



## Communities and Local Government Committee

Oral evidence: Business Rates, HC 665

Tuesday 22 March 2016

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**Members present:** Mr Clive Betts (Chair); Bob Blackman; Helen Hayes; Kevin Hollinrake; Liz Kendall; Julian Knight; David Mackintosh; Jim McMahon; Mr Mark Prisk; Mary Robinson; Alison Thewliss.

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**Evidence from witnesses:**

### **Questions 121 – 190**

*Witnesses:* **Sean Nolan**, Senior Local Government Adviser, Chartered Institute of Public Finance and Accountancy, **David Magor**, Chief Executive, IRRV, **Andrew Hetherton**, Chairman, IRRV Valuers Association Board, Institute of Revenues, Rating and Valuation, gave evidence.

**Chair:** Good afternoon and welcome. Thank you for coming to our evidence session on the Government's business rate reform. You are in the same meeting as us; unfortunately, it is not an ideal room for this type of event. Hopefully if we all shout loudly the microphones will pick us up and we will be able to hear each other, if not actually see each other very clearly. To begin with, if I ask members of the Committee to put on record any interests they may have. I am a Vice President of the Local Government Association.

**Julian Knight:** I employ a local councillor in my office.

**David Mackintosh:** I am in Northamptonshire County Council.

**Helen Hayes:** I am a councillor in the London Borough of Southwark and I employ a councillor in my staff team.

**Jim McMahon:** I am a councillor in Oldham and I employ a member of staff who is a councillor.

**Q121 Chair:** Thank you for that. Thank you for coming to give evidence to us. Can you just go down the table and say who you are and the organisation you represent?

**David Magor:** My name is David Magor. I am the Chief Executive of the Institute of Revenues Rating and Valuation.

**Andrew Hetherton:** My name is Andrew Hetherton. I am Chairman of the Valuers Association of the Institute of Revenues Rating and Valuation.

**Sean Nolan:** Good afternoon, Chairman. I am Sean Nolan, Senior Adviser with CIPFA.

**Q122 Chair:** Thank you all for coming. Without expressing any preference or, certainly for any preferential treatment to come, just to say a particular welcome to Sean, who was our adviser when we did our report on fiscal devolution in the last Parliament. Thank you for your help with that; the report was generally very well received. Certainly the technical expertise you put in was greatly appreciated. Nice to see you see back in a different capacity today. **Do you think the financial context in which 100% retention is taking place affects what is happening? Does it influence it? Does it shape it? Would you like to say a little bit about your thoughts on that?**

**Sean Nolan:** There are two points to make. One is that if we look at the budget and the Chancellor's announcement recently, what is clear is that we are still looking at a very tight financial situation down the line. My shorthand is I do not foresee the ability of an additional pot being available for central Government to work the system over and above 100% of business rates it intends by its policy to have retained locally. That is quite important because what it means, as far as I am concerned in my advice to you, that the 100% system therefore that gets devolved or retained locally by local government has to look after itself.

Chairman, that brings me onto my second point and forgive the analogy but it works for me. On the 100% business rate in that context that I have just talked about, the analogy that comes to my mind is somebody in the middle of a circus ring trying to hold four horses. These four horses are moving in opposite directions. If you are a resourced council, you have a higher tax base and you are looking forward to the prospects of growth, you generally welcome the idea of retention. If you are a high-need council, despite your efforts—it may be to do with history and geography—you may be a bit fretful with the prospect of 100%

business rate retention because you are nervous about the amount of money you will be able to retain and grow.

There are two other horses in this ring. There is an incentive horse and in my analysis the fact that the system will have to run itself, it is incentives. If you allow a council to keep most of its growth that is good if you can grow, but that same money that comes from the incentives is the same money that would help pay for those who cannot grow and would also help pay for the shocks in the system. At the other extreme, if you have no incentives what is the point? Incentives are important to motivation and that is as true as an individual as it is for a council.

The fourth horse in this circus ring is stability. Stability is a bit boring; it is focused on risks and steadiness. Who is going to pay for the shocks? Who is going to pay for the income? That may go down. Who is going to pay business decisions to move? Who is going to pay for appeals? Those four horses are in the circus ring called 100% business rate retention. Chairman, in the context of the financial position, finding the right balance—and it is a balance, it is a line of best fit between those four horses—as far as CIPFA is concerned, is the essence of the challenge.

**David Magor:** The wider issue, and looking at the wider financial context, is these revised powers have been introduced at a time when local government finance is under immense pressure. One could argue that that is not necessarily the best time. There is a great deal of suspicion in local government, particularly around the reductions in income and whether the Government's promises to compensate local authorities for those reductions in income will be fulfilled. There is also uncertainty around the trial areas. Every day we see another trial area being introduced. If those trial areas are going to be able to retain 100% of their business rates, what happens to the rest of England? There is a real danger here that you have more and more trial areas and you will end up with rural wasteland areas that are not included in trial areas. There needs to be some clarification about how the trial areas are going to work and what that actually means in the long term.

Then there are the extra services, how they are going to be funded and what the consequences are on the individual local authority. We do not really know what those services are. It is interesting—when business rates retention was originally introduced, there was a list of services that were funded by the Government's 50%. One would logically think that those services would be carried forward into any new funding regime. In the Autumn Statement we had mention of two things. The attendance allowance was mentioned. Every time any form of benefit is mentioned you view it with a degree of suspicion and you wonder exactly what the plans are behind that, particularly with the problems with growing social care. This is not a new target; it has been a target in the past.

There was a suggestion also about housing benefit for older people. The wording in the Autumn Statement was the "administration" of

housing benefit for older people. What did that mean? Did it mean the administration or did it mean the benefit cost? If it meant the benefit cost then that is an enormous amount of money. These are uncertainties and at a time when local government is under so much pressure, those uncertainties are very worrying.

**Andrew Hetherton:** Chairman, it might be quite useful to put this in context in terms of rate payers as well. They are certainly looking at a system that is simplistic; it needs to be transparent and responsive. The big issue, as far as many billing authorities are concerned, where you have 100% rates retention, is what you do when the unexpected arrives—the unexpected in terms of losses on appeal, changes in the locality or in nearby localities. All of these need to be factored in as a change within the local area. From a valuation perspective, many businesses will look at decisions about where they invest, open new stores and try to develop and grow in a particular area. Clearly there could be differentials between one local authority being within a group and another just being on the other side of the boundary.

**Q123 Chair:** On the issue of change that the system will have to deal with or may have to deal with, there were changes in the budget the other day to small business rate relief and the way that uplifts in business rates in the future are calculated—a change from RPI to CPI. How easy do you think it will be for Government, first of all, to compensate in the short term up to 2020 for the changes in small business rate relief and how much more challenging in the longer term?

**Andrew Hetherton:** Before we get to the point of—as you mentioned, Chairman—2020, the question from many will be why is it necessary for it to take that long because a move to CPI is very much more needed now. From that perspective, consideration should be given to that.

