

## Business Rates Review: call for evidence Tranche Two response

October 2020

### About the Local Government Association

1. The Local Government Association (LGA) is the national voice of local government. We are a politically-led, cross party membership organisation, representing councils from England and Wales.
2. Our role is to support, promote and improve local government, and raise national awareness of the work of councils. Our ultimate ambition is to support councils to deliver local solutions to national problems.

### Key points

3. We welcome the opportunity to make this submission to Tranche Two of the call for evidence as part of the Business Rates Review.
4. We would draw attention to the key points made in our Tranche One response, in particular the effects of the COVID-19 pandemic on business and the increased pressures on local government. The Call for Evidence acknowledges that business rates are an important source of revenue for local government and the impact on the local government funding system should be an important consideration in reviewing the tax.
5. Local government needs a system that raises sufficient resources for local priorities in a way that is fair for residents and gives local politicians all the tools they need to be the leaders of their communities. For councils, it is also important that the tax system, including business rates, provides as much certainty as possible.
6. In our view taxes should adhere to certain principles. These are:
  - Sufficiency - Financing for local government services must be sufficient.
  - Buoyancy – rises along with economic activity with protection for local government from losses in income given the need to support local government services.
  - Fairness – The taxpayer makes a fair contribution and the taxbase is not too narrow.
  - Efficient to collect - Any tax should be efficient to collect; if the costs of administration and collection of a tax are high then the net yield will be lower than it would be for a more efficient tax.
  - Predictability and transparency - Income from a tax should be predictable and it should also be relatively straightforward to work out how the tax has been derived.
  - Incentive – Incentives should be provided to both business and local government.
7. Local government has strong interest in a reformed business rates system which commands confidence. An income which keeps up with demand is also important given the pressures on local government especially at this point.

8. Property continues to provide a good basis for a local tax on business. Business rates is efficient to collect and has been relatively predictable and buoyant in recent years. However, the changing nature of business alongside the nature of demand pressures on councils means that we cannot look to business rates to form such a substantial part of local government funding in the future and alternative means of funding councils will be needed instead or as well as a reformed business rates system.
9. As can be seen from [research](#) commissioned by the LGA, online businesses pose a challenge to traditional businesses and to business rates as a tax. If an activity can be carried out online without the requirement for premises this will reduce the yield of business rates which goes to both central and local government. It is true that online commerce may lead to other activities that will generate business rates, such as distribution warehouses but, without reform this is unlikely to raise comparable amounts to the high street premises it replaces. Taxation should be fair for both physical and online businesses. We welcome the consideration of this in section 6 of the consultation.
10. In the context of the current system of business rates and notwithstanding our views about the need for new sources of finance, our responses to the specific questions posed in Tranche Two the consultation are set out below.

#### **Section 4.1: Valuations and transitional relief**

11. The LGA is concerned that different methods of valuation can lead to very different valuations (such as the case of purpose built doctors' surgeries where the courts found that they should be valued on the 'contractors' method rather than the 'rental' method of valuation and which implied a reduction in rateable value of 60%. It does not seem credible that two different methods of valuation can produce such different results. We made this point in our 2015 submission to the Business Rates Review and discussion paper.
12. We note that the Government decided on a policy of revaluations once every three years as a result of the previous consultation. The 2021 revaluation would have been a transition towards this as the next revaluation would have taken place in 2024. Now with the postponement of the revaluation to 2023 the 2017 valuation list will be in force for six years.

#### **Question 10: What are your views on the frequency of revaluations and what changes should be made to support your preferred frequency?**

In [our response](#) to the 2016 consultation on more frequent revaluations we said that the LGA would not support more frequent revaluations unless there is a significant change to the way valuation is done and a restriction on speculative appeals, although this was before the Check Challenge and Appeal (CCA) system was introduced. It is important to design any revaluation system to reduce speculative appeals, but it is too early to tell whether CCA has been effective in reducing these. We believe that a time limit on appeals, and a requirement for ratepayers to provide more data so that valuations take less time, might make more frequent valuations a viable proposition.

#### **Question 11: What are your views on a banded or zone-based valuations system and the trade off with valuation specificity?**

In our 2016 response referred to above on we said that we would support a move to a formula approach if one could be found which was simpler than the current method of valuation and did not lead to too many winners and losers. The same would apply to a banded or zoned system, particularly at the lower end. However, we would be concerned for the implications for business rates retention if growing businesses were not reflected by an increase in rateable value. For example; if a ratepayer refurbishes property it would be expected to increase its market rent and so should lead to an increase in rateable value, whatever system is used.

