CBI

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CBI submission to the Treasury's Business Rates Call for Evidence – Tranche 1

Introduction

As the UK's leading business organisation, the CBI speaks for some 190,000 businesses that together employ around a third of the private sector workforce, covering the full spectrum of business interests both by sector and by size. We are pleased to be able to contribute our views and evidence to support the questions set out in the Treasury's business rates call for evidence document.

A fair and sustainable business rates system is critical to support business investment and growth, and ultimately UK prosperity. To achieve this requires a fundamental rethink to the functioning of the business rates system. We are therefore hugely supportive of the government's announcement to fundamentally review business rates. With the tax rate on an unsustainable path, the objective of reducing the overall burden of business rates on business is the right one.

The call for evidence covers a whole range of issues that businesses have been grappling with for many years, from transitional relief to plant and machinery. As business rates is such an important but complex area, the decision to consult in two tranches will provide businesses with the necessary time to contribute effectively towards the debate. Businesses are facing heightened uncertainty, both because of the continued economic impact caused by the pandemic, but also because they are looking ahead to the end of the transition period of the UK's departure from the European Union and future trading arrangements with the bloc. Despite this, business rates reform remains at the top of business' agenda. Getting this right is critical to supporting businesses as we look to rebuild the UK economy and build back better.

To achieve a fair and sustainable business rates system that promotes economic growth and prosperity, the CBI and its members believe fundamental reform is necessary, and this call for evidence presents a real opportunity to take the critical first steps towards this. This document consolidates the views of our members pertaining to the tranche 1 questions and puts forward a set of recommendations on how the business rates system can be reformed. We will provide a second response to the tranche 2 consultation in October.

The context of our response

While business rates are an important source of government revenue, reform is crucial to minimise economic distortions

In 2019/20 businesses paid over £29 billion in business rates across the UK, which is over half the revenue raised from corporation tax in the same year.[1] The business community therefore recognises that this is an important source of revenue for the exchequer, but evidence shows that the UK relies more heavily on property taxes to fund public services than its international counterparts. Property taxes as a share of GDP is the highest in the UK across the G7; at 4% compared to 1% in Germany.[2]

As the economy evolves, this brings new challenges for a property-based tax. Over time, longer term structural changes, including the increased use of digital tools in the retail sector and increased automation

[1] Public sector current receipts – ONS, August 2020
[2] OECD Revenue Statistics, 2019

in the manufacturing sector, mean the business rates system is now operating in a very different environment to the 1990s when it was last reformed.

The tax has simply not kept pace with a changing economy. Taking an example of the out-of-home advertising sector, intangible property such as advertising rights remain rateable hereditaments while other rights, such as sporting rights have been exempt from 1997. Not only is it an anachronism that they remain within scope but the pernicious nature of business rates (the potent combination of the valuation and multiplier) means commercially viable businesses are under threat because the business rates they pay looks set to become the single highest cost for the business. We have one example in this sector where business rates will potentially represent 17% of their total revenue.

A combination of these changes, amongst others, has resulted in a shrinking tax base (as the total rateable value has not kept pace with the rate of inflation) and a tax rate that is now over 50%. The system as it stands is simply not sustainable.

As discussed in the CBI's response to the Treasury Select Committee (TSC) in 2019[3], there are a combination of economic distortions that are a consequence of the workings of the business rates system:

- **Exacerbating regional inequalities.** Revaluations typically penalise those businesses in areas of slower growth because transitional arrangements prevent these businesses from benefitting from a reduction in their rateable value immediately.[4] The hardest hit businesses tend to be in regions of slower growth. For example, at the 2017 revaluation the North West and Yorkshire & Humber saw the biggest impact, while at the same time 2018 GDP growth in these regions lagged the UK.[5]
- **Restricting investment in the stock of property in the UK.** The high tax burden and the inclusion of some plant and machinery (P&M) in the rateable value prevent businesses, both national and global, from investing in buildings and some P&M across sectors and regions in England. Despite digitalisation, investment in buildings remains a significant part of business investment, accounting for 42% of the total.[6]
- **Hitting sectors most reliant on commercial property.** Although not designed to target specific sectors, the reliance of certain business models on commercial property results in a disproportionate incidence of the tax falling on retail, services, logistics and manufacturing firms. At the 2017 revaluation, almost 75% of rateable properties consisted of what are defined as bulk classes - shops, offices, warehouses, and factories. As a result, businesses occupying these types of properties contribute a significant proportion to the total revenue raised from business rates.[7]

Covid-19 has exacerbated many of the challenges inherent in the system, impacting business investment at a time when it is already subdued

The coronavirus pandemic has undoubtedly had a dramatic impact on the economy. In the second quarter of 2020, the economy contracted by over 20%.[8] As a result, many businesses have seen a remarkable fall in demand and revenues. This has only reinforced the need for a fair business rates system that reflects economic fluctuations and business' ability to pay.

The significance of property costs to businesses has been highlighted by the pandemic, as fixed costs need to be paid regardless of market demand. For many firms, business rates have therefore had a significant impact on their cash flow.

Many small and medium sized firms in the middle of supply chains are still paying a business rates bill based on 2015 rental values which does not reflect the current economic conditions, nor the trends in economic

[3] CBI submission to the Treasury Select Committee's inquiry into the impact of business rates on business, 2 April 2019
[4] Transitional arrangements are put in place so businesses can gradually adjust to their new business rates bill following a revaluation.
[5] ONS (2020) regional economic activity by gross domestic product, UK
[6] ONS (2020) Gross fixed capital formation by sector and type of asset
[7] 2017 RV using Revised Rating List Data from Analyse as at 10/07/2019
[8] ONS (2020) GDP first quarterly estimate, UK: April to June 2020

activity seen since 2015. This is partly because revaluations are not sufficiently frequent to allow a prompt adjustment to economic conditions. In addition, commercial rents often respond slowly to an economic shock because tenants are generally locked into a lease arrangement.

There is a case to examine relief for all business sectors that have experienced significant reductions in footfall over and above those that have already been identified. While some sectors have benefited from the business rates holiday, the support has not been applied across the board. Member examples in sectors such as air travel, manufacturing, advertising, distribution, or professional services have highlighted the detrimental effect of a non-negotiable tax on property during times of economic distress, where cost savings had to be made elsewhere in the business.

Moreover, because business rates are a fixed cost, an increase in the burden (following an increase in the tax rate) would impact business investment by increasing the average cost of production and therefore reducing the incentive for businesses to invest. A higher tax rate will also reduce the viability of investment in buildings and some P&M. This effect can be particularly pertinent for foreign businesses deciding where to locate, and as a result could reduce the UK's international competitiveness.

The impact of the pandemic on business investment is already being observed in the data: in Q2 business investment fell by 31% over the quarter, reaching its lowest level since 1997.[9] This comes at a time where business investment is already subdued due to Brexit uncertainty.[10] Looking ahead, CBI surveys point to weak investment intentions, with both the services and manufacturing sectors expecting to cut back on investment in buildings and P&M next year.[11]

Despite signs of an economic recovery, there may be a long way to go before economic activity returns to pre-Covid-19 levels. Already, the crisis has left many businesses with higher debt levels, adding further challenge to businesses' ability to stay afloat once government schemes come to an end.