**David Magor:** It is interesting that there was a statement from the Institute of Fiscal Studies yesterday around the uncertainty saying that the funding was not going to be in real money terms as far as small business rate relief was concerned; that it was going to be by service adjustments. What on earth does that mean? How can there be any certainty around that?

The other problem is that the Treasury has missed some significant detail. Whilst the small business rate relief is going to cost around £6 billion, there is the decision to transfer schools to academies. What that will mean overnight is that they will become education trusts and will qualify for mandatory relief. Therefore, they will get 80% relief and that is another £2.6 billion that will not be there for local government. Already, the Education Funding Authority has said that it would top up the other 20%. It is quite interesting that that decision is made, which

is obviously attractive if you are going to create an academy, but without any thought to the impact on local government finance. With the suggestion that certain benefits might be included there is this worry about the impact on people in poverty.

I would parallel that with the creation of the council tax support scheme. That was one of the original mechanisms that was to be funded by Government's 50% when the original retention scheme came in. That lasted two years and then it got rolled into the Revenue Support Grant. It looks like now it is going to disappear. That was originally funded by the DWP. You will find all of these pressures are mounting on local government and it is creating a considerable amount of uncertainty.

**Sean Nolan:** What has been announced by the Chancellor was the first instalment of the business taxes road map, with business rates being part of it for small businesses. My understanding is in 2017 and 2018 onwards it is going to cost of the order of £1.6 billion. In that announcement the Government clearly said that they are looking to ways to compensate local government for the consequence of that. Under the current scheme, where 50% of business rates are retained locally and 50% are given back to Government, then local government, if I was them, should start with the point that is: "Government, you said you would look to compensate local government. Are you going to take this from your central share?" I could not tell you where the Government had plans in terms of compensating local government but they have said it. It is now for them to explain how they will do it.

**Q124 Chair:** What the Secretary of State actually said yesterday—I asked him a question—was that until 2020, section 31 grants will be used to compensate, though we actually cannot find them in the red book yet. We are still searching for those. After 2020, the grant will have gone and it will have to be by adjusting the responsibilities that are transferred to local government.

**Sean Nolan:** I agree.

**Chair:** Can anyone think of how the change from RPI to CPI might be compensated?

**Sean Nolan:** What is key in the 100% retention argument is moving from 50% to 100%. I am not certain what the exact number is but we have had a Government Minister recently quoting £13 billion additional resources—I use that phrase guardedly—into local government. If it is £13 billion, then local government is not expecting £13 billion pre-cash; they would expect £13 billion of matching responsibilities. Under this business relief proposal, if Government are deciding it is not £13 billion,

because they have made decision from a macro point of view to boost growth, I would expect the matching responsibilities to be adjusted downwards.

**Q125 Chair:** That assumes that even in 2020 you can guess right on what inflation is going to be in future years, to do the compensation, or do you have to do it on a yearly basis? I am wondering how it would be done.

**Sean Nolan:** The system would just have to adjust to a starting point and there on in we would have to live with that.

**David Magor:** Unless they assist local authorities by finding extra sources of revenue or making extra sources of revenue available. The central list is a mystery; no one knows what the central list is spent on. Is it the Chancellor's central pot? The central list should be distributed to local government because it is part of rate income. There is no logical reason why the central list should continue in its present form. That in itself creates an opportunity to compensate local authorities.

There are other areas in the road map that was mentioned earlier where the Treasury talks about tax avoidance. It is very disappointing there is no mention of dealing with tax avoidance as far as the rating system is concerned. There is now a massive avoidance of empty property rate. Some of it is becoming completely laughable. The real problem is that it is real. Local authorities are losing an enormous amount of money and that amount of money grows every day. There is a desperate need for some kind of measure to fight against that.

**Q126 Chair:** Without commenting on the rights and wrongs of the Chancellor wanting to help small businesses—most people would think is a reasonable thing to do—what happens if a different Chancellor after 2020 suddenly changes the business rate system? Where does that leave local authorities at a time when they will have had what powers they were going to have devolved to them and there will not be any spare cash at the centre? Is there a real vulnerability in any system after 2020 where Government have control of the system and councils have not? They just receive the money.

**Sean Nolan:** Yes. Back to my analogy, that means Government changing the size of the ring. How this is rolled out in 2020 has to be a bit of a settlement between Central Government and a Local Government, effectively. This does raise the spectre of the certainty of your financial planning, if you are planning locally, after this very point. What happens if the Government of the day decides to do things for good reasons? How does that impact on that 100% retention? More importantly, how does it impact on the spending responsibilities you



have devolved to match that 100%? Who pays for those? That is the issue. That would need to be part of the consideration.

I would go further. What I have just said implies Government become 100% responsible for shocks, but I do not think under the retention of business rates locally, local government can have that. They have argued for it, but I do not think they can have that and expect to be always protected from shocks outside. Notwithstanding Government just deciding to change the size of the ring, if you are talking to shocks to business rate income generally, under this scheme local authorities would have to set up some kind of insurance arrangement. They would have to self-insure, which means they would have to come together, in whatever grouping, to anticipate—there could be changes in local income.

That is different from your opening question, Chairman, in the sense that the Government of the day could just change the ring dramatically but there are other shocks in the system, in relation to business rates, where local government would have to come up with some scheme to pool risk and insure against it. By insure, I mean just putting money on a deposit and having it there to help.

**David Magor:** The real problem is when you go to 100% retention the local authorities will be in the position where they have to make provision for any risks. Those risks have been enormous in relation to the scheme that was introduced in 2013. For example, no one ever saw the appeal risks coming. The real tragedy about the appeals problem is that the retrospective nature of it took some of the appeal settlements back into the old pool days. There was no mention of Government ever compensating local government for retrospective refunds. Some of those refunds went right back to 2010. That just seemed to be grossly unfair. When you get to 100% retention local authorities will have to protect themselves against changes in Government policy and you get these unfortunate changes in the rating system. For example, the challenge on National Health Service Trusts recently came completely out of the blue. That was not expected. The financial impact on local authorities is quite dramatic.

**Q127 Kevin Hollinrake:** You gave your description of the four horses of the apocalypse. Are you in favour of these changes?

**Sean Nolan:** Ultimately, yes. What my position and CIPFA's position would be is that this is a great long-term opportunity, but it has short to medium-term challenges that have to be worked through. I know for a fact this Committee does not look at this too simplistically but there is a danger that elsewhere this is considered just about rolling out some money but it is not. The point of my analogy—for my benefit and I share it with you—is that we will need to find something that is a subjective judgment on fairness between the resources horse and the

needs horse, and something that is recognising that you do need incentives but actually it is the incentives that pay for the stability. We are going to need to find something that does that. That will undoubtedly have short to medium-term challenges. But undoubtedly we would support the longer-term direction of travel.

**Q128 Kevin Hollinrake:** You made the point it needs to have incentives to make it worthwhile. There has got to be some mitigation around those incentives.

