incentive for businesses to appeal their rates bills will diminish as a result.

8. To put this reform into practice the CBI advocates a phased move towards more frequent revaluations. A maximum 3 year revaluation period would be most appropriate, with the potential to move to an even more frequent revaluation cycle over the longer term as the billing and revaluation process is modernised.

9. The antecedent valuation date (AVD) should also be reduced from 2 years to 1 year, following the next revaluation in 2017. A more transparent and accessible record of the valuation data used by the VOA would also help minimise appeals and the widespread perception that business rates are unfair.
10. In the medium term it should be considered whether transitional relief – upwards and downwards – is needed in the event of more frequent revaluations, since its removal would greatly simplify the system. In the meantime however, this review should be used to investigate ways of reforming transitional relief to make the impact of the 2017 revaluation immediate for businesses caught in the downward taper. Continuing to apply the downward transition will be unfair and hamper the economic recovery in regions where a recovery in property values are taking longer to materialise. Indeed, delaying the benefits of a lower rates bill for those taxpayers whose property has decreased in value over the last seven years will run counter to the government's regional rebalancing agenda. The CBI does not advocate funding the end of downwards transition via a supplement to the multiplier, as the increases to the multiplier are already scheduled to exceed the 50 pence rate of tax. We strongly recommend maintaining upwards transition as it currently applies, to make the jump in increased rates bills more manageable for those businesses affected since the 2010 revaluation, based on the 2008 antecedent valuation.

Switching the index for uprating business rates from RPI to CPI will ensure the burden of business rates does not outpace the official measure of inflation.

11. A modernisation of the uprating of the business rates multiplier is needed as RPI is no longer an official measure and systematically overestimates inflation.
12. Switching from RPI to CPI is necessary, as without this change applying RPI will take the 2020 UBR close to the 60p barrier, an unsustainable rate for businesses to pay.
13. We estimate the cost of switching indexation from RPI to CPI to be around £1.9bn by 2020/2021, the end of forecast period. However, this cost is relative to an RPI-indexed baseline that is not appropriate, and therefore reform is necessary to avoid a rising business rates burden on UK firms, relative to general inflation in the economy.
14. If the government were to adopt the CBI's recommendation to switch to CPI as the official index for business rates businesses would save close to £2bn in tax in 2020/21, however the government would still receive more in tax every year for the next five years.

Removing the smallest properties from paying rates will provide significant efficiency savings and will help to drive growth by reducing the burden for SMEs.

15. A disproportionate amount of resource goes into the administration of the business rates system for properties of low rateable value by the VOA, local authorities and business rates valuation tribunals. It has been calculated that 64% of valuations have an RV of less than £12,000 but owners of these properties contribute just £1.5bn per year in business rates[1], or around 6% of the total amount paid after small business rates relief has been taken into account.
16. The CBI calls on government to use this review to remove properties with a rateable value below £12,000 from paying rates. This threshold should then be indexed-linked to ensure it

[1] *Gerald Eve*

retains its value in real terms over the longer term and avoids the need for discretionary changes each year.

17. Removing these properties from the system will achieve several clear benefits:

    d. Firstly it will reduce the burden of business rates on smaller businesses and recent start-ups, freeing up resources for investment and growth.

    e. Secondly the reduced administrative burden of revaluation for the VOA and other relevant authorities, would free up resource to be re-invested in more frequent revaluations.

    f. Finally this proposal can lead to a reduction in the cost of administering the system overall, if the savings from the reduced load of revaluations are not wholly reinvested in more frequent revaluations.

    g. Taking this step, is preferable to the government's current approach of short term temporary quick fixes announced at successive fiscal events which undermines the certainty and stability of the system and does not permanently address the underlying problem.

18. Putting this reform into practice is feasible, while remaining broadly fiscally neutral relative to the current process whereby costs are booked at successive fiscal events. The net cost to the exchequer of implementing this proposal is estimated to be £0.95bn by 2020/21. The majority of the cost would be mitigated by removing the reliefs that apply to these properties and the reduced billing authorities' costs. Billing authorities will no longer bear the cost of issuing rate demands, collecting payments, and, in many instances, taking bailiff action to recover small debts from this band of rate payers. It is also important to bear in mind that even the potentially moderate cost of this proposal would not be incurred until the 2017/18 fiscal year.