A slower recovery, coupled with higher indebtedness will reduce the viability of many investment decisions, impacting business investment in buildings, and some P&M in the short to medium term, and in turn the business rates tax base. To aid the economic recovery, it is therefore crucial that policy encourages rather than discourages businesses to invest.

Covid-19 has also brought with it long-term challenges for the business rates system reinforcing the urgency for reform

There are also signs that structural changes in the commercial property market are likely to occur in the medium to longer term. However, there are a several factors at play that mean both the extent and the timing of this change is still highly uncertain:

- **Working from home is likely to become a more permanent feature of working practices.** Across all industries, around 51% of the workforce were working remotely instead of at their place of work in late June 2020.[12] This differs by sector, with the share of those working from home highest in the education (86%) and information and communication (75%) sectors. This has prompted businesses to reassess their property portfolios, with anecdotal evidence suggesting these working patterns are likely to be retained to some degree in the future in some sectors.
- **Some sectors will continue to rely on commercial property.** Many job roles across the economy cannot be performed at home. For example, only 14% of workers in the accommodation and food services are working remotely.[13] Businesses in these sectors will therefore continue to rely on commercial property as part of their business model as the economy recovers. An example of this is the aviation sector: airports have considerable amounts of rateable infrastructure. However,

[9] ONS (2020) GDP first quarterly estimate, UK: April to June 2020
[10] Ibid.
[11] CBI Quarterly Trends Surveys, Q3
[12] ONS (2020) Business Impact of COVID-19 Survey. Wave 8: 15 June to 28 June 2020.
[13] Ibid.

passenger numbers reduced by up to 97% at the Covid-19 peak, and recovery to 2019 levels is unlikely before 2024.[14] However, passenger numbers declined by up to 97% at the Covid-19 peak, and recovery to 2019 levels is unlikely before 2024.[15]

- **Consumer behaviour could shift even further towards online retail.** Online retail spend has increased significantly since 2007, from 3% of total retail expenditure (excluding fuel) to 19%.[16] The pandemic is expected to accelerate this trend. The CBI's surveys show that, while trading conditions for the retail sector remain tough due to subdued consumer demand and declining household incomes, online retailers saw increased sales volumes month-on-month of more than 30% while retail sales volumes as a whole decreased by 49%.[17] The extent to which this trend will persist is unclear, as some of this change will have been driven by the closure of non-essential retail stores.
- **Long leases are likely to lead to a slow adjustment in demand.** In general demand and supply for commercial property can be slow to adjust to economic shocks. On the demand side, this can partly be explained by the structure of the UK's tenancy market, with new leases in the first half of 2019, lasting on average 6.3 years, and rent-weighted leases lasting 10.6 years.[18] This is likely to limit the ability of businesses renting commercial property to adjust their property portfolios in the short term.

Creating a fair and sustainable system should focus primarily on fundamental reform to the existing system

As the government and business look to build back better, there is an opportunity to re-think the future of the business rates system. Businesses need certainty to be able to make investment decisions that will deliver the economic growth needed to help rebuild the economy. Business rates reform has a part to play in both incentivising green investments in the stock of commercial property and in ensuring these investments, and by extension growth, is distributed evenly across the country. To help achieve these policy objectives, business rates reform should focus on creating a fair and sustainable system in the long-term, which will require fundamental change from the status quo.

We believe the best way to achieve this is by reforming the existing system so that it not only works more effectively for businesses across the economy, but so that it also promotes sustainable public finances. Replacing business rates with another tax or introducing additional taxes would further complicate an already complex tax system in the UK and add to the cumulative burden of firms.

Therefore, the government should ensure appropriate consultation with businesses on any alternative taxes to ensure all views and evidence is considered. For example, there is a clear division in our membership on the issue of an online sales tax and so it will be important that these views are considered in their entirety before any policy changes are announced. These views will be considered in more detail in our response to tranche 2.

As a key first step, any tax system should be based on the following principles of good tax policy making:

- **Predictable** – Businesses need to be able to plan when making decisions for the future, and tax liability will be one of the deciding factors.
- **Stable** – Stability in the tax rate, the tax base and the tax administration are important in encouraging businesses to make investment decisions effectively.
- **Simple** – Businesses need to be able to navigate the tax system to reduce the risk of error and minimise the cost of compliance.

[14] Iata: https://www.iata.org/en/iata-repository/publications/economic-reports/Five-years-to-return-to-the-pre-pandemic-level-of-passenger-demand/
[15] Iata: https://www.iata.org/en/iata-repository/publications/economic-reports/Five-years-to-return-to-the-pre-pandemic-level-of-passenger-demand/
[16] ONS (2020) Internet sales as a percentage of total retail sales.
[17] CBI Quarterly Trends Surveys, Q3
[18] MSCI (2019) UK Lease Events Review 2019

- **Fair** – The incidence of the tax should be fairly distributed across the economy to minimise economic distortions.

To achieve the above principles of good tax policymaking, the CBI and its members believe a reformed system should continue to be based on annual rental values but with the following six characteristics:

- ✓ **A fixed tax rate.** Indexing the multipliers to inflation has resulted in a standard multiplier that is now over 50%, significantly higher than the tax rate for other business taxes. Fixing the tax rate would not only align business rates with other taxes, but it would also increase the stability and predictability of the tax for businesses, enabling businesses to make more informed decisions.
- ✓ **A tax base that is frequently aligned to the economic cycle.** Business rates is the only business tax where the liability is out of kilter with the economic cycle due to the infrequent updating of the tax base and the requirement to ensure revenue stability. Allowing government revenues to fluctuate will ensure business rates bills reflect economic realities, increasing the predictability and certainty of a business' business rates liability.
- ✓ **A tax burden that enables business investment.** Reducing the overall tax burden on businesses will support investment in the stock of commercial property. In addition, the tax system could be used more effectively to incentivise investment in areas where the government has a clear policy objective, such as decarbonisation and delivering gigabit-capable digital infrastructure.
- ✓ **A tax liability that is transparent and simple to administer.** There is a lack of transparency in the system relating to how business rates bills are determined. At the same time, the system is complex due to the number of reliefs and the difference in application by local authorities of discretionary reliefs. A transparent and simple system would enable businesses to access the appropriate reliefs and provide stability to support wider business planning decisions.
- ✓ **An appeals process that is simple to navigate.** Engaging with the new appeals system is challenging, which is adding to the administrative burden associated with paying business rates. The speed of the process often means that businesses are unclear on what level of refund they are entitled to and cannot factor this into their planning.
- ✓ **Fit for purpose with possible English devolution.** It would be inappropriate to devolve a tax that needs reform, but the CBI recognises that further devolution of business rates in England may be coming down the line. Therefore, any reform to the current system should consider the impact this would have on further devolution.

The rest of this document covers the CBI's views on the first three characterises above in response to the questions set out in tranche 1 call for evidence document. The CBI's response to the questions in tranche 2 will cover the remaining three characteristics.