**Sean Nolan:** Absolutely.

**Kevin Hollinrake:** What about resetting within those? That is the other issue, in terms of certain authorities powering away and doing tremendously well for how long.

**Sean Nolan:** I know this Committee, in an earlier report, talked about something like 10 years. On reset—

**Chair:** We will come to reset a little bit later on.

**Q129 David Mackintosh:** Do you think it is sensible at this stage to identify the particular additional responsibilities that could be transferred to local authorities when the 100% business rates are retained?

**Sean Nolan:** Absolutely. I do not know if you are interested in some of the principles that would go into that selection process, but in the spirit of making it work, from a local authority point of view and from a central Government point of view, you want look at things under the heading of synergy. You would want to look under the heading of things round influence, i.e. the opportunity for the local community to get more efficiency for public money. That kind of influence in synergy would make sense. There is something about predictability as well. By that, I mean something that has consistency around the country, and you may want to debate that later.

Finally, this may sound a bit like the stability horse talking now, but it has got to be something that you can attribute to a local area because if you remember under the current 50% scheme, the point of reference for everyone was the current formula grant. The top-up in tariffs are by relationship to the current formula grant. I am not saying the 50% scheme was easier; it was not, but the 100% scheme is x times more complicated, and not just twice as complicated. First, we do not know what these additional responsibilities are; secondly, we do not know how they fall in an individual area and therefore we do not know how complicated that new calculation of top-up tariffs will be when you are



talking about that extra £13 billion on things that were not there before. The sooner that is done for everybody in that debate, the better.

**David Magor:** It creates more certainty. It is really important that the funding is in place and local authorities can plan. It is ludicrous not to give local authorities early notice of what the new services are to plan and be in a decision to deliver those services.

**Q130 Mary Robinson:** How does the current redistribution system balance localism and fairness?

**Sean Nolan:** It made a judgment. If you go back to the reference I just made to formula grant, formula grant at the time was not perfect but it reflected a formula—that had been frozen in many cases—based on relative needs. People would argue whether that formula at the time was right, it should have been updated, or whatever. At least that was in the system. From day one under the previous scheme the Government basically said, “You will keep whatever you have under that formula grant. Clearly, if you are a resources horse, if you have a higher tax take, we are going to take that away from you in the form of a tariff. If you are a needs horse and you have higher needs than tax then we will give you a top-up, funded effectively”. That is how the current settlement in fairness has been derived.

Going forward, as well as the not inconsiderable challenge of working out what these additional £13 billion of challenges are and how they currently haul, we have—what has been announced by Government recently—a review of the needs formula. Looking at needs this is a zero-sum game; you get winners and losers. I could not say to you now that the current system is unfair because the current system reflected a formula that at least had been frozen since 2013 when it was introduced. To come to a new view of needs will need a lot of work. People need to sit down, compare relative needs and do that in a way that people can understand in the modern age. What it will mean is that that will be happening and one of the questions Government will have to consider is that when they roll out this in 2020 with this additional £13 billion, is: do they take a judgment of reallocating need there and then at the same time as they roll it out? The implication in the announcement from Government is that they will do that. That is a process that people will have to go through, but that will prove to be quite a challenging exercise at the same time as roll out generally.

**Q131 Mary Robinson:** Do you feel that that addresses the issues around the localism agenda?

**Sean Nolan:** This is very difficult, but it needs some sense of fairness up and down the country. That is part of the localism agenda—a sense of starting fairness, but the incentives are also part of the localism agenda, i.e. that behaviour of being able to benefit from your efforts is really quite important because it never used to feature. It used to be a very two-dimensional debate between needs and resources. Incentives are there and have to be respected but, for the reasons I have alluded to in my circus analogy, you cannot let incentives run away completely, otherwise you have got no money to pay for anything else.

**Q132 Mary Robinson:** What do you think will be the effects of abolishing the current levy and safety net arrangements?

**David Magor:** You need to put something in place. The comment I was going to make about the general system is that it has worked quite well. We have been pleasantly surprised how well it has worked. It has reflected localism, particularly in the shire areas, where the relationship between district councils and shire counties has worked quite well. The system has worked well but there has been some unfairness around the edges: the safety net could have been more expensive. The safety net has worked reasonably well, but none of us saw the issues around the safety net surfacing. The things that caused the implementation of the safety net, like losses in value and properties shifting from a local authority list to the central list are being made retrospective to 2010. I could name four or five local authorities that were in very serious financial difficulty as a result of what appeared to be arbitrary decisions. All those issues need to be looked at again.

Under the new regime, there needs to be very careful thought about the way the safety net is going to work and how it is going to be funded, and obviously the levy is going to disappear. The working groups that are being set up by the Local Government Association and DCLG need to sit down carefully and look at the possibility of new models to make sure that every eventuality has been explored. With 100% retention you have to be careful about the volatility and make sure local authorities are protected from that volatility. Will there be a safety net? How is it funded? What is the certainty about that funding? How is it going to work if local authorities get into serious financial difficulty? Where will the decisions be made? At the end of the day, the tariffs and top-ups were a glorified equalisation system. That is exactly what you are going to get under 100% retention.

**Q133 Mary Robinson:** Would you be able to give a view on how the system of tariffs and top-ups should be adjusted?

**David Magor:** I would like to look at the bigger picture. It works surprisingly well. You do not want to interfere with the process if you do

not have to interfere with it. Because it is a 100% retention scheme, the working groups over the next couple of months have got to look carefully at alternative models. They always have the assurance of going back to the model we have because the model we have is effective. I am not for disturbing something that has worked reasonably well. We should explore what the other models are and make sure that local authorities are protected through an effective safety net mechanism.

**Sean Nolan:** CLG did do a good job in putting together the 2013 scheme. They were trying to balance these four different horses. They did it well. I would not be surprised, and in fact it would seem logical, if they introduce the top-up in tariffs. The point I was trying to make in an earlier contribution was that under the 100% business rates retention and the economic situation that we have alluded to, I cannot see the prospect of additional money outside the system being available to deal with shocks. You are left, then, with the sector itself having to be statesmanlike, grown-up in the sense that it therefore has to think about the risks to the stability of the system to the extent that it starts to put pots in place—i.e., that suspiciously looks, walks and talks like a levy and it looks, talks and walks like a safety net but it may just be called something else. Without it, I do not see how you could have stability in the system which is 100% devolved retention of business rates.

**Andrew Hetherton:** I was looking at it from a point of view in terms of where you are on the cusp. The big problem areas could be, for example, down in Hampshire where a number of local authorities are going to work together. How are those that are just on the edge going to cope or that are not within a major scheme? That is similarly so in the north.

**Q134 Mary Robinson:** You mentioned working together and, Mr Nolan, you said earlier that local authorities may have to come together in local groupings to pool risk and insure against it. Should redistribution be regionalised then and, if so, at what scale?