19. Computer Assisted Mass Appraisal (CAMA) techniques could make it possible to very quickly determine, with a high degree of accuracy, the top 10% of properties that are below £12,000 in rateable value. Any properties falling below this threshold could be removed from the re-valuation process. The VOA could then revalue the remaining properties. Having already removed 90% of the band from the process this method would significantly reduce the administrative burden.

Undertake a full review of existing exemptions and discounts to ensure they represent value for money.

20. The Government spends over £3bn in business rates exemptions and reliefs. As part of this review, exemptions and reliefs should be fully reviewed to ensure this represents good value for money.

21. The current design of business rates is acting as a barrier to investments which add to the rateable value of properties. Aligning reliefs and exemptions, including empty property relief, to reflect the Government's own policy goal of incentivising business investment could significantly benefit the wider economy by helping companies to grow.

Review the impact of existing business rates retention schemes to see if they improve local growth rates.

22. Businesses are sceptical about the real terms benefits provided for constituent companies by existing local business rates retention schemes, which were introduced to incentivise local

growth. Currently businesses do not see a satisfactory link between local financing from business rates revenues and the service provision for rate payers in their local communities.

23. Prior to any further devolution of business rates revenues, the CBI urges government to review the outcome of existing rate retention schemes, including the pilots introduced in the March 2015 budget. We would suggest a period of two years to assess how well these schemes work in practice to boost growth, before deciding whether or not to introduce or extend business rates retention schemes in other areas.

… but to make business rates simpler, fairer, and more competitive, government should continue to work towards ambitious reform over the course of this parliament.

24. Business rates are hampering private sector led growth, investment and job creation.UK companies will be disappointed if no further action to reform business rates materialises over the course of this parliament, beyond the outcomes of this broadly fiscally neutral review. The risks of not pursuing longer-term reform are clear, UK firms, of all sizes, will appeal business rates bills more vigorously, and in a worst case scenario they may invest less, downsize, reduce employee numbers or move away from using property altogether. We are already seeing evidence of this happening across worst hit sectors and regions.
25. The CBI supports the government's plans for deficit reduction, in order to ensure stable and sustainable long term growth, however we also support and expect action over the course of this parliament to look openly, at achieving ambitious business rates reform, as part of the broader roadmap to fundamentally improve business taxation.
26. Any future work to reform business rates will need to provide a simple, fairer, more competitive system, which is responsive to economic conditions and changing business needs and supports growth, job creation and investment. Business is committed to working with government over the course of this parliament to identify and test reforms which meet these conditions. We are realistic about the time it may take to find a lasting solution which achieves this goal.
27. As an immediate first step, government should set out a detailed work plan with clear aims, which can be used to continue the business rates reform programme, as kicked off by this Structural Review consultation.

To make the system simpler, government should take advantage of modern technology to deliver a one-stop shop, self-service web portal to ease compliance.

28. There is great degree of diversity in the process used for business rates billing across local authorities, including the application of reliefs; the format of bills; the nature of information on bills; the medium of communication and the payment of bills. This all means that the complexity and variety of the administration of business rates is, from a rate-payer perspective, overly burdensome.
29. To manage this we propose a common filing system, eventually in the form of a one-stop self-service web portal. The creation of a single web portal would allow ratepayers to access their billing information and other connected information, such as detail on how reliefs have been applied. This would boost the transparency of the system particularly for smaller and

medium sized business, which lack the dedicated resource to navigate the complex rates system in detail. It could also greatly enhance data capture by the authority, the VOA and other agencies, providing support for a suite of analytics that would support better and more efficient use of data. The benefits of a truly shared-service portal could also deliver cost savings associated with the administration of business rates.

30. A common filing system as described above, would not only improve the user experience, but could radically improve the data processing that the VOA and authorities have to carry out. Appeals would be quicker and easier to process if all relevant data was more up to date and stored in a recognised place, in a common format. Analyses could be quickly and easily carried out across local authorities, for example to establish whether reliefs were being consistently applied. This, in turn, would likely give rise to new information about where further reforms to the system could take place to make the administration of business rates better.