Summary of recommendations

To achieve a fair and sustainable business rates system that promotes economic growth and prosperity, the CBI propose the government should do the following:

1. Review the current suite of reliefs available to ensure they are correcting clear market failures and represent good value for money.
2. Introduce a similar measure to Scotland's Business Growth Accelerator that enables new properties or improvements to existing properties to receive a holiday from business rates payments for a specified period.
3. The government should ensure all businesses in downwards transition from 1 April 2021 move onto their new liability following the 2017 revaluation to reflect the postponement of the next revaluation and provide further support to the recovery.

4. It should also remove transitional arrangements for properties whose rateable value decrease following a revaluation, so the business rates bill of those properties reflects the true rateable value; while upwards transitional relief should be maintained to allow a smooth transition to a new higher business rates bill for those properties. This cost to government will vary depending on the outcome of the revaluation and the detail of the transitional scheme but based on previous schemes this could cost in the region of £1.5 to £2 billion.
5. While revaluations occur less frequently than annually, the government should consult on alternatives to transitional arrangements that support those businesses facing a sudden increase in their business rates bill, while allowing those facing a decrease to move to that new bill immediately. Moving to annual revaluations would negate the requirement for transitional arrangements.
6. The government should consider the impact that reliefs could have on creating cliff-edges such as Small Business Rate Relief.
7. Review the interaction of partly occupied relief and empty property relief and the circumstances under which partly occupied relief is granted, to ensure timely access to reliefs when these are needed.
8. Extend the scope of the Fibre Rates Relief to include other gigabit-capable technologies.
9. Extend the relief beyond 2022 to better align with the build timeframes and ensure delivery on the government's rollout target. Longer-term, the government should look to align this policy to that in Scotland, where the relief applies until 2029.
10. The government should consider the impact cliff-edges have on business, for example the current business rates holidays will see businesses going from not paying any rates one month, to pay full rates the next month. This should be considered as part of the wider support package for businesses as they recover from Covid-19.
11. Standardise discretionary reliefs across England so there is a consistency in approach.
12. Introduce a strict set of guidelines setting out in what circumstances local authorities should grant partly occupied relief. This should be revenue neutral to local authorities such that any relief is reimbursed by central government.
13. Introduce a simple system, along the lines of that for council taxpayers, to allow businesses to challenge the mandatory and discretionary relief decisions of local authorities through the Valuation Tribunal.
14. Delay the valuation date to 1st October 2021 to shorten the period between the antecedent valuation date (AVD) and the start of the next revaluation period to ensure the tax more accurately reflects the economic situation and allow a more stable property rental market post-Covid-19. Subsequent revaluations should consider reducing this period to 12 months.
15. Use the upcoming comprehensive spending review to increase the VOA's funding to ensure they have the necessary resource to shorten the valuation period to 18 months in the first instance, and subsequently to 12 months, and to deal with the increase in challenges from Covid-19. As a starting point this should be at least £9 million each year to make up for the fall in revenue in 2018/19.[19]
16. For the remainder of the 2017 revaluation period (up to 2022/23), the government should freeze the UBR and therefore not continue to index it in line with CPI. This is estimated to cost government £0.8 billion per year.
17. For future revaluations, the government should fix the UBR at a lower and sustainable rate so that any business rates revenue growth relates to growth in rental values. The exact cost to government will depend on the level the UBR is rebased to.

[19] Valuation Office Agency (2019) Annual report and account 2018-19

18. Maintain consistency across local authorities by keeping as single multiplier, differentiated only as the small business multiplier and the standard multiplier, without further breakdowns.

The government should look to move towards annual revaluations, as this will negate the requirement or many of the above recommendations. We will address what will be required to meet this objective in our tranche 2 response.
The rationale and detail underpinning each of these recommendations is provided in the sections that follow.

Reliefs

1. How well do current reliefs and exemptions deliver their intended outcomes and satisfy the principles of good tax design? What changes would you suggest to the system?

A key variable in the business rates bill is business rates relief, which can come in many forms and act to offset some of the liability for business. While reliefs inevitably reduce receipts for government, the benefits clearly offset the costs by seeking to achieve the following objectives:

- **Stimulating growth in the UK economy.** Examples include the government's decision to remove a third of all commercial properties from business rates through Small Business Rate Relief and the 100% business rates exemption granted in Enterprise Zones to encourage inward investment to more deprived areas.
- **Supporting struggling business sectors.** In response to the pandemic, the government provided a business rates holiday to the retail, hospitality, and leisure sectors at a cost of around £10 billion to support some of those most impacted.[20] Similarly, the government has previously offered targeted help to the traditional high street retailers through the Business Rates Retail Discount scheme.
- **Subsidising sectors that make wider social contributions.** An example of this is charitable rates relief that ensures valuable societal contributions can be made by increasing the sector's viability.
- **Smoothing the impact of significant increases in business rates between revaluations.** Transitional relief, for example, enables businesses facing a significant increase in their business rates bill following a revaluation to adjust to the new higher bill gradually over time.

In England, there are currently 26 forms of business rates reliefs (that can be mandatory or discretionary) and 14 classes of exemption. Since 2010 the number of available reliefs has increased more rapidly, from 17 to the current 26 reliefs, but until the 2017 revaluation the proportion of relief granted has stayed broadly the same at around 12.4%. Subsequently, the generosity of reliefs has increased, with reliefs granted averaging around 14.7% since 2017.[21] This increase has broadly resulted from more reliefs being granted to small businesses and through greater help for high street retail.

Nevertheless, businesses have found it difficult to navigate the numerous reliefs now available, with much confusion around which ones might apply and ensuring consistent application for businesses with properties situated in several different local authorities. Moreover, while reliefs have become more generous, this increase has only gone part of the way to offsetting the cumulative increase observed in the UBR. For example, in 2018/2019, net business rates receipts (after reliefs) were 27% higher than those in 2010/2011, whilst gross receipts were 30% higher. Businesses would welcome greater simplicity and uniformity in the application of reliefs across the country.

Business also sees this review as a welcome opportunity for government to look at how cliff-edges can be smoothed on some reliefs such as Small Business Rate Relief (SBRR) where revaluations can lead to significant impacts on businesses. Different tax rates can create cliff edges which reduces the incentive for growing firms to move from one bracket to the next. This is also a challenge of the VAT system as there is a

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[20] MHCLG - *Expanded Retail Discount and Nursery Discount Reliefs*, Aug 2020
[21] Reflects 17/18 & 18/19 – later data not yet published.

revenue threshold underlining when a business should be VAT registered. The government should ensure there is a smooth transition, possibly through tapered relief, for businesses with properties whose value will move to the higher rate.

We therefore believe there is an economic rationale to maintain reliefs as part of the business rates system. However, evidence shows that some reliefs are not as effective at achieving the four objectives set out above as others.

Transitional relief limits the amount business rates bills can change each year because of a revaluation, with the aim of phasing businesses to their new business rates bill over time. In England, businesses receive transitional phasing when their business rates bill increases (upward transition) or decreases (downward transition) by a certain amount depending on their rateable value.

This supports businesses located in areas where rental values have increased significantly, enabling them to adjust to their new business rates bill gradually. However, as transitional relief is also in place for those properties with a lower rateable value following a revaluation, businesses occupying these properties take on the burden of the overall price shift as they are unable to benefit from a reduced business rates bill immediately.