**Sean Nolan:** The answer is, in principle, yes, in that it gives an opportunity for things to be done at some sub-national basis, rather than nationally. Back to an earlier question, we really need to know what these £13 billion of additional new spending responsibilities are before you decide which regions you think you are talking about. We do not know. People points of reference at the moment are in reference to the formula grant so they are thinking of regions in that context. We do not know if that works at the moment because we do not know what those £13 billion are unless regions come first and you find services afterwards. It could work and it is logical you do it at some sort of sub-

national basis. Actually, I would find it very difficult to say what the regions should precisely be until we have a better grasp of what the additional responsibilities will be.

**David Magor:** I am nervous about regionalisation. We need to be sure what effect that is going to have. You need to look at the whole local government map for England; you cannot afford to just look at regions. My fear is that the areas outside the trial areas, for example, will lose out. You have to look at the bigger picture. Distribution being regionalised is something that has to be very carefully considered, and I am not convinced.

**Q135 Julian Knight:** What principles do you think should determine when a reset takes place?

**Andrew Hetherton:** From the point of view of the resets at the moment, we were due to have one from 2013 to come up shortly. With the welcome prospect now of a further consultation on revaluations, the fact that we might move to three-yearly revaluations is one that needs to be carefully considered. Also, there are significant decisions in the courts with regards to a recent case in respect to the City of London offices and how that is having a massive impact on rental values in central London changes to the central list. There is also other material change in circumstances. From a rating perspective it is a common theme, but those could include, for example, closures of major power stations, the impact or ascendance of particular retail developments and also, potentially, major socio-economic changes within a particular region. Those could all affect either one individual local authority or several local authorities. Those need to be carefully considered.

**David Magor:** The statement that was made when the original legislation came out was that a reset should take place when it was felt that, "Resources no longer met the changing service pressures sufficiently within individual local authority areas". That was the statement that was made. That statement still holds good. Look at the steel industry, for example, the closure of steel plants, what the impact of that is, and how that affects local authority service delivery and the types of services that they deliver. Going back to the point Sean made, what are these new responsibilities and how will it affect it? On the list that Andrew has mentioned these things all come in but we must not forget the original principle around resets that was set when the new scheme was introduced in 2013.

**Sean Nolan:** The point of the reset debate is a philosophical one but it is basically that you wanted to give sufficient time for the benefit of whatever you have done to promote growth to accrue to that local area. That feels logical. If you then put that into the context of 100%

retention of business rates the opposite pressure on that incentive is: what about needs changing? The steel works closing, for example. That is the dilemma. It is not scientific; it is a judgment call. You want something that is long enough that does justify what could be longer-term infrastructure investment because all this on the incentive horse is about local economic growth. You do need that incentive. If people thought you were going to reset it every four years, in local authority terms, from my days there, that is quite a short time frame. That really would get in the way of your enthusiasm.

Equally, if you are on the front end of major population changes, and we can allude to those, or you are on the front end of major economic shocks—I do not mean economic in the sense of global contraction, but literally an industry deciding, “We are out of here, we are into some other part of Europe or the far east”—you are going to feel massively vulnerable. When I talk about a principle, the longer you have the reset period the more you need some kind of pool or some kind of resource internally and in the system that is somehow able to help those areas that are suffering or are suddenly faced with what would be measurable and quantifiable shifts in population and/or shocks to their income. That is if you have 100%. The Government of the day will not have a spare pot of money once we go to 100% retention and say, “We will bail in.” It will not work that way.

**Q136 Julian Knight:** Mr Nolan, I want to press you on one point here. What we are talking about here is a baseline reset and what you are talking about is flexibility around that. Is that correct?

**Sean Nolan:** Yes.

**Q137 Julian Knight:** What should the baseline be? Should it be five years or 10 years?

**Sean Nolan:** If I was thinking in infrastructure terms I would be thinking about eight years. I have to also add that in this 100% world, with the economic situation we start off with, we are going to have to be very grown up about how would you deal with those situations where needs are changing quite dramatically? Define “quite dramatically”. We would need to have some settlement out there that people can look to as being some kind of relief in the context of needs could change a lot. Four years is too small; eight years feels about right; you could argue 10. I am talking about what that means to incentives on investment. I repeat: my nervousness is that if you do that, you are just riding the incentives horse and you are forgetting about how we deal with real shocks; I do not mean lack of energy. I mean real shocks: population shifts and economic changes outside of the control of the local area.

**Q138 Julian Knight:** Why eight years? Why not seven? Why not nine?

**Sean Nolan:** What was in my mind was I was thinking of two CSR cycles. That was the only logic.

**Q139 Julian Knight:** Can I ask the other witnesses the same question of the baseline: how many years?

**David Magor:** It was originally set at 2020 when we came in in 2013 unless exceptional circumstances occurred. That is the situation. You set the period, but you need the flexibility to bring it forward if anything exceptional happens. Providing you have that flexibility I can see no difficulty. When you have a revaluation you can alter the tariffs and top-ups without having a complete reset. Providing you have got the flexibility assurances it can be four years—it was 2020 from the original arrangement so that was seven years—or providing you have got the flexibility to do something about it in the intervening period I do not see any problem with a seven or eight-year period.

**Andrew Hetherton:** I tend to agree. My experience is more in terms of the valuation and revaluation that you may be coming onto.

**Q140 Julian Knight:** How well would three-yearly revaluations keep up with changes in the UK property market?

**Andrew Hetherton:** That is an interesting one because quite a lot of pressure at the moment is about the transparency of the system and the evidence that people are relying upon. A move to a three-yearly revaluation needs to be coupled and there has been a call from many for an occupier and rental register. That will provide an opportunity for many to have greater confidence. A more frequent revaluation is also going to reduce the amount of notional refunds that a rate payer might see by having appeals in the system, whereas at the moment, with a seven-year revaluation you effectively, at 50p in the pound, are going to get £3.50 for every RV pound that you save. On a three-year revaluation you are effectively going to see £1.50.

The other issue is about that availability of rental evidence. With three-yearly revaluations, what you are going to see is a need to review how that process works. Certainly from a rent review perspective, the evidence on which the valuation office relies can be difficult to obtain. You can find that rent reviews are not settled until a year after the rent review date comes to fruition. One way of overcoming that must be to make that information more transparent; it gives credibility to people's assessments and transparency to the system.



**Q141 Julian Knight:** There has been lots of talk about discounts and appeals. Should we be looking to widen the scope of the business rate base and, if so, how do we do that?

**David Magor:** I have mentioned the central list going to local authorities at least three times. I will mention it a fourth time because those rateable resources quite properly belong to the local authority. For missing rateable value, we need to make sure that the current rating lists are accurate. My institute has been working with the private sector on looking for missing rateable value. We have already found £64 million free money for the Treasury they did not pay us. The reality is that there missing value out there. We need to ensure that the list is accurate. There is a possibility of reducing exemptions; it was a little disappointing to see that there was nothing in the road map to deal with exemptions in business rates. The exemptions have become far too generous and they have a wider impact, particularly in relation to charity shops and other areas. More can be done to include vacant sites into the rating system. It will be quite easy to value those on a highest and best-use basis. That would actually encourage the development of those sites.