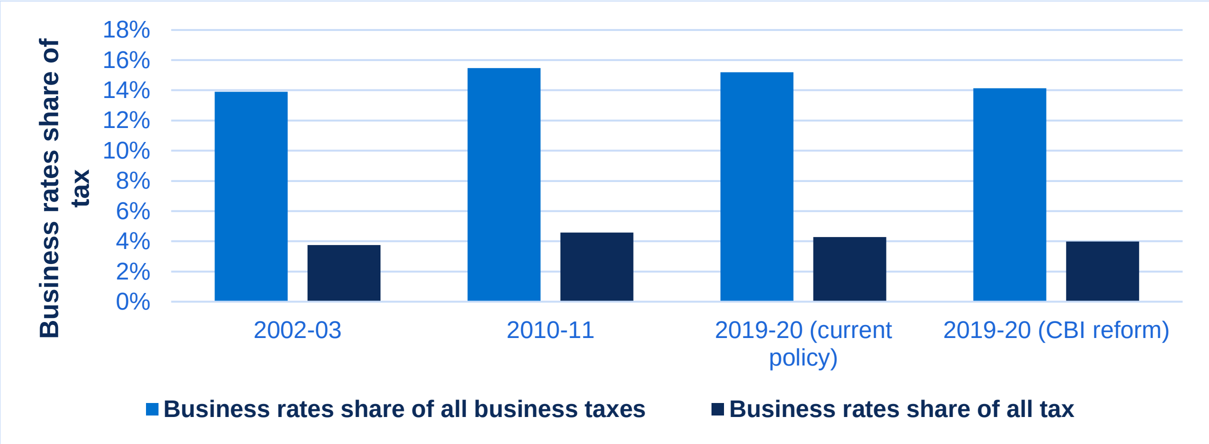
31. At the very least, full digitisation of data capture should be a priority for the VOA. Building out from this could involve the VOA and local authorities providing pre-completed forms for ratepayers and agents to confirm or validate, perhaps annually akin to a Companies House return, rather than to complete information requests from scratch. A single portal would also make it easier for companies to supply relevant, up to date information about their property usage.

To create a fairer tax system, government should look at the disproportionate impact of the business rates system on property-based businesses.

32. The significant burden of business rates is having a distortive effect on business behaviour. The weight of tax paid through business rates, levied on firms which use properties is disproportionate compared with the basket of other taxes paid by UK companies. Over the last five years government has taken welcome action to reduce the burden of business taxation, but business rates have not received similar attention. The lack of comparative action on business rates means the burden facing property based businesses is even more pronounced. This is having a distortive impact on business practices, altering the property profile of the market and potentially reducing the long-term sustainability of a property-based tax base from business rates. Reforming business rates so that the system supports trends in economic activity, rather than creating economic distortions by creating perverse incentives is vital, because most businesses have varied yet essential property requirements.

33. Taking a fair and consistent approach to reduce business taxation is critical. The CBI does not advocate offsetting the burden of business rates through increases in other types of business taxation, which will only negatively impact upon the UK's tax competitiveness in other damaging ways. Instead we urge government to undertake a focused and ambitious work-plan to identify a lasting solution to reform business rates, which adequately reduces the burden facing existing rate paying sectors, once improvements in the UK's fiscal position allow. The CBI's business rates reform package, which involves a fiscal cost of £3 billion, would still result in an increase in business rates as a share of both all business taxes and overall tax between 2002/03 and 2019/20 **(figure 1)**.

Figure 1: The increase in business rates share of overall tax during the recession is not forecast to fully reverse under current policy



To create a more competitive system, government should consider the impact that business rates has on UK investment and growth.