Avison Young's research paper, 'Win, Lose or Draw' found that over 66,000 businesses were affected by downward transition at the 2017 revaluation (with a combined rateable value of £6.6 billion in 2017), at an estimated cost of almost £823 million over its first year.[22] By 2020/2021, almost 10,000 businesses remain affected, and in a scenario with a 2021 revaluation, these businesses would never have paid their true business rates bill from the 2017 revaluation. Overall, by the end of the original four-year 2017 rating period, it is estimated that downward transition will have cost affected businesses almost £1.8 billion over four years.[23]

The burden of that cost is estimated to be disproportionately distributed due to differences in changes in rental values across sectors. Retail is estimated to have fronted almost 38% of this cost (at £688 million), and the industrial sector 15% (£281 million). These sectors are also those that were most severely affected in 2020 by the pandemic and are therefore paying a fixed cost that does not accurately reflect their true ability to pay.

Transitional relief also has a disparate regional impact because an area with low rental growth is also likely to be an area of slower growth in economic activity, further hampering the recovery of those businesses.[24] Avison Young's research finds that the North West and Yorkshire & Humber saw the biggest impact from the transitional relief scheme as part of the 2017 revaluation, while at the same time 2018 GDP growth in both of these regions lagged behind the UK as a whole in both regions.[25] For businesses in these regions, there is therefore a double hit.

Furthermore, the discretionary nature of some reliefs and the inconsistency of administration by local authorities can create unintended economic distortions across regions. This has been observed during the pandemic, with businesses being awarded the business rates holiday by one local authority but not by another.

The challenge with discretionary reliefs being in the hands of the Billing Authorities is that it makes the issue more complicated as each Billing Authority applies their own criteria and there is no consistency across the board. This creates major administrative challenges for firms dealing with multiple Authorities, for instance many businesses with numerous assets spread across multiple local authority areas are finding it impossible

[22] Avison Young (2019), Win, lose or draw
[23] This is based on Avison Young (2019) Win, lose or draw but updated to reflect the business rates holiday.
[24] IPF (2013) The Role of Commercial Property in the UK Economy
[25] ONS (2020) regional economic activity by gross domestic product, UK

to obtain consistent treatment, and some have had to use business rates consultants to manage this complexity for them.

The Covid-19 business grants further emphasised this issue with the inconsistency in the application processes posing a major challenge to navigate and access urgently needed funds, often being wrongly rejected, or delayed for months. The reliefs provided need to be better targeted by being more specific in the criteria in the first instance. Below is an example from one business on how this discretionary relief is currently not being properly administered by Billing Authorities:

A section 44a application has been made on behalf of a client on a significant property that has been occupied in stages. The agent and client met with Billing Authority representatives on site twice to agree the phased occupation. The indication was that the application would have been granted, which would have saved circa £250,000. Several months on, the decision has not been received. The business has mentioned that a uniform policy from Billing Authorities would be helpful, as well as better legislation and deadline times for a response would of value.

Moreover, members highlight that state aid implications for discretionary reliefs are also a limiting factor to accessing these reliefs, and hence to the government's use of reliefs as a support tool. This is particularly the case for multi-site occupiers.

Revenues from business rates represent a significant share of local funding needed for local infrastructure. Discretionary reliefs can therefore often create perverse incentives for local authorities whose income is heavily reliant on business rates revenue, which often means the interpretation of reliefs differs across England. The increased localisation of business rates also means local authorities often do not have an incentive to grant the relief.

This has been observed by members particularly in relation to the partly occupied and empty rates reliefs. Examples in the distribution and manufacturing sectors highlight that there is a gap between taking up a building and starting activity and making profits. One business who has recently taken on 7 new sites this year and are building a large facility, are concerned about having to pay rates in the first two years before they are up and running.

Reviewing the interaction of partly occupied relief and empty property relief and the circumstances under which partly occupied relief is granted, will help to encourage efficient use of space and the accompanying economic benefits. Furthermore, setting out a strict set of guidelines for granting partly occupied relief and reimbursing local authorities for any loss in revenue will ensure its effectiveness.

Another challenge of the business rates system is the gap between qualifying for a relief and moving onto the main rate, which is acting as a barrier to growth and diversification. As a principle, the system should encourage a transition between qualifying for reliefs and moving to the higher UBR. While reducing the UBR will help with this by reducing the gap, the government should also consider how the business rates system can help to encourage growth through, for example, tapered relief.

The evidence clearly demonstrates the importance of reliefs in ensuring an equitable tax system and in promoting economic growth. But to achieve this, it is important that reliefs are appropriately targeted and reviewed frequently to ensure they continue to meet their original objectives and represent value for money. Reliefs are most effective when there is a clear market failure that is disadvantaging one area of the economy over another.

When the government considers introducing additional reliefs, it should look at how the business rates system can be used to incentivise business behaviour that aligns to the government's wider economic strategy with the objective of stimulating growth in the UK economy. For instance, business rates reliefs could be used to incentivise investment in improving the stock of properties in the UK.

In April 2018 Scotland introduced a measure called the business growth accelerator following the Barclay Review in a bid to encourage businesses to invest in property and property improvements. Providing an exemption from business rates for new properties and property improvements for a specified period will give business the necessary time to begin commercial activity before facing the cost of business rates. By reducing the immediate burden, investing in commercial property is more likely to be financially viable.

Recommendations:

1. Review the current suite of reliefs available to ensure they are correcting clear market failures and represent good value for money.
2. Introduce a similar measure to Scotland's Business Growth Accelerator that enables new properties or improvements to existing properties to receive a holiday from business rates payments for a specified period.
3. The government should ensure all businesses in downwards transition from 1 April 2021 move onto their new liability following the 2017 revaluation to reflect the postponement of the next revaluation and provide further support to the recovery.
4. It should also remove transitional arrangements for properties whose rateable value decrease following a revaluation, so the business rates bill of those properties reflects the true rateable value; while upwards transitional relief should be maintained to allow a smooth transition to a new higher business rates bill for those properties. This cost to government will vary depending on the outcome of the revaluation and the detail of the transitional scheme but based on previous schemes this could cost in the region of £1.5 to £2 billion.
5. While revaluations occur less frequently than annually, the government should consult on alternatives to transitional arrangements that support those businesses facing a sudden increase in their business rates bill, while allowing those facing a decrease to move to that new bill immediately. Moving to annual revaluations would negate the requirement for transitional arrangements.
6. The Government should consider the impact that reliefs could have on creating cliff-edges such as Small Business Rate Relief.

2. How can reliefs be targeted more effectively? How can reliefs and their administration be simplified?

As set out in our response to Q1, we think there are four objectives that reliefs should seek to achieve; given that reliefs result a reduction in revenue, it is important to ensure they represent good value for money. The CBI, and our members urge the government to fundamentally review the extent to which these reliefs still meet their original objectives. More generally, a significant reduction in the Uniform Business Rate (UBR) and more frequent revaluations would remove the need for some of the existing reliefs, and the reliefs could be primarily used as temporary measures in response to unexpected shocks, such as flooding, or the Covid-19 pandemic.