**Questions 12: What are your views on changing the valuation process or the information provided to the VOA, to enable more frequent revaluations?**

We would like to see a situation where ratepayers provide more information to the VOA. We support the change for the 2023 revaluation where the VOA is likely to make more use of occupier data supplied by billing authorities in order to obtain rent and lease details from occupiers. The VOA needs to have sufficient powers to obtain this information from ratepayers or it should be the responsibility of the ratepayer to provide it.

**Question 13: What are your views on the relative importance of the period between the AVD and compilation of the list vs. more frequent revaluations?**

It is desirable for the rents used in working out rateable values to be as up to date as possible. On the basis that ratepayers provide better quality information to billing authorities and to the VOA, it might be possible to reduce the AVD below the current period of two years, but this should include sufficient time for publication of a draft list so that authorities can carry out the necessary administrative arrangements in time for the compiled list.

**Question 14: What are your views on changing the definition of rents used in the valuation process? How could this be done in a way that most fairly reflects the value of the property?**

We do not have a view on this. We note that basing rates on actual rents rather than estimates of open market rents would move the approach closer to that of a capital value system, where impairments to properties are taken account of in capital values.

**Question 15: If you have had concerns over the specific method of valuation applied to your property, what were these concerns and how could the process be improved?**

The LGA does not have a view on this question but would comment that it is not credible for different valuation methods to produce such different results, for example for purpose-built doctor's surgeries.

**Question 16: What are your views on the design of the transitional relief scheme, and how transitional arrangements should be funded, given the requirement for revenue neutrality?**

The LGA has heard concern over the effects of the transitional relief system. The last minute introduction of reliefs such as the discretionary revaluation relief scheme as a supplement to transitional relief in 2017 led to increased work for councils. Any such schemes should be incorporated into transitional relief from the outset, including their financial implications. It may be necessary for there to be increased Government funding for this.

**Section 4.2: Plant and machinery and investment**

**Question 17: What evidence is there that the business rates treatment of P&M and changes to property affects investment decisions?**

The LGA does not have any evidence it would wish to submit.

**Question 18: Are the current P&M principles and regulations still relevant? How could these be updated if necessary, and what would the effect of any proposed changes be?**

The current plant and machinery (P&M) principles distinguish between 'service' plant and machinery (such as heating and lighting) which is rated, and 'process' plant and machinery', which relates specifically to the ratepayer's business, which is not rated. The distinction between one and the other is not clear and this means that the courts are often called on to rule as to whether a piece of plant and machinery is rateable.

For example, both the ATMs and Iceland cases were related to whether plant or machinery should or should not be included for business rates valuation purposes. We consider that if plant and machinery is economically useful and so contributes towards the ratepayer's income, it should be included as part of the valuation. This would be likely to lead to more rating of plant and machinery and less need for the courts to exercise judgement. It should be up to local authorities to give any temporary or permanent exemptions or judgements in the light of local circumstances using relief and multiplier powers.

**Question 19: What evidence is available on the potential benefits of exempting certain types of P&M on a permanent or time-limited basis?**

The LGA does not have any evidence it would wish to submit. As mentioned above we would welcome giving authorities more discretion in this area in line with the general reform of reliefs and the multiplier which we proposed in our [response](#) to Tranche One of the Call for Evidence. If councils had more discretion, they would be able to exempt some forms of P&M, perhaps for a fixed period.

**Question 20: What practical challenges would the implementation of wider exemptions for P&M pose, and how might those be addressed?**

If more P & M were to be exempted the total yield from business rates would fall – this would have to be replaced by alternative sources of funding.

**Question 21: How can business investment and growth best be supported through the business rates system, and how effective would business rates changes be compared to other available measures?**

As we have said in our response to Tranche One, an alternative would be to give local authorities more discretion to vary the multiplier or allow more reliefs to be determined locally so that local authorities could support local businesses through the reliefs system. This would imply giving local authorities more discretion over centrally determined reliefs in order to allow them to target reliefs to local priorities, including giving businesses incentives.