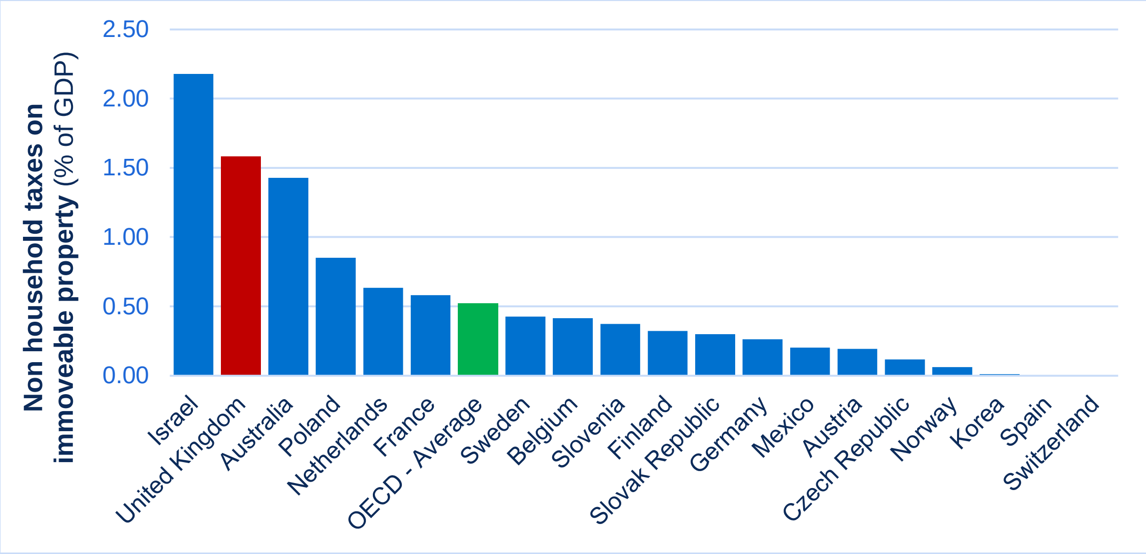
34. Business Rates are an unpopular tax because they represent a very heavy burden on taxpayers with physical operations in the UK. When reviewing business taxes on property as a percentage of GDP we have the highest rate of almost any country in the OECD[2] **(figure 2)**. In Germany for example the contribution of property taxation to GDP stands at less than 0.3% compared to over 1.5% in the UK. In France businesses pay a third of the property tax receipts compared to UK firms. Business rates therefore represent a key barrier to UK competitiveness and our ability to attract and retain business investment.

35. A significant proportion of businesses we surveyed consider business rates as a rising fixed cost. Indeed, business rates is increasingly considered as a downside cost when firms plan and evaluate making investments, including capital investments such as energy efficiency, renewables and plant and machinery. Businesses typically seek out low fixed cost environments and fixed costs are usually given greater prominence over taxes when making investment decisions and therefore comparative distortions in this area undermine the UK's case as a destination for investment. Many international firms tell us that when they make investment decisions, business rates acts as a very real disincentive to invest in the UK, especially when compared with the level of property taxes paid by firms on the continent.

36. Therefore we believe the government should continue to pursue business rates reform beyond the terms of this review, in order to achieve a lasting solution which results in an internationally competitive business rates burden for UK rate payers which supports investment and growth.

[2] *Total shown for Israel in Figure.2 includes agricultural land.*

Figure 2: UK business property taxes significantly exceed the OCED average



Source: OECD

In the longer term any plans for further devolution of rate setting powers will need to be critically assessed to ensure the growth benefits outweigh any distortive impacts between regions.

37. This review asks for views on the devolution of business rates as a mechanism to incentivise local growth. In response, the CBI is clear that any devolution of rate setting powers that will result in a distortive, uneven operating environment for UK businesses should be avoided. The benefits of a single centrally administered UBR should therefore not be underestimated in the course of this review.

38. Any form of devolution, including the creation of new business rates retention schemes, also takes financial resource away from the redistributive fund that business rates revenues provide for central government to administer. Many low income local authorities rely heavily on this pool of funding in order to provide essential services to their constituents. It is worth bearing this in mind when considering submissions arguing for greater local powers to retain revenues or set business rates regionally or in certain cities.