One assumes that sooner or later fracking will become commonplace. They would be very significant rating assessments. The Valuation Office Agency made a few estimates of what they expected that to be. Looking for new sources, I still favour a transaction levy on internet retailers. I would use that money to improve the high street. That seems to me to be poetic justice. Of course the problem is that more high street retailers are using the internet as well, but I do not see any reason why they should not contribute. We really need to do something about that about being very passive about it.

**Julian Knight:** John Lewis loses both ways in that way. Do you have any thoughts, Mr Hetherton?

**Andrew Hetherton:** I am very much the same as Mr Magor.

**Sean Nolan:** I tend to agree. One thing that I know in local government that is a challenge is that in terms of current methodologies you do get the internet trading and all that warehousing. That is generating quite a lot of value, but, in a sense, is not easily caught by the current system. I support the point about central lists, but to make the point more generally, I am assuming that when Government talks about 100% of business rates being retained locally that does mean 100% of business rates—i.e., including the central list, one hopes.

**Andrew Hetherton:** One final comment is that we have to go back to the first principles of what business rates are and the way they have been set up. They are a property tax. It is a very clear and sustainable tax. It generates good revenue for both local authorities and central Government. Should you link in other means of taxation and tie it to some form of property tax? Property taxation is best in one part. When we talk about going for an internet sales tax, it is extremely difficult to be able to do that and link it to property. It should be separate.

**Q142 Jim McMahon:** I was going to come onto this later, but it makes sense to follow on from the introduction about the internet sales tax. It struck me that last year internet retail sales increased by 10%. If it continues at the current rate in two years' time, we will be spending £1 billion a week on internet retail. It strikes me that we need to capture the value of that to local areas if the world is changing in that way. We are having quite a technical debate and maybe this point is for later witnesses. However, businesses are two-fold. They are income generators, they employ people and they pay business rates that fund public services. On the high street they are also the community. When the community notices that the high street is declining that affects confidence in the community and how communities function. I would like to give an overtly leading question to ask whether there would be support for the introduction of a, say, 5% internet sales tax if that was directly going to save high street business rates.

**Andrew Hetherton:** I am no retailer, but when I speak to my retail clients, one of the things that concerns them is the way that they are doing business by actually investing in their estate and offering the likes of click and collect. They asked the question as to why, necessarily, they are going to be caught by an internet tax, as well, because they are trying to drive an additional presence within town centres and within shopping parks. Do they get hit with a double tax?

**David Magor:** It is interesting because an internet levy has been looked at all around the world. It is causing a problem everywhere and there is deep concern that there is no contribution, particularly in those countries where there is a very strong traditional of property tax. Something has got to be done about it. The traditional high street is part of the community; you are absolutely right. The efforts so far to rejuvenate the high street have not been that effective and not that much money has really been put to it. I say a transaction levy in order to try and get around European law, particularly in relation to VAT and sales taxes, which they are very nervous about. There is plenty of international evidence of—not attempts: the reality that internet levies are being raised, are being charged and they are very effective. I do not see any reason why we should not at least consider that as part of

the overall structure of government finance. As Andrew quite correctly said, it is not a property tax. I have this dream of creating a virtual high street with virtual assessments. That would be very good.

**Q143 Chair:** I recollect from last time we had some evidence that we might even look at a rolling reset where the eight years was not simply a cut-off and everything came back to square one. The benefits from additional rates of income would last for eight years in each case. Would that make more sense? Would that be possible to do in this complicated world we are going to move into?

**Sean Nolan:** It feels to me that that is doable. Obviously, it is complicated. The balance is still what I was trying to allude to earlier, Chairman. It is the behavioural signal that is most important in this. Actually, you need some trade-off, particularly when 100% has been devolved, if I can use that phrase. You need something locally that people can still feel it is worth making an investment in. Equally, Chairman, if you are caught on the needs horse where there has been a shock to the system or a major population change—

**Q144 Chair:** We need to deal with that. Actually, if it is eight years full stop and then you start again, the average benefit time is only four years.

**Sean Nolan:** You can change the terms of reset.

**David Magor:** We have an opportunity to look at that. Obviously the working groups will look at that over the next three months and that is something that needs to be looked at.

**Q145 Kevin Hollinrake:** This incentive is really important, is it not? It is whether you retain a proportion of the growth going forward or if you set a benchmark for what growth should be then keep the surplus, for example, then that still drives the incentive beyond the reset.

**Sean Nolan:** That would be my view, but it is the balance you would have to agree with.

**Q146 Kevin Hollinrake:** Could we touch quickly on valuation, because you mentioned clarity, Mr Hetherton. You alluded to this occupier register. Are you talking about giving more clarity around what the basis of your valuations are to other businesses?

**Andrew Hetherton:** When a rate payer comes to look at what they are paying and when they compare it to the rate that they are paying in the current cycle, there is a significant difference. When it comes to revaluation everything is reset. Certainly, the research that we have

done shows that necessary rental values, particularly in the retail sector, are going to fall in particular locations. There will be some difficulty in people reconciling the fact that their rateable values have fallen, but in fact how much they are paying will be not necessarily going down as much as perhaps the rent that they are paying. That is a massive problem for business; they would not understand why if rent has gone down I am not paying less.

**Q147 Kevin Hollinrake:** When you get to appeals, a lot of appeals are brought forward because there is a misunderstanding on the basis of the calculation in the first place. Would it not be better to provide that evidence about how they arrived at the initial evaluation so people can see that?

**Andrew Hetherton:** You are right. I have heard it described as: "People need to be grown-up. Businesses and the valuation office need to be grown up in terms of being able to exchange information. It happens in the rent review sector. Landlords and tenants share information." At the moment, the problem that we encounter is a resistance from the valuation office and it is before you in the Enterprise Bill in terms of how that information is disclosed. Yes, there are measures by which that information is going to be disclosed once certain steps are gone through. Actually, by having a register of both occupiers and key rental information, or where you can get that information, this would benefit all parties. The overall aim of this Government is, rightly, to reduce the number of appeals, and if you can do that by having that register, then it will benefit everybody.

**Q148 Kevin Hollinrake:** In terms of business rates, billing authorities have the dispensation now to vary business rates with potential reliefs. We have heard quite a lot of evidence that billing authorities have not used that. Is that a fair criticism?

**David Magor:** They have considerable discretionary powers. Obviously, since the introduction of the retention scheme in 2013, 50% of the cost of those decisions impacted locally. That was a factor. The real issue is: should it be a factor? The reality is that local authorities must not fetter their discretion. There is plenty of case law on how that particular issue is dealt with. Sometimes local authorities have to make difficult decisions in relation to exercise of their discretions purely and simply because of the impact of state aid rules. State aid comes into this and so local authorities could actually make a discretionary decision that would trigger the state aid rules. That would not help the rate payer at all.