**Question 22: How could the business rates system support the decarbonisation of buildings? What would the likely impact of any changes be compared to other measures, including other taxes, spending or regulatory changes?**

As mentioned above, one option would be for this to be done through locally determined measures including a lower multiplier which could be paid for by a higher multiplier for other properties or through reliefs.

## **Section 5.1 Valuation transparency and appeals**

**Question 23: What further changes would you like to see made to the (a) Check, (b) Challenge and (c) Appeal stages?**

At this stage of the 2017 list, Check, Challenge and Appeal has led to a lower number of appeals. It is not yet clear if this will rise substantially during the remainder of the 2017 list, which has now been extended to 1 April 2023.

In our original submission to the CCA consultation we proposed that check should not be part of the formal process, which should instead begin with challenges. We repeat this suggestion.

We are of the view that there should be a much shorter deadline for the submission of appeals. In Scotland appeals have to be submitted within 6 months of a list coming into force. We would support a similar situation in England, although this would have to take account of the existence of CCA.

**Question 24: What are your views on sharing information, such as rental/lease details, with the VOA? What are your views on the risks and benefits of this information being shared with other ratepayers, public sector organisations or more broadly?**

As mentioned above, we support this and note that in the 2023 revaluation the VOA is likely to make more use of rent and lease of occupiers supplied by billing authorities. The VOA needs to have sufficient powers to obtain this information from ratepayers or it should be the responsibility of the ratepayer to provide it.

**Question 25: What are your views on who can currently use the CCA system and become party to a challenge or appeal? What are your views on who can use the system, when and on what grounds?**

Local authorities should be allowed to be parties to appeals as was the case before the introduction of Check Challenge and Appeal. Local authorities frequently have an interest in strategically important ratepayers, particularly given the implications for business rates retention. This would enable authorities to bring their own perspective to the CCA process by providing evidence which the VOA, and, if necessary, the valuation tribunal, would have to take into account.

## **Section 5.2 Maintaining the accuracy of ratings lists**

**Question 26: What are your views on introducing a requirement to provide the VOA with rental information, either routinely or where changes to a lease occur?**

We consider that there should be a requirement to provide rental information to local authorities and to the VOA.

**Question 27: What are your views on making a register of commercial lease information publicly available?**

We would support this measure.

**Question 28: What are your views on introducing a requirement to notify the VOA or billing authority of changes to a property that could impact the business rates liability?**

We would support this measure as it would mean that both the VOA and the billing authority would be up to date. We consider there should be a legislative requirement to inform billing authorities and the VOA. We support the continuation of the penalties for knowingly, recklessly or carelessly providing false information in connection with checks and challenges.

## **Section 5.3 The billing process**

**Question 29: How can the current billing process be improved? What changes would provide the most significant benefits to ratepayers through for example, cost or time savings?**

A lot of billing is already online and local authorities have had a lot of experience in dealing with reliefs and grants to ratepayers in the current COVID-19 pandemic period. Local authorities and software providers need to time to make any necessary changes and this should be built into the timetable and not left to the last minute.

**Question 30: What are your views on a centralised online system linked to other business taxes, enabling more joined-up data and management of billing across different locations? How could this best support ratepayers and billing authorities?**

We would support a centralised online system on the proviso that it does not change the billing authority's responsibility for the collection of business rates.

**Question 31: What sort of support would businesses and agents expect to receive when moving to a centralised online process, and from where would you expect to receive it?**

The LGA is an organisation that represents local authorities and cannot speak from the perspective of businesses or agents. Billing authorities would expect to receive support from central government and from software providers, with appropriate new burdens payments in order to implement the change for ratepayers.

**Question 32: What, if any, criteria should be applied in exempting certain ratepayers from online billing?**

It would be appropriate to exempt very small ratepayers or those without access to IT.

**Section 6 Exploring alternatives to business rates**

**Question 33: What are the likely benefits and costs of implementing a CVT? What are the practical implications of implementing a CVT?**

The LGA believes that local authorities need the powers and flexibilities to be able to raise income from a variety of sources given the fundamental changes that have affected the economy for over more than a decade. The impact of COVID-19 on the economy, which is likely to have a lasting effect, reinforces the need to widen the taxbase available to local authorities. This includes, but is not limited to, an online sales tax as referred to in questions 40 to 43. The LGA's response to the questions on CVT should be viewed in this context.

