Committee(s):	Date:
Finance Committee – For Information	18 February 2020
Subject: Business Rate Update	**Public**
Report of: Chamberlain	**For Information**
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Summary

This report provides a general update on a number of current issues relating to Business Rates and their potential impact on the City.

Central government has recently announced that it plans to undertake a fundamental review of Business Rates which follows on from the pledge made in the Conservative Party manifesto. In the short term the Government has announced new business rate reliefs for 2020/21 which have focused on providing assistance to the High Street, including an increase in retail relief from 33% to 50% and an additional relief of £1000 made available to some Pubs. The City will be taking steps to raise awareness with ratepayers of the new reliefs.

The new Business Rate retention scheme whereby Local Authorities retain some of the additional rates raised by economic growth in the local area has been delayed until 2021/22. The design of the new scheme or 'alternative model' appears to be focused on rewarding underlying growth by removing some of the uncertainty created by valuation appeals.

Business Rate avoidance continues to increase particularly in relation to empty property. A number of Court decisions have legitimised some avoidance schemes. Whilst this is not a significant issue in the City, the Revenues Team continue to monitor these cases whilst investigating cases that stray into tax evasion.

The increase in serviced office space means more properties are exempt from business rates or are attracting Small Business Rate Relief (SBRR). If the trend continues it may impact on the amount collected in the longer term by the City Premium and could impact on growth.

Recommendations

Members are asked to:

- note the contents of the report.

Main Report

Background

1. Business Rates has been a regular feature in the national press over the last few years and it was a topic of debate during the recent elections. The new Conservative Government has committed to carrying out an early review of business rates with reductions in some sectors promised for the first budget.

2. There is still some significant uncertainty around the future of the Business Rates retention scheme. The previous scheme has been extended through 2020/21 with a new scheme expected to be introduced with effect from 2021/22. The details of this scheme are still unknown but the joint working groups that are taking place provide some insight as to how the new scheme might operate.

3. The issue of Business Rates avoidance has also gained some attention in the press in recent weeks. There are various methods that some landlords and owners will employ to mitigate their business rate liability particularly when a property is empty.

New Government Plans

4. As part of its election manifesto the Government undertook to “cut the burden of tax on business by reducing business rates”. This will be done via a fundamental review of the system”. It is unclear exactly when this review will be carried out. The commitment follows a Treasury Committee report which was released in October 2019 and was critical of the burden and fairness of the current scheme.

5. Much of the coverage has focused on the negative impact of Business Rates in the high street and the Government has committed to “further reduce business rates for retail businesses, as well as extending the discount to grassroots music venues, small cinemas and pubs”.

6. The current retail relief scheme is being extended for a further year and the relief increased from 33% to 50%. Relief has also been expanded to encompass small music venues and small cinemas. A separate scheme has been introduced to provide additional relief to pubs with a rateable value of less than £100,000.

7. The current retail relief scheme is claimed by approximately 400 retail properties in the City which is less than 2% of the City’s Business Rate tax base. The cost of these reliefs is met in full through a government grant so there is no cost to the City Premium. Properties that qualified for this relief in 2019/20 will have the increased relief automatically applied to their bill and properties that could qualify will be sent an application form.

8. It is unclear what a future review of Business Rates will recommend but it is unlikely that there will be a major shift from the fundamental basis of the current scheme. Business Rates accounted for around £31 billion in tax last year and has a better

collection rate than any other UK tax so this would be very difficult to replicate with an alternative method of taxation.

9. The increased regularity of valuations, moving from five years to three, is due to begin in 2021/22 which may address some of the issues such as valuations lagging behind current rental values by up to seven years.

10. A full review of reliefs would be welcome and may provide more focused assistance for retail property. There would also be an opportunity to close some loopholes that are currently being exploited through business rates avoidance schemes which are discussed later in this report.

11. Alternative options that have been suggested, such as replacing Business Rates with an expanded sales tax does not appear to have considered organisations and businesses that do not create a profit or sell goods. There is also a suggestion to base the tax on land ownership, but this is problematic with landowners often located outside the UK. In the short term a review is most likely to lead to some evolution of the current business rates system and this may be coupled with an online sales tax.

12. The City will be seeking to engage with the Ministry of Housing, Communities & Local Government (MHCLG) at an early stage to ensure that our views are taken on board. Of particular importance will be the need to maintain the City Offset.

Business Rate Retention

13. Business Rate retention was introduced in 2013 with the intention of linking Business Rates more directly to the local authority. The scheme rewards the local authority for the amount of growth achieved in the tax base over and above a government set baseline. In 2020/21 the government has returned to the underlying 50% business rate retention scheme with a City share of 30%.

14. The London Pool will continue for 2020/21 under these amended conditions. By continuing to operate as a pool it will allow the Greater London Authority (GLA) and London authorities to combine and to operate a 67% retention scheme.