Partly occupied relief

Businesses renovating their property could benefit from partly occupied relief under the current system. Businesses can apply for the relief and if granted, their business rates bill will be apportioned based on the use of the property.[26]

When this relief was first introduced, it worked well and was welcomed by business. However, the subsequent introduction of empty property relief in 2008 has made it more difficult for businesses to access relief for partial occupation, due to a reluctance by local authorities to grant it. Some businesses believe that, since 2013, when local authorities took on the cost of the relief, they have become more protectionist in granting the relief and have preferred to keep the properties empty than to give reliefs for part-occupation.

[26] Section 44a as set out in the legislation.

The increased localisation of business rates has also meant that local authorities often do not have an incentive to grant the relief.

Reviewing the interaction of partly occupied relief and empty property relief and the circumstances under which partly occupied relief is granted will help to encourage efficient use of space and the accompanying economic benefits. Setting out a strict set out guidelines for granting partly occupied relief and reimbursing local authorities for any loss in revenue will ensure its effectiveness.

Empty Property Relief (EPR)

Under the current system, businesses that occupy a building for non-domestic purposes are liable to pay business rates annually. The business rates bill is due regardless of whether the building is being used for commercial activities. In a scenario where the property is entirely vacant, businesses would be able to claim empty property relief for 3 months (or 6 months if an industrial building) and, in a scenario, where part of the warehouse is unoccupied are able to apply for partly occupied relief as described above.

However, empty property relief is restricted to “buildings” which does not extend to the full range of properties that are within the scope of business rates. In addition, there is typically a lag between the purchase of a commercial property and putting it to productive use, which is significantly longer than 3 or 6 months. This lag can vary significantly by sector and by business model, placing some businesses at a disadvantage. In some cases, business rates can be the tipping point when deciding whether to invest in a new premise. Although the 2008 changes to the relief were aimed at disincentivising landlords from holding empty properties from use, anecdotal evidence from business suggests that in some cases landlords can accommodate businesses to occupy properties without paying rent, indicating it is the business rates that are disincentivising occupation, rather than the landlord’s rent charges.

A telecommunications member has highlighted that issues can also arise for businesses that have to cease using commercial properties before the end of their lease, while having to continue to pay business rates until the lease ends. This factor, coupled with the impact of Covid-19, has meant that this business has reluctantly decided to close shops on the high street. Whilst they have received empty rate relief, this has in many cases ceased or will come to an end before the end of the lease (post the 3-month maximum allowance). They will therefore continue to pay full rates liability until the lease ends with no ability to sub-let and limited demand to allow them to utilise the premises.

Even in the absence of Covid-19, a similar situation arises when renovating or expanding part of an existing premise. The business rates bill increases immediately after the renovation is complete, regardless of whether the improvements have started to deliver value for the business. As with new buildings, it can take time for businesses to get back to full operation following facility improvements, but in the interim, businesses will be hit by a potentially significant increase in their business rates bill.

Providing an exemption from business rates for new properties and property improvements for a specified period will give businesses the necessary time to begin commercial activity before facing the cost of business rates. By reducing the immediate burden, investing in commercial property is more likely to be financially viable.

Fibre rate relief

While the introduction of the Fibre Rate Relief in 2017 was welcomed by telecommunications companies, which government introduced to mitigate the impact of the 2017 revaluation, our members believe that there is more to be done to make this relief fair and effective. The current administration of fibre rate relief across gigabit-capable technologies is uneven. It favours FTTP (Fibre to the Premise) over other gigabit-capable technologies like HFC (Hybrid Fibre Coax), and it does not cover all the infrastructures involved in the delivery of high speeds.

Furthermore, businesses believe there is also an uneven application of fibre relief across regions. Scotland, for example, is leading the way with its fibre relief being in place until 2029. The Scottish Government has also introduced legislation to prevent liability to rates on new build properties until the premises are occupied. Once occupied, the ratepayer continues to receive full 100% rates relief for a further 12 months. This regional disparity goes against the spirit of the government's nationwide gigabit ambition.

Given that both the government and Ofcom take a technology-neutral approach to policy and regulation of broadband, the business rates system should reflect this and level the playing field by extending the current fibre rate relief beyond 2022 and expanding it to include all gigabit-capable technologies and assets.

A recent BDUK report states: 'With the impact of Covid-19 on both the economy and our reliance on digital connectivity likely to be ongoing for some time, the case for sustained investment in gigabit connectivity in support of the UK government's 2025 ambitions has surely never been stronger, nor the need for regulatory and policy certainty greater.' The impact of the rollout cannot be understated, particularly in the current climate. It is therefore more important than ever that the current business rates system is flexed to accelerate deployment of gigabit-capable connections. The level of support from government should reflect the new scale of ambition which has been set by the government.

In addition, the existing relief on full fibre has not been as effective as it could have been on the basis it is too time limited, and only applies to full fibre deployment made in the very early years of the rollout. The payback on full fibre infrastructure is c.15-20 years and requires up-front investment which only starts to make a return once customers start to use the service.

Despite the increasing pace and scale of the full fibre deployment, the industry is still in the relatively early stages of investment, with much more needed in the years after 2022 when the relief is currently scheduled to end. As operators make investment decisions in the period leading up to the manifesto commitment date of 2025, having longer term certainty about the relief would draw in further investment.

Extending the relief to match the length of the investment payback would help secure new investment in full fibre and would be an important step towards meeting the government's own manifesto commitment. Securing this investment would not only help to meet the manifesto commitment but would also generate significant benefits for the UK economy – supporting productivity gains and the levelling up agenda.

It is also important to note that while the government has provided significant funding for the hardest to reach areas – which is a welcome and necessary commitment – this does not go far enough to support the investment case outside these areas. While commercial pressures will incentivise rollout, the need to accelerate deployment to meet the manifesto commitment means further action is required to support the sector to invest.

This can be highlighted by an example where a company is not currently able to make full use of the relief for new FTTP networks because some parts of their network are powered by a different technology (Hybrid Fibre Coax). This technology is recognised by Ofcom and the government as a way of supporting the delivery of the 2025 rollout target, but this is not recognised by the current business rates system.

Our members would like this review to consider enabling further rollout of gigabit-capable connectivity. In the meantime, extend the current full fibre relief to 2029 to align with Scotland until wider reform takes place. Lower business rates bills mean that firms will have more capital to invest quickly and therefore deliver gigabit-capable connectivity further and faster. Wider reform must be technology-neutral and cover all infrastructure, focusing on the outcome of gigabit speeds and greater reliability.

Covid-19 business rates holiday for retail, hospitality, and leisure sectors

As previously mentioned, accessing the necessary cash flow has been critical for businesses to stay afloat throughout the crisis. The government's business rates holiday aimed at supporting businesses severely affected by the Covid-19 pandemic has been welcomed by businesses in these sectors. Many members have pointed out the importance of this support. Those who have benefitted from this have seen it as a

lifeline yet are concerned about the uncertainty of trading conditions and their finances once this support comes to an end.

Those out of scope of the rates holiday believe this would have gone a long way towards helping them save costs and would have prevented them from having to furlough and lay off staff. This has been seen in manufacturing, travel, and distribution sectors, but also amongst professional services businesses who have had to pay for empty offices and had to manage costs by holding back on contracts, labour costs, investment, and innovation. This is why the CBI previously called for an extension of the business rates holiday to all businesses for three months.