We consider that any tax, including a CVT, should conform to the principles we outlined in paragraph 6. A new system could use modern valuation and collection methods, particularly online, which would make it more efficient and a clear methodology would make it more predictable and transparent. It could also be designed in a way to provide incentives to councils and businesses, and flexibilities could be built in for example where both land and buildings are valued which could be valued and weighted separately. Sufficiency would depend upon the overall yield of the tax, and buoyancy on building in an annual inflation adjustment as is the case for the business rates multiplier and regular revaluations.

Some councils report that it is currently hard to get property owners to engage. Moving liability from occupier to owner as would be the case for a capital values tax would give owners more of a stake in localities. It could also mean that any tax liability would be attached to the property and so would have to be paid by the new owner if the property were to be sold. On the other hand, property owners may be more difficult to locate and could be based overseas which could make collection difficult.

Based on examples internationally it would be possible to design a capital values tax which conformed to those principles and overcomes some of the issues with business rates. However, the above advantages may not be unique to a CVT and any advantages would need to be assessed against any disadvantages which could include locating the owner, the possibility of more appeals, transitional costs, and the incentives that could be created for high density usage of land or building on green spaces.

Overall, the LGA believes that there is merit in the Government doing some research on CVT and LVT (Land Value Tax) including a review of current international practice and forward plans for local taxes on business in order to avoid a scenario where England, and potentially other nations in the UK, opts to implement a CVT just as other countries are considering alternatives. This review should also consider whether the tax could be used to incentivise socially useful behaviours, whether any benefits or disadvantages are unique to CVT, or whether there could be unintended consequences as a result of the tax.

**Question 34: What evidence is there of the benefits that replacing business rates with a CVT would have in practice, for example, on business investment and growth?**

There do not appear to be any empirical studies on the effect of replacing business rates with a capital values tax and we would encourage the Treasury to commission these.

We note that a 2003 World Bank study<sup>1</sup> stated that rental value, which is used to determine business rates, is usually based on actual use of the property rather than the 'highest or best use'. It states that "from a land use perspective, a tax based on value in highest and best use is more efficient than a tax based on current use because it stimulates use to its highest potential by increasing the cost of holding unused or under-used land (as compared to developed land)." There are also issues about taxing vacant land which is not generally taxed under a rental approach.

However as noted above we consider that there should be safeguards built in so that, for example, councils have power to take effective action against any unintended consequences such as building on green spaces which have a social utility.

**Question 35: How can land and property be valued fairly and efficiently under a CVT in England? What evidence is available to do this?**

There are a variety of approaches used internationally. For any variant of capital value tax, it is likely that valuation would be done by professional valuers although ratepayers would have an input in providing evidence in order to generate a market value. Other tools such as statistical modelling and quality assessment could be used drawing on examples from the Netherlands and Australia. The Land Registry keeps a register of sale prices which could be used for valuation and to impute values of similar properties.

In England at present valuation expertise is held by the Valuation Office Agency, although in most countries, including Scotland valuers or assessors are employed by local governments. In a new system, there would be a judgement to be made as to where the function should sit. It would be necessary for local government to be funded appropriately for any transfer of functions and new burdens.

**Question 36: How would replacing business rates with a CVT affect the distribution of taxation?**

Whatever the options available to local authorities for raising taxes there will need to be equalisation between local authorities to reflect the different tax raising abilities and differences in need for, and costs of, services. This is fundamental to funding public services.

Location already has a significant influence on rental value. Therefore, replacing business rates with a capital values tax would lead to changes in the distribution of taxation only where capital values differ from estimated open market rental values. There would be more of a change if property that is currently assessed using a different method of valuation were to change to a pure property value, but it would be possible to consider alternative methods of valuation for such cases, such as schools and hospitals.

**Question 37: What are the likely implications of moving the liability for tax from tenant to landowner or property owner? How could the government ensure effective collection from and compliance by these taxpayers?**

As the Call for Evidence states, there is an argument that at least a proportion of business rates is capitalised in the form of lower rents for owners. However, the extent to which this actually occurs would depend on the individual property market and the

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<sup>1</sup> Richard M. Bird and Enid Slack (2002) Land and Property Taxation: A Review; World Bank

bargaining power of landlords compared with tenants as well as the lag in changes in rates being passed on in changes in rents.