There are discretionary powers; local authorities should be encouraged to use those. They just have to be careful when making those decisions

they have guidelines as opposed to policies. You cannot have a general policy because if you have a general policy, you are fettering your discretion. They have to look at each individual case on its merits. There are lots of different forms of discretion that can be exercised. The decision-making has to be careful, particularly when the full cost of that decision impacts locally.

**Q149 Kevin Hollinrake:** What about abolition of uniform business rates? Was that the right thing to do? Will that stimulate growth? Are there other ways that can be achieved?

**David Magor:** It would be a disaster. You mean the abolition of the property tax or just of the uniform business rate?

**Kevin Hollinrake:** The uniform business rate.

**David Magor:** You would go back to the pre-1990 days. Again, that is quite interesting because if you go back to pre-1990s, people forget that we used to have equalisation schemes then. I worked for Oxford City Council in those days and it was per head of the population. We used to get very cross because our students were counted as fifths. It was a very strange system but the creation of the multiplier and the certainty that was created by 1990 was welcomed—not the certainty around the community charge, that is best forgotten, but the certainty that the multiplier gave business was welcomed. The rules that are being proposed—particularly in relation to the ability to reduce the multiplier, but not to increase the multiplier—give certainty that business requires.

Of course, the property tax will never be popular. It is not popular in any part of the world. It is a major tax in the UK as it is in three or four other countries. Because of the extent of that tax liability you are going to find situations where the taxpayers are very unhappy paying it. It is a direct property tax, it is a certain tax, it yields an awful lot of revenue and it is a successful tax. You must not lose sight of the fact that when the IMF and the World Bank were dealing with Portugal, Ireland, Greece and Spain to sort their finances, the first thing they ordered them to do was to review their property taxes. You have seen revaluations and reintroductions of certain taxes in Ireland and a complete reform in Spain and Portugal. This is the reality: the property tax is popular in terms of the overall economic picture.

**Andrew Hetherton:** There is another point, though, which is in terms of how a varying multiplier is going to work. You are going to have different approach across 300-plus local authorities around the country. That is going to be extremely difficult to manage for any business that has a presence in every high street across the country. It is not a

simple solution. In addition to that multiplier, you have bids, you have special authority supplements and you have transitional relief calculations.

**Q150 Chair:** Why is it difficult what the multiplier is? The business will get a bill.

**Andrew Hetherton:** If you get a bill, it is actually about understanding and budgeting. Many clients that I work for want to see certainty about the forecasting of what costs they are going to have in order to make a decision whether or not they are going to open in that particular high street or anything.

**Q151 Jim McMahon:** I do not understand that at all, because if you are a business looking to expand and open a new facility, the rate or value of that premises is not just based on the use, of course; it is square footage and how the units are divided up from storage, from toilets, from kitchens to retail space. You always have to look at it on a like-for-like individual basis, of course.

**Andrew Hetherton:** It might be from the point of view of people looking from an existing building, but if you are looking at new developments and the question is, "What is the valuation officer going to assess it at?" it is more of a problem. Yes, you get a bill, Chair, but we know that bills need to be checked and they need to be processed by teams within either specialised agents that do it on behalf of clients or the retailers themselves.

**Q152 Kevin Hollinrake:** From a business point of view, I would rather that bill be as low as possible. What this is about is trying to get local authorities thinking about how they attract new business to that local authority area. One way of doing that may be enterprise zones or it may be across the board in terms of reducing rates here compared to other local authorities.

**Andrew Hetherton:** I agree with that principle, but there are add-ons that you need to factor in.

**Sean Nolan:** On your point about discounts, there is no correlation between business rates and needs. If you go to a world where it is 100%, where local government services are paid for by business rates then you are having to make a very complicated value judgment locally. If you decide to offer a discount and relief—which is clearly a massively valid thing to do from a business growth point of view—you are also playing into that calculation and not just whether you attract the business, but how do you pay for it? What is the impact on the



services you are dealing with? That becomes quite a complex calculation but local authorities should be up for it.

The bit about uniform business rates and moving away from that clearly opens up the possibilities of competition between different areas for attracting businesses. That one, in my opinion, is quite complex. You clearly could drift out of areas that make life even more difficult for them; you could say that is the right thing to do and that is what it is about: competition. Equally, at what point do we think, "Hang on, are we going to have some kind of safety net?" That extension of policy down the line is not straightforward. I understand the point of it, but it has consequences.

**Q153 Kevin Hollinrake:** It gives autonomy. In terms of the infrastructure premium, you mentioned bids. An infrastructure premium is like an uber-bid, effectively. Is that the right thing to do? Is it going to be popular with business? Is it going to be popular with local authorities?

**Andrew Hetherton:** Certainly, providing you have engaged with the local community. I know that is something that comes through the bid process at the moment. It is about having that wider aspiration to develop an infrastructure project across an area. It comes back this issue about those that are just on the cusp of it and how they are going to be potentially just outside. We already know for Crossrail everybody is paying for it, but if you happen to be down in Croydon you might have the prospect of Crossrail 2. Ultimately everybody is paying for that at the moment.

**Sean Nolan:** Do I interpret your question as being the infrastructure premium around devolution deals where local areas have been allowed to—

**Kevin Hollinrake:** Yes, absolutely.

**Sean Nolan:** If you go back to my analogy of the four horses that is quite complex and needs to be got right for the whole country. I am actually quite nervous, frankly. The analogy that I would employ here is that it is like the Government saying we are all going to drive on the right by 2020, but we are going to trial it in a few areas beforehand. We do not know enough at the moment, allowing a local area to keep 100%, what that will pre-empt down the line when you do the 2020. This is a complicated enough challenge just to get the 100% thing done, with the four horses I talked about, without introducing new moving parts by pre-empting decisions later, by saying, "This area currently can have another 100%". It is about a sense of how you end up with a coherent solution at the end when you have already pre-

empted your judgments by deciding now to give a local area 100%, but you have not worked out how the scheme will work out nationally.

**Q154 Kevin Hollinrake:** If you ask any businessperson in an area, they want infrastructure, don't they? I am not saying there are not some issues on the premiums if you are outside the catchment for that particular infrastructure but that is what they want. Why would you wait another 10 years to be able to trial something like this?

**Sean Nolan:** It is interesting because in a sense you could still do that in the current scheme. I guess what I am preaching about is there are short to medium term challenges to get it to work generally for the country as a whole. The observation I would make is that if we have now decided, as the Government have, that we are going to do this by 2020, in absence of what they are going to do and what spending responsibilities they will be devolving to match this other £13 billion, the more you start deciding, "This area is 100%," you are going to lose your flexibility down the line. If you have to come to a judgment that, "I have to move resources out that particular area when I have just said you are going to keep 100%," then the more you do that the harder it becomes.

**Q155 Jim McMahon:** We are looking this in a very narrow way, which is about one element of taxation that is linked to property so that means we can very easily identify it to a local area and that is why we are having this debate. It is the reason why it is the first real sense of fiscal devolution to local areas. In the move to devolve resources and responsibilities down would you not accept that it is not one of the most logical ones to devolve in that mix and, notwithstanding the issues and concerns around it, it is probably better that we start here than somewhere else, such as VAT, for instance?