A notable example we can refer to is a manufacturer with different types of property (showrooms, offices, and a manufacturing plant) who, due to the impact of the pandemic, have had to close their plant and downsize their shipping of products. This has led to them having to manage the impact on turnover and costs by holding back on contracts, freezing pay, furloughing staff, and making redundancies. The business feels this would have been avoidable had they been able to benefit from business rates holiday, which makes up the largest proportion of their fixed costs.

Another example shows that the lack of footfall in retail districts has had a disproportionate effect on advertising demand for out of home advertising panels on bus shelters, billboards and digital displays however that industry, dependant on physical presence / footfall just as much as retail, leisure and entertainment has not benefited from the same relief. There is a case to examine relief for all business sectors that have experienced significant reductions in footfall over and above those that have already been identified.

Moreover, the impact can be seen in the professional services sector. Businesses who were unable to benefit from business rates holiday during lockdown have had to manage the costs of empty offices that continued to be subject to rent and business rates bills by furloughing staff, leading to difficulties in meeting customer demand and stifling innovation.

As a result, many small and medium sized firms in the middle of supply chains are still paying a business rates bill based on 2015 rental values which does not reflect the current economic conditions, nor the trends in economic activity seen since 2015. This is partly because revaluations are not sufficiently frequent to allow a prompt adjustment to economic conditions.

Despite signs of an economic recovery, there may be a long way to go before economic activity returns to pre-Covid-19 levels. Already, the crisis has left many businesses with higher debt levels, adding further challenge to businesses' ability to stay afloat once government schemes come to an end.

Forecasters including the Bank of England (BoE) expect the recovery to ease from Q3 due to the longer-lasting impacts of Covid-19 such as increased unemployment and lower investment, and therefore do not expect the economy to return to its pre-Covid-19 levels until the end of 2021.[27]

While it is too early to observe the full impact, the Office for Budget Responsibility (OBR) considers changes in the property market in their latest coronavirus scenario. They assume commercial property prices fall by almost 14% in 2020/21 and rise slowly in subsequent years, while at the same time they expect commercial property transactions to fall by almost 24%.[28] This is estimated to leave purchase prices 5.5% lower than their forecast back in March, emphasising the uncertainty of the future business rates tax base.

Going into Q4, one of the key challenges for businesses is the cliff-edge of many of the government's support schemes including the business rates holiday. It is therefore important to consider how these cliff-edges will impact business. Regarding the business rates holiday specifically, businesses currently not

[27] Bank of England Monetary Policy Report, August 2020.
[28] Office for Budget Responsibility, Fiscal Sustainability Report, July 2020.

paying business rates will be faced with a sudden change in their business rates bill from 0% liability to 100% liability in one month.

While the shape of the economic recovery is highly uncertain, several commentators point towards a more prolonged recover than originally anticipated. The CBI has continued to work with the government on what further support will be required for the rest of 2020 and looking ahead to 2021. We recognise this is out of scope of this submission and will be considering this further as part of our Autumn Budget submission where we will set out our proposals for further support in response to the pandemic.

In the longer-term, we argue for a tax bill that is aligned to economic fluctuations and are reviewed annually (as we propose later in this paper), as well as easier access to reliefs such as empty or partly-occupied relief would make for a fairer and more responsive system.

Recommendations:

7. Review the interaction of partly occupied relief and empty property relief and the circumstances under which partly occupied relief is granted, to ensure timely access to reliefs when these are needed.
8. Extend the scope of the Fibre Rates Relief to include other gigabit-capable technologies.
9. Extend the relief beyond 2022 to better align with the build timeframes and ensure delivery on the government's rollout target. Longer-term, the government should look to align this policy to that in Scotland, where the relief applies until 2029.
10. The government should consider the impact cliff-edges have on business, for example the current business rates holidays will see businesses going from not paying any rates one month, to pay full rates the next month. This should be considered as part of the wider support package for businesses as they recover from Covid-19.

3. What evidence is there on the capitalisation of business rates and business rates reliefs into rents over time? What does any evidence mean for the design of rates reliefs and business rates more broadly?

Some existing criticism to a change in the business rates bill, is that economic theory shows any reduction in rates is reflected in an increase in rent charged to tenants in the long run, and as a result there would only be a short-term benefit.[29] This is based on the principle that tenants tend to consider total occupancy costs (rent and business rates) when negotiating their lease terms, so if business rates fall they may be prepared to pay higher rent. However, in practice, many of the assumptions underpinning this theoretical view - such as the presence of a perfectly competitive market - often do not hold.

Firstly, business rates are paid by the occupier of the property, which in many cases is the tenant rather than the landlord thus separating the costs out. Secondly, many commercial properties are owner-occupied and therefore businesses will mechanically benefit from a reduction in rates since this landlord-tenant relationship does not exist. Finally, commercial landlords typically prefer cash flow certainty over fluctuations in rents which means tenancy agreements tend to be over a longer period. The lease length will therefore impact the ability of landlords to adjust their rents in response to a change in business rates. Over the long-term it is plausible that some of the change in business rates costs will be captured by changes in rental growth, however, given the imperfect nature of the market it is unlikely to be completely capitalised into rents.

In current economic conditions it is possible that a business rates cut may enable a tenant to bid a rent greater than zero, but there would not be mass passing through of rates reductions to landlords. More importantly, if we moved to annual revaluations with a fixed UBR – as the CBI proposes – a tenant would not

[29] IFS (2019) Submission to Treasury Committee inquiry: The impact of business rates on business

agree a higher rent due to reduced rates as they would know that this would just lead to an increased rateable value and rates bill the following year.

4. What role should local authorities have in determining business rates reliefs and exemptions? Should reliefs and exemptions be set by central government or set locally?

As raised in Q1, we think there are issues around discretionary reliefs. There is a clear conflict of interest arising when the Local Authority is the collection authority and the beneficiary of the revenue collected. The reliefs need to be targeted, refined, with the criteria set by central government and applied to rate demands locally and not left to the Billing Authority for discretion. Currently, with 300 + Billing Authorities, ratepayers are dealing with 300+ different criteria/approaches which does not provide a clear understanding on behalf of the ratepayer. Whether or not you are a single site operator or operating sites across the UK, certainty and fairness is vital. Certainly, the government should avoid any further devolution of business rates while the system is still in need of reform.

The ability to set different reliefs and exemptions in local areas would also depend on the resource of expertise of LAs which can differ significantly across the country. Businesses reference instances where Billing Authorities have refused or delayed repayments for reasons which appear to be motivated by revenue retention rather than by reference to the correct application of the law. We believe it should be the responsibility of central government to set rate reliefs and how they are administered to ensure there is a level playing field across the country.

Businesses have also raised that there is also no appeal route for discretionary reliefs, which means businesses are unable to challenge their bill unless they refuse to pay their bill and get summoned to Court. Responsible businesses will therefore have no option but to continue paying a rates liability that, in their view, is too high.

Recommendations:

11. Standardise discretionary reliefs across England so there is a consistency in approach.
12. Introduce a strict set of guidelines setting out in what circumstances local authorities should grant partly occupied relief. This should be revenue neutral to local authorities such that any relief is reimbursed by central government.
13. Introduce a simple system, along the lines of that for council taxpayers, to allow businesses to challenge the mandatory and discretionary relief decisions of local authorities through the Valuation Tribunal.

5. Are you aware of ratepayers misusing tax reliefs or other means to avoid paying their full business rates liability? What could be done to tackle this?

The view from our members is also that there are inherent problems within the new Empty Property Rates regime that are conducive of businesses engaging in mitigation and avoidance, which is seen as a levy on uneconomic properties. One of the consequences of this is the issue of recurring re-occupation of a small proportion of the space to gain the benefit of empty rate relief. Members suggest that, if empty property rates reverted back to 50% of occupied rates as originally set out in Local Government Finance Act 1988 there would not be any perceived issue which did not exist prior to the Rating (Empty Properties) Act 2007.

The Business Rates Multiplier

6. What are your views on how the business rates multiplier is set annually and at revaluations?

On its inception, the Uniform Business Rate (UBR), or multiplier, was calculated and applied at 34.8p for every £1 of rateable value. This was then uprated each year by the Retail Price Index (RPI) measure of inflation to maintain growth in government receipts in real terms. The UBR is therefore the lever by which the

government annually increases the total amount collected each year in business rates. Unlike any other tax base, this provides a stable revenue source for government.

However, this comes at a cost to business who face a tax burden that does not accommodate demand fluctuations. Business rates are treated as a fixed cost rather than a conventional tax which can vary. For example, in 2019/20 corporation tax payments reduced by 10% in a single year following weaker economic activity (real GDP growth slowed in 2019/20 to 0.5% from 1.6% in 2018/19), whereas business rates payments increased by 3%.[30,31]

The UBR is reset at each revaluation to account for changes in the total rateable value. In a strong market, this allows government to ensure the total bill does not increase above inflation as it can reduce the UBR to better reflect market conditions. The objective of this mechanism was to ensure the UBR would remain at the original rate of 34.8p in real terms, with every revaluation correcting for changes related to movements in the property market. However, the UBR has seen a steep increase in its first decade, and subsequent revaluations have resulted in a much higher UBR, an average of 45p. Our members firmly believe that the tax rate is on an unsustainable path and must be reduced for their business to survive and thrive.

The significance of property costs to businesses has been highlighted by the pandemic, as fixed costs need to be paid regardless of market demand. For many firms, business rates have therefore had a significant impact on their cash flow. While some sectors have benefited from the business rates holiday, the support has not been applied across the board; many other sectors (such as manufacturing, professional services, or aviation) continued to see business rates as a non-negotiable burden that had to be accommodated through changes in variable costs, such as labour costs, with the unintended effect of business not being able to meet consumer demand, invest, or innovate. At the same time, sectors out of scope have been unable to use HMRC's time to pay scheme for business rates.

Because business rates are a fixed cost, an increase in the burden (following an increase in the UBR) would impact business investment by increasing the average cost of production and therefore reducing the incentive for businesses to invest. A higher tax rate will also reduce the viability of investment in buildings and some P&M specifically as the basis for the business rates calculation. This effect can be particularly pertinent for foreign businesses deciding where to locate, and as a result could reduce the UK's international competitiveness.

Much of the growth seen above can be attributed to the choice of index used to account for inflation. The switch from the RPI to the CPI method of indexing in April 2018 came after considerable pressure from business due to the consistently higher RPI measure over-inflating the business rates bill.

At the 2010 Budget the government announced a switch from RPI to CPI for the indexation of benefits, tax credits and public service pensions to start in April 2011.[32] Between 2011/12 and 2018/19 RPI has been on average 1% higher than CPI.[33] This RPI-CPI wedge is driven by a 'formula effect' caused by using two different formulae to aggregate prices. Research by the CBI and Avison Young suggests that if CPI inflation had been applied to business rates at the same time, gross receipts in 2019/20 would have been an estimated 12% lower, resulting in a much lower UBR of 44p.[34] This is estimated to have cost businesses in England £13 billion in additional gross business rates.

Another reason the business rates system is slow to respond to changes in both the commercial property market and the economy, is the length of time between the date commercial properties are valued for a revaluation, the antecedent valuation date (AVD), and the start of the new rating list (when the updated rateable values and UBR are applied). The best-case scenario would be for a revaluation to occur on an

[30] ONS (2020) Public sector current receipts
[31] OBR (2020) Fiscal sustainability report
[32] HM Treasury (2010) Budget 2010
[33] Based on Avison Young analysis
[34] This estimate includes both the local and central ratings lists.

annual basis, so the tax base is updated regularly to reflect the economic situation. However, to conduct a revaluation of each commercial property in England, the VOA needs to compile a significant amount of data and information, which means there are two years between the AVD and the start of the new rating list. This therefore acts as a barrier to more frequent revaluations. We will address this issue as part of our trance 2 response.

To account for the impact of the pandemic at the next revaluation, the government announced in July the postponement of the revaluation to 2023 based on rental values at 1 April 2021 (originally set for 2021 based on 1 April 2019 rental values).[35] This means that, under the rules of the current system, the UBR for the financial year 2021/22 will be increased in line with CPI from 1 April 2021 until the next revaluation in 2023.

As a result, individual rate payers will see an increase in the UBR for two more years, while the tax base this is applied to (the rateable value of their property) will remain as it did at the 2017 revaluation, based on 2015 rental values. Continuing to uprate the UBR by CPI for the next two years could result in a UBR of 50.1p and 50.9p in 2021/22 and 2022/23 respectively.[36]

This will increase the average business rates bill, and in turn firms' costs, at a time when many firms are still expected to be in a recovery phase and are facing the financial pressures of higher levels of debt. Forecasters including the Bank of England (BoE) expect the recovery to ease from Q3 due to the longer-lasting impacts of Covid-19 such as increased unemployment and lower investment, and therefore do not expect the economy to return to its pre-Covid-19 levels until the end of 2021.[37]

The next revaluation in 2023 is expected to have an AVD of 1 April 2021 with the new rating list commencing on 1 April 2023, a period of two years. While it is important to postpone the revaluation to reflect the impact of Covid-19, there is a risk the economy will have had insufficient time to recover by April 2021, increasing the difficulty of valuing the market at this time. The Scottish government have recognised this challenge by announcing a reduction of the AVD to 12 months. The government should consider taking a similar approach to reduce the uncertainty surrounding rateable values.

However, delaying the AVD will mean shortening the period between the AVD and the start of the new rating list. To be able to do this will require more resource for the VOA. Between 2008/09 and 2018/19 the VOA has almost halved the number of offices in Britain from 83 to 43 and lost 680 full time staff.[38, 39] Funding has fallen by 11% in nominal terms over 10 years and in 2018/19 alone had dropped by £9 million on the previous year.[40] At the same time, the VOA has had to deal with an increase in challenges as a result of the pandemic, which is putting further pressure on their resource.

To support the VOA with this, the government should increase its funding at the upcoming comprehensive spending review (CSR) to, as a first step, offset the fall the VOA saw in its funding in 2018/19. Going forwards, the government should freeze any further cuts to the VOA's funding or staffing during this period, unless driven by technological improvements that support the VOA's capacity.

Recommendations:

14. Delay the valuation date to 1st October 2021 to shorten the period between the antecedent valuation date (AVD) and the start of the next revaluation period to ensure the tax more accurately reflects the economic situation and allow a more stable property rental market post-Covid-19. Subsequent revaluations should consider reducing this period to 12 months.

15. Use the upcoming comprehensive spending review to increase the VOA's funding to ensure they have the necessary resource to shorten the valuation period to 18 months in the first instance, and

[35] Finance Bill 2020-21 draft legislation and tax documents: Written statement – HCWS400
[36] Forecast for CPI inflation is based on OBR (2020) Fiscal Sustainability Report taking the previous year's annual CPI inflation as business rates is indexed based on inflation from the previous September.
[37] Bank of England Monetary Policy Report, August 2020.
[38] VOA (2009) Annual report and account 2008-09
[39] VOA (2019) Annual report and accounts 2018-19
[40] VOA (2019) Annual report and accounts 2018-19

subsequently to 12 months, and to deal with the increase in challenges from Covid-19. As a starting point this should be at least £9 million each year to make up for the fall in revenue in 2018/19.[41]

7. How could the multiplier be set in future to ensure the sustainability of public finances and support growth and productivity? What would the impact of any proposed changes be on the level of the multiplier and revenue from business rates over time?

It is clear from the evidence that the current trajectory for business rates growth is unsustainable as it is growing out of sync with rental growth, as well as the economic cycle. At its current rate of 49.9p, the burden is already significantly higher than other taxes; with the burden estimated to continue on this upward trend, it is crucial that the government uses the Budget in the Autumn to set a path to rebase the UBR back to a sustainable level.

The UBR has increased at a much faster pace than initially expected, an increase of 44% over a thirty-year period, resulting in a UBR of 49.9p in 2020/21. There are likely several factors contributing towards this. One of the largest factors is the indexation of the UBR to inflation. As demonstrated by Avison Young analysis, if the switch from RPI to CPI occurred in 2011 alongside other policies the UBR would now be at 44p instead of 49.9p. As a result, this delay is estimated to have come at a cost to businesses of £13 billion over the nine-year period.

Another factor is that revaluations have generally led to real growth in rates revenues due to overcautious assumptions for 'losses on appeal'. Rates receipts also grow due to 'buoyancy of the List' i.e. new properties being added to the rating list, which can either be because they have been newly constructed or because the Valuation Office Agency (VOA) has decided to rate premises previously excluded, or assessed differently – examples are port occupiers in the 2005 List and sites of ATM machines more recently. Because of these factors, analysis by Gerald Eve finds that gross rates receipts have grown from £10.4bn in 1990 to £30.5bn in 2017/18, an increase of 193%. This compares with inflation over the same period of 128% when using RPI and 94% when adopting the CPI measure of inflation.

Due to these factors, and others, businesses unanimously feel strongly that the UBR should come down to reduce the overall rates burden. However, there is a more divided view on the exact extent of this reduction. In general, reducing the UBR should seek to balance both the evidence used to derive a new lower UBR with evidence from businesses pertaining to a fair tax burden.

For example, analysis by Avison Young suggests this could be 44p to offset the delay in switching from RPI to CPI, and therefore we believe this represents the minimum the UBR should be reduced to. However, as demonstrated above there are other factors that have led to an increase in the UBR over time, indicating that an exercise to rebase the UBR could result in a much lower UBR. Some businesses suggest this could be around 40p, while others would prefer a more ambitious initial reduction to 35p to enable the business rates system to revert to that of the 1990s. This is because 44p would still represent a significantly high tax rate, much higher than other business taxes and higher than other jurisdictions.

However, we recognise that the lower the UBR, the higher the cost to government in lost revenues and as a result the government would be required to make up this shortfall elsewhere in the tax system. Therefore, when considering the value of the UBR, the government should consider this in the wider basket of business taxation and the wider economic benefits this could generate.

In general, the business community feels strongly that the reformed business rates system should operate like any other tax, where the revenue generated can fluctuate in line with changes in rental values. Permanently fixing the multiplier would mean that when property values are declining (i.e. those typically experiencing weaker economic growth) businesses would automatically benefit from a lower rateable value at the next (annual) valuation. Similarly, when property values are increasing, businesses would pay higher

[41] Valuation Office Agency (2019) Annual report and account 2018-19

business rates bills in line with this increase, with the government receiving - or contributing - any difference between the total raised and the fixed receipt normally gathered.

Reducing the burden of business rates on individual businesses has the potential to bring with it large economic benefits as a reduction in business rates would reflect reduction in a firm's fixed costs allowing the saving to be spent elsewhere in the economy. A UBR of 44p, for example, would reduce the overall business rates liability in the order of £4 billion (before reliefs), an average reduction of 12% per property. This new burden would lead to a reduction in the share of business rates of fixed costs from 6% to 5% on average, providing them with a saving to spend elsewhere and to invest.[42]

Recommendations:

16. For the remainder of the 2017 revaluation period (up to 2022/23), the government should freeze the UBR and therefore not continue to index it in line with CPI. This is estimated to cost government £0.8 billion per year.
17. For future revaluations, the government should fix the UBR at a lower and sustainable rate so that any business rates revenue growth relates to growth in rental values. The exact cost to government will depend on the level the UBR is rebased to.

8. How should the multiplier and any supplements relate to business rates reliefs? Should these be discrete, or should supplements fund specific reliefs?

For simplicity and fairness, members support a single multiplier across the country, although continuing to differentiate between the small business multiplier and the standard multiplier. There are at present too many relief schemes in place and the multitude of reliefs has made the system hard to understand. Reducing the business rates multiplier would be the first step, as it would reduce the need for additional relief schemes.

We understand the merits of using supplement schemes to fund investment projects, such as Cross Rail, but not when this is set to be levied over a long period of time. As these types of capital projects have a wide economic benefit to a city, region or even nationally, the government should consider funding these investment schemes at a national level.

9. What are your views on introducing additional multipliers that vary by geography, property value, or property type?

The Uniform Business Rate (UBR) was introduced in 1990 as a replacement for the previous system where each Billing Authority could levy its own rate. This historic approach resulted in over 350 different rates, with significant variations between local authorities, ranging from as low as 122p in the Royal Borough of Kensington & Chelsea to as high as 400p in Sheffield City Council. It was therefore primarily introduced to remove significant variations between local authorities to allow for greater stability in business rates over time.

In principle, the introduction of additional multipliers that vary by geography, property value, or property type, runs to counter to this key aspect of the system. The setting of additional multipliers varying by geography would replicate the issues that were resolved by a UBR. Indeed, rental values, which underpin rates will necessarily reflect geographical locations.

We are supportive of the principle of consistency and simplicity, as businesses feel that differential multipliers introduce additional complexities to an already over complex system. It is clearly important not to stunt growth by businesses avoiding improving their properties at the risk of moving into the next multiplier bracket if there were differences by value. Likewise, varying by geography could simply distort where new

[42] CBI analysis based on ONS (2016) Input-Output tables

property is located depending on how the boundaries are set. Therefore, businesses feel introducing a wider set of multipliers should be considered with extreme caution.

Recommendations:

18. Maintain consistency across local authorities by keeping as single multiplier, differentiated only as the small business multiplier and the standard multiplier, without further breakdowns.