Billing authorities should have responsibility for collecting the tax and for ensuring compliance. They should be able to levy appropriate sanctions for non-compliance, including on owners resident abroad.

As mentioned in the reply to question 33 above, some councils report that it is currently hard to get property owners to engage. Moving liability from occupier to owner as would be the case for a capital values tax would give owners more of a stake in localities. It could also mean that any tax liability could be attached to the property and so would have to be paid by the new owner if the property were to be sold. On the other hand, property owners may be more difficult to locate and could be based overseas which could make collection difficult.

We have given examples in our response to Tranche One of avoidance of business rates through the misuse of mandatory reliefs. It would be necessary to design and set up any new system to limit avoidance and to give councils effective powers to curb any avoidance which did occur.

### **Question 38: What lessons can be learned from other countries experiences with CVTs?**

We would comment that many countries and jurisdictions have experience in capital values taxation. We would point to the following examples in particular:

- Requiring all businesses to submit an annual return on the lines of the New York [Real Property Income and Expense](#) form. We note that the City of New York uses this, along with statistical modelling, to compute market value. There are stiff penalties for non-completion, up to \$100,000 for property with an assessed value of \$25 million or above;
- The Brazilian concept of 'valor venal' ('Assessed purchase value') in calculating IPTU (Urban Buildings and Land Tax) which starts from the sale and purchase price but also takes account building characteristics and use and the average value of property in the street. It may therefore be lower than market price. It is calculated by the municipality which also sets the rate and has discretion on how the different elements are weighted;
- The Brazilian approach where municipalities have discretion to charge higher rates of IPTU for unimproved or under-used land, linked to local plans;
- Assessing land and buildings separately on the Australian model; this is used by almost all Australian states to calculate land values on which Land Tax is based. Generally, a mass valuation approach is used where properties are valued in groups called components, whose market values move uniformly. In [New South Wales](#) valuers analyse property sales, including vacant land and improved properties. They then adjust the sales price to remove the value of improvements. A representative property in each component is individually valued as at 1 July each year to determine how much the land value has changed from the previous year. This change is then applied to all properties in the component to determine their new land values.
- The approach in the Netherlands where the local authority carries out annual revaluations of property value (WOZ) and is responsible for setting the multiplier.

We consider that the Treasury should study other countries including those mentioned above to see how the system they have in place is seen locally by different stakeholders including business and local government.

### **Question 39: What other international alternative approaches to the taxation of non-residential land and property merit consideration for England?**



Other than the examples in reply to question 38 above, we do not have any other examples to suggest.

**Question 40: What would be the benefits and risks of introducing an online sales tax?**

We welcome the recognition in the Call for Evidence that while an online sales tax would not replace business rates, it could still provide a sustainable and meaningful revenue source for the government and that while the scope of an online sales tax would need further consideration, it could be levied on the revenues that businesses generate from online sales to UK customers, and focused on sales in direct competition with those carried out through physical premises.

The LGA commissioned [work](#) on this from WPI Economics and we would support consideration of the options set out in the report, which could be a local e-commerce levy along the lines recommended in this report or VAT (Section 3). Although there would be risks that it would put up the cost of doing business online, we consider that if it was introduced at a relatively low level that this would be a low risk.

**Question 41: Which services and products do stakeholders think should be subject to an online sales tax and what evidence is there to support this?**

We would agree with the proposal in the Call for Evidence, it should be levied on the revenues that businesses generate from sales to UK customers. (WPI found that these represented 90 per cent of all sales). WPI used for their modelling the value of website sales to private customers, produced by the ONS. These website sales totalled £160.2 billion at the end of 2017. Based on assumptions about the proportion of businesses that undertake e-commerce sales, they estimated that these website sales are generated by roughly 218,000 businesses.

**Question 42: What evidence is there for the effects of an online sales tax, for example, on changes in consumer behaviour, or prices?**

It would be up to businesses and the market to determine the extent to which it was passed on in prices; they might set it off against the savings from physical premises, both property and staff costs. The WPI report for the LGA suggests that the move to e-commerce is part of wider structural changes in the economy. It is unlikely that a small levy, which might not be passed on, would have much effect on this.

**Question 43: How could an online sales tax affect the distribution of taxation?**

It could broaden the range of taxes to local government and should be considered alongside the reform of business rates and other alternatives.