15. The retention scheme was due to be completely reset for the start of 2020 but has been delayed until 2021. This has benefited the City as it has resulted in the City retaining the £35m already achieved in growth for an additional year.

16. The details of the new scheme are yet to be confirmed and the working groups that are advising MHCLG on the design of the revised scheme or ‘alternative model’ continue to meet on a regular basis. The last meeting took place on 28th January 2020.

17. The discussions that are taking place and the feedback that has been received indicate that the most likely outcome is a revised scheme with some significant differences from the current retention model. The ‘alternative model’ aims to reduce volatility in the system and reward underlying growth in an authority’s rate base.

By factoring out the negative impact of appeals it should benefit the City, assuming that there is continued growth in the City tax base.

18. All indications are that implementation of the 'alternative model' will result in a 'hard re-set' without any transition from the current model. It is therefore likely that the financial benefits achieved under the current retention model will be absorbed into future baselines. Consideration is being given to lobbying MHCLG on applying some transitional arrangement to the reset to lessen the 'cliff edge' impact of a hard reset.

19. Whilst there is no indication of when the alternative model will be finalised and confirmed, the topics put forward for discussion at the Working Groups are encouraging. By removing a significant portion of the impact of appeals it would allow the City to benefit fully from any underlying growth in the tax base and remove some of the risk and uncertainty related to the City's calculation of the appeal provision.

20. There are a number of factors that MHCLG and the working groups are considering. These include but are not limited to the following areas:

    a. Floating "Top up and Tariffs" – these are currently fixed and determine the amount an authority receives or pays to central government in relation to business rates. The City is a tariff authority. By calculating these on an annual basis it would adjust a local authority's income to its baseline funding level, taking account of changes to the appeal and bad debt provisions.
    b. Setting growth baselines on a "lagged" or "non-lagged basis". Under the "lagged" system any growth reward for 2021/22 would not be realised until 2023/24. Under the "un-lagged" approach an estimate of growth would be built into the top up or tariff for 2021/22 and only the reconciliation would be left to be paid in 2023/24.
    c. Which data set to use to calculate growth; either the "in year" net rates payable figure e.g. the amount the authority collects or the Valuation Office Agency rateable value data.
    d. How to factor reliefs and transitional relief into calculations and how to deal with provisions that authority's already hold for the 2010 and 2017 valuation lists.
    e. Determining the safety net, growth thresholds and future scheme resets.

21. It is expected that there will be an opportunity for the City to provide detailed feedback through consultation prior to the introduction of the 'alternative model'.

Business Rate Avoidance

22. Business Rates avoidance has always been a factor in the collection of business rates, particularly since empty property owners were required to pay 100% Business Rates. In the last few years there have been some significant court decisions that have confirmed the legality of some of these schemes.

23. The City has seen all types of avoidance schemes and we are challenging some instances that border on evasion or where we believe the legislation requires

clarification. For instance, the City recently successfully resisted an attempt to claim that an empty building qualified for the ancient monument exemption as it contained a section of Roman Wall. This resulted in Business Rates of over £1 million being collected.

24. The City Revenues Team regularly inspects all empty property to identify and monitor any avoidance schemes but generally the properties are not vacant long enough for this to be a significant issue.

25. The use of empty property by a charity for ‘charitable’ use such as putting on exhibitions or storing boxes is another method being used to avoid liability and appears to border on tax evasion. The City is currently challenging one of these cases and has asked the Charity Commission to investigate the Charity.

26. Whilst not direct avoidance, the City is also seeing a significant increase in serviced offices, with large serviced office companies occupying more property. At present approximately 6000 out of 22,000 assessments are serviced offices and this number is growing.

27. With large properties being split and valued into multiple assessments many of the occupying companies qualify for small business rate relief and in some cases the rateable value falls below £11,999 and the assessment becomes exempt. This means that they then receive a nil bill or a much-reduced bill. The Serviced Office provider is responsible for paying the Business Rates and they then benefit from the reduction. This reduces the amount we collect for both Business Rates and the City Premium. The reduction is not currently significant, but it is an area the Revenues Team continue to monitor; if the trend continues it may start to have a significant impact on how much the City collects and the growth it can achieve for rates retention.

28. Related to serviced offices is a recent request made to the City to split Barristers’ Chambers into individual assessments with the intention of Barristers being able to qualify for SBRR. This is currently being considered by the Valuation Office and depending on the decision and given the potential impact the City may consider a legal challenge.

29. It is hoped that the promised government review of Business Rates will address some of the avoidance tactics detailed above and tackle some of the loopholes in the legislation. As the second largest collector of Business Rates in the country, the City is continuing to highlight these issues with MHCLG.

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