**Sean Nolan:** My personal view is absolutely. I repeat that there are a number of things to get right to land it safely in 2020. Everyone has been calling for it so it would be too late now for people to say, "It was the wrong idea. We did not really mean it." Whether it is how we deal with needs, whether it is how we deal with safety nets, all these things would have to be thought through so that we do have something that lands safely in year one and actually is relatively stable in the sense that we do not have something that automatically has too many tensions in the system. I am enthusiastic about us doing it but I am equally enthusiastic about us doing it safely.

**David Magor:** This is really important. It is a great opportunity for local government, but you have really got to sort of the mechanics of it. The next six months is very important that the advisers from the OGA and DCLG actually look at the models and make sure they work. This is

an opportunity that must not be missed by local government. It has to be used effectively to push the localism agenda but, at the same time, to actually encourage local economies, pick up some of the localities that are suffering and give them real opportunities for the future. It is a challenge for local government but it is a challenge that must be met.

**Q156 Jim McMahon:** Is there confidence amongst the three of you that there is—with the time that there is and the process that has been laid out—time and opportunity for full and proper consideration of the points that you have raised?

**David Magor:** Yes, absolutely. Progress has been made since 2013. The lead-in time to 2013 was not that long, but progress that has been made since 2013 and these proposals are on the table now. As Andrew said, we have got the changes taking place with relation to the Enterprise Bill and there are other things that are being suggested in relation to small businesses. The whole package is quite exciting; local government needs to grab this package and make sure that it works.

**Sean Nolan:** I agree. I would be confident, but we have until 2020, which is not too far away. We will need every minute of that. My counsel is: let's not introduce even more moving parts to what is already a fairly complicated thing to get right.

**Q157 Chair:** I am still worried about these horses. The horse representing equalisation and the one representing incentives representation are pulling in opposite directions. We took some evidence in a previous session and there was some talk about whether it was really possible to devise a system where you could have opposite forces within the system and whether you might not need an extra element of Government funding to deal with equalisation, assuming that they would then devolve even more powers to local government as a result. Do you have any reflection on that?

**Sean Nolan:** Totally, Chairman. It is a thing I have heard elsewhere and that is what I was trying to allude to in my opening comments. Under the context of the Government devolving 100% of business rates, you are then saying to central Government, "By the way, we want you to have a separate pot to deal with these kinds of equalisation." I do not think it is going to happen in the context of the financial situation we are facing. They will say, "Sector, we want you to come up with a solution yourself." I would offer the fact that they do pull in opposite directions. In a sense, that is life and it is even more pronounced with business rates; it does not correlate with needs spend on local government services. Therefore, you are going to have to find something that will hold this in a reasonable amount of equilibrium.

I hope I am not giving up too early, but in the current economic situation, which I think is going to go on for a long time, there is not going to be a spare pot of money that can make these adjustments. Sectors are going to have to think very carefully and sensibly about how it introduces something that will equal equalisation and equal responding to sudden jumps. The equalisation could be dealt with in the way—David has spoken well about it already—DCLG introduced top-up and tariffs in 2013. That was a form of equalisation. At least it looked in the current formula grant at that moment. They could that again in 2020 but we do not know what the £13 billion is currently spent on, so that is part of the challenge. Thereafter, the bit that troubles me is it is unduly optimistic to imagine the Government of the day will then step in and somehow deal with needs outside the system once it is devolved 100%.

**Chair:** Thank you very much all of you for coming to give evidence. That has been really helpful to the Committee. Thank you very much.

### **Examination of Witnesses**

*Witnesses:* **Mike Cherry**, Policy Director, Federation of Small Businesses, **Tom Ironside**, Director, Business Regulation, British Retail Consortium, **Chris Richards**, Senior Business Environment Policy Adviser, EEF, gave evidence.

**Q158 Chair:** Thank you very much for joining us this afternoon. For our records, could you just go down the table, say who you are and the organisation you represent, please?

**Mike Cherry:** Mike Cherry. I am the National Chairman for the FSB.

**Tom Ironside:** Tom Ironside, Director of Business and Regulation at the British Retail Consortium

**Chris Richards:** Chris Richards, Senior Policy Adviser looking after business rates and devolution at EEF, the manufacturers' organisation.

**Chair:** Thank you very much for coming. Mike, Cherry, congratulations are in order. You have just become the National Chair.

**Mike Cherry:** I have, Chairman. Thank you.

**Q159 Chair:** How do you think the Government has so far performed in its approach to business rate reform?

**Chris Richards:** If you look at the two reviews they conducted—the administration review and the structural review—that dredged up a lot of issues that I do not think the Treasury and DCLG have fully understood. There are issues around, for instance, manufacturing, around plant and machinery and wider issues around the stability of the system. If they were to do the review now they probably would start off with some core outcomes and then perhaps do a more fundamental look at what some of the issues are, rather than this iterative process that we recently had.

**Tom Ironside:** Our perspective is quite similar. We think that the measures that were announced recently show there is focus on some of the right issues. There is obviously an issue around the timing of their introduction but for us they do not address some of the fundamental underpinning that, for an industry that has a process of structural change underway, we view as being really important. There is an issue there about the sustainability of where the business rate system is currently at—simplicity, as well, both in terms of reliefs and exemptions; we believe there is something there that could and should be engaged with.

**Mike Cherry:** Clearly, with the current context around the issues that small businesses are facing at the moment, we were very pleased indeed with the announcements in the Budget last week. There is still much needed work to be done on the reforms, especially around localisation and particularly around the appeals process that is now being consulted on and suggested is now being put into place. Also, a lot of the anachronisms and the anomalies in the system are not being address at the present time.

**Q160 Chair:** Whenever there are criticisms made on business rates or suggestions for change, they always seem to be made by organisations or businesses who want to see their share of the business rate reduced or what they pay reduced. Is that not a bit optimistic for businesses to expect that everyone is going to be able to pay less in the current circumstances?

**Mike Cherry:** No, the problem that you have at the moment is that there is a lot of unfairness in the system, particularly for those small businesses that are not outside of the latest announcements. You also have to look at the fact that you are dealing with a system that is on a fixed yield policy, which means, irrespective of the number of players within the system, the yield still remains more or less the same. That creates problems. We currently have, according to our recent surveys,

around 7% of our members who are paying more business rates than they are in rent. That cannot be right.

**Q161 Chair:** Small businesses must be cheering now. Is that not a problem for the Government: that they give small businesses a windfall—even your press release has managed to accept you have done fairly well out of the budget—and the next complaint is there are some slightly bigger businesses that now feel totally unfairly treated?

**Mike Cherry:** No, Chairman. If you look at what we have been proposing, when you look at the fact that 64% of businesses only garner between 6% and 8% of revenue, you will understand why we were cheering so much around the budget announcement to exempt those at 12,000 rateable value.

**Tom Ironside:** The fixed yield is a real issue for the retail industry. If we look at where the business rate system is heading currently, we can see that we are already in a territory that is not looking particularly sustainable. We have a business rate multiplier that is approaching 50p in the pound. At the time of introduction in 1990, as you know very well, it was much more in the region of 34p in the pound. It is quite a difficult situation that we find ourselves in at a time when retailers are looking closely at their property portfolios as the approach of consumers and the potential of technology changes some of the dynamics around the industry.

**Chris Richards:** From the point of view of manufacturers, one thing that has not come out of conversations I have had with our members is the look around this as a cost. Manufacturers largely see business rate as a tax on property. When they are looking at investment decisions around their property, because their sector is more likely to be owner-occupied, they will look at this more on the investment side of things. That is why things like plant and machinery fall out, where if you do invest in plant and machinery within your property, your business rate increases. That is the kind of level that the manufacturing sector looks at business rates.

**Q162 Chair:** You all want to pay less, don't you?

**Chris Richards:** The view that is coming back from manufacturers is that actually they want a stable system. They want a system where it actually encourages them to invest; then, looking more broadly at incentivising growth, having the local authorities invest within their local area to build up their local business environment to make it more attractive.



**Q163 Chair:** They cannot invest without getting money from you in the first place, can they? Is it a chicken and egg?

**Chris Richards:** To some extent it might be. Manufacturers will not start off from the point of, "This is too high; it needs to be lower". It is more, "How can we make the system more stable and allow them to invest with a bit more certainty?"

**Mike Cherry:** You also need to have fairness in the system. At the moment you have a property tax that is clearly levied before a business even makes its first pound of sales.

**Q164 Chair:** I cannot hear anyone coming forward with suggestions about how some businesses could pay more to make sure those who are unfairly treated should pay less.

**Chris Richards:** If you look at how the system works, particularly around revaluation the issue is you do get flexibilities where properties are revalued with each revaluation cycle. Therefore there is always going to be a bit of uncertainty. Some will end up paying more, some will end up paying less based on that kind of hypothetical rental value. We are not looking for how to pay less, it is more about how does the system overall work and that is what we are trying to get out of a more stable system going forward.

**Q165 Kevin Hollinrake:** Is not what business wants a level playing field? Realistically, you cannot turn the rating system upside down or it is very risky to. The implications are almost impossible to assess. I can certainly see the internet sales argument and I can see the plant and machinery argument. To say, somehow, that we are going to fight one corner of this it is not realistically to want to alter the business environment like that.

**Tom Ironside:** To be very clear, from a retail perspective, we already pay 25% of business rate within the industry. We have 6% of GDP GVA. We account for around 11% or 12% of all business taxes. We do not think that the way to go is to try and find additional mechanisms within business rates to address internet retail when the line between what is a traditional retailer, an online retailer and any other sort of retailer is becoming increasingly blurred as they respond to change in consumer demand and change in technological activity. That does mean that the industry is any less committed to its role on the high street. It would be strange to look to business rates as a mechanism to raise additional funds from the industry in relation to some notional value around internet retailing.

**Q166 Kevin Hollinrake:** That was not the proposal from me. My point is: is this is a zero sum gain? However you all want to fight your different corners, the reality is, to wait until a business is making money before it starts paying business rates is just not realistic. What I would have thought from the business profession—and I was in business for 25 years before doing this—is that you are looking for a level playing field where we can all compete and the creative destruction of capitalism can win the day.

**Mike Cherry:** For fairness in the system, you still have the anomaly where manufacturers or large companies who need space are rated on that whole space. You now have internet companies in particular and high-tech companies that can be working out of somebody's bedroom. That brings unfairness into the system where it is a manufacturer or whether it is a retailer. It is good for the individual with the high-tech company that is running it from home. If I come back to the fixed yield policy, the BAA's own figures meant that 20% increase in the multiplier would have been necessary if the 2015 revaluation had actually gone ahead. We had seen a rise in almost 8,000 business payers when we had seen a fall in rateable value.

You have those anomalies already in the system; surely we need some fairness into that that is more related to the economic environment that a business is working in. At the moment, we have very low rentals—or rentals are tending to move low—and we have got problems in the economic environment, yet we are paying some of the highest rates that we have known for some time because we have not had that revaluation and it is not related to economics.

**Tom Ironside:** We were looking to see whether there would be more of a solution that would sit within the business tax road map. For us, we are perhaps in a different position, in that we do believe there should be a general downward pressure on the level of business rate and its contribution. However, looking within the context of a business tax road map approach, there may be other ways to balance of taxation more generally. That would be where we would come from in relation to this issue because we can see have one of the highest commercial property tax levels in the OECD and it falls very heavily on property in terms of businesses.

**Q167 Jim McMahon:** It has to be balanced. There is always going to be a schedule of taxes that society has to pay, because as a society we demand decent public services and a quality of life in return for that. There will always be a schedule; there will never be one and that does it, because life is more complicated than there. It felt that there is a contradiction in the evidence, which was that you were reasonably critical of the idea that you charge a tax on a property whether you make money

or not. That is true. The minute you occupy that premises, you are liable to pay rates regardless of whether you make any money or not.

Juxtaposed with that was the point about an internet sales tax, which would be a tax on selling things and making money. Surely, in all this there has to be some balance because although, as a business you must see the value in this, trading is important. It is also very important for communities that they have a viable high street that is part and parcel of the community. Surely, with internet retail growing 10% last year, taxation needs to catch up with that changing world.

**Tom Ironside:** To be very clear, we do not support any form of internet sales tax. We think there are already many systems in place that capture the value that is generated through sales. There are other sorts of taxation as well. One thing we really would not be in favour of is using business rates to try and capture that value.

**Q168 Jim McMahon:** How would you marry that then? If life was that simple, we would not have had such a debate in the House about Google and their tax arrangements, or Amazon and Facebook.

**Tom Ironside:** I am talking about internet retailing here, rather than broader internet activity. We do not have a locus in relation to that.

**Q169 Jim McMahon:** Do you have a view about an internet sales tax for international transactions? Can the UK address this?

**Tom Ironside:** That is not something that we have an existing policy position on.

**Q170 Jim McMahon:** If you do not support property tax and you do not support an internet sales tax, what type of tax do you support?

**Tom Ironside:** We do not support using a tax for that purpose. We pay 25% of business rate. We do not see that there is a case for additionality within the system.

**Chris Richards:** Manufacturers are not against a property tax. It is a tax that is used in a vast number of countries. It exists and, as you heard in the previous session, it is easy to collect as well. We are not arguing against a property tax. From a manufacturing point of view, it is the stability within the system that is important and whether or not it allows them to invest. Manufacturers have all been competing internationally and they would be looking at other countries in terms of their property taxes is and how competitive the UK's business rate system is as part of that. If they are making an investment, they need that stability, year on year, to know what their return on value is.

**Q171 Jim McMahon:** Would you not welcome, then, a closer relationship with the local area and the business that have chosen to invest