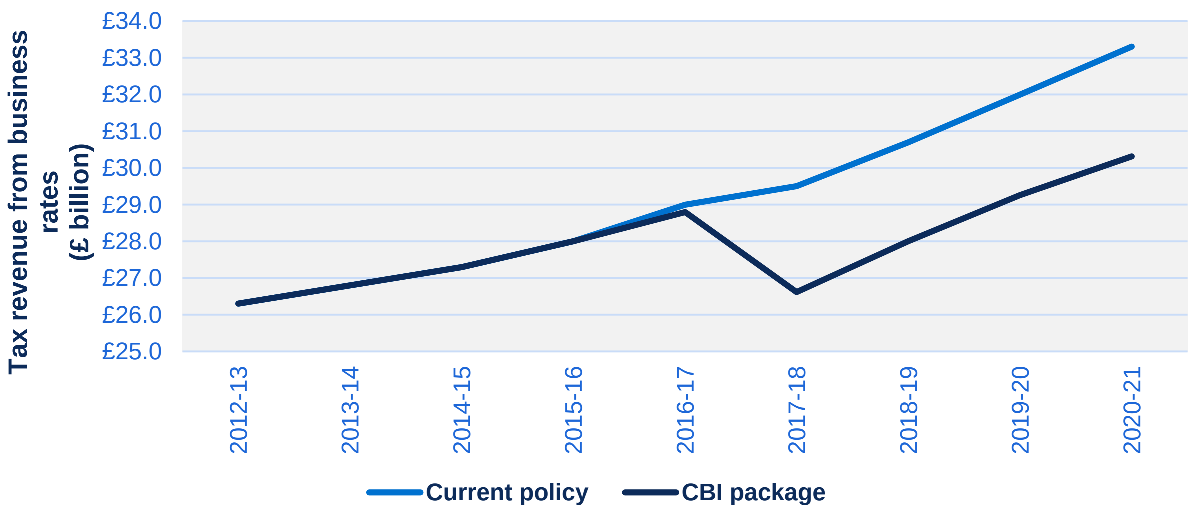
Annex 1: Costing analysis of the CBI's Business Rates Reform package

39. The CBI recommends a number of policies to improve the current system of business rates:

- Modernise the billing and collection of business rates.
- More frequent revaluations with a shorter implementation lag.
- Switch the indexation of business rates from RPI to CPI.
- Remove business below £12,000 rateable value from business rates (partly funded by the planned expiry of small business and retail relief).
- Remove downward transitional relief to give immediate tax relief in depressed regions where property values have been in decline[i].
- Re-examine over £3 billion per annum of expenditure on business rates reliefs and exemptions in light of current policy priorities.

39. The total cost of the CBI's package involves a fiscal giveaway relative to baseline of less than £3 billion per year. However, in terms of the business rates contribution to the exchequer business will continue to make a greater contribution through this tax compared with 2015/16 in all years other than 2017/18 and as has been mentioned, the current baseline is neither fair, competitive nor representative of economic conditions.
40. After this reform the government can expect to receive £30.3 billion in business rates in 2020/21. This is 8.3% more tax revenue than the current year 2015/16 and broadly matches cumulative CPI inflation between 2015/16 and 2020/21, therefore business will contribute to contribute as much in real terms over the medium term.
41. Through the CBI's package of reforms the government can ease the tax burden on businesses least able to pay and contribute to regional rebalancing. This reform can secure the long term tax contribution from business rates through ameliorating or removing the elements which business regard as most distortionary and unfair.
42. Annual profile of the costs of adopting CBI's reform package:

£ BILLION	**2016-17**	**2017-18**	**2018-19**	**2019-20**	**2020-21**
Cost of switch to CPI indexation	£0.20	£0.51	£0.95	£1.45	£1.94
Cost of exempting property below £12k from rates	£0.00	£0.91	£0.93	£0.95	£0.97
Scrapping downward transitional relief	£0.00	£1.47	£0.82	£0.34	£0.07
CBI business rates package	***£0.20***	***£2.89***	***£2.70***	***£2.74***	***£2.98***



[i] Please note that the CBI's estimate for removing downward transitional relief assumes:

1. The same compensation scheme as was applied in 2010;
2. Greater dispersion in rateable values due to the economic cycle, which has included a period of recession and recovery, and a higher business rates multiplier, which is expected relative to 2010;
3. £71million of compensation paid to the smallest business properties is not required as these properties would no longer be part of the business rates system in the CBI's reform scenario.

The CBI is the UK's leading business organisation, speaking for some 190,000 businesses that together employ around a third of the private sector workforce. With offices across the UK as well as representation in Brussels, Washington, Beijing and Delhi the CBI communicates the British business voice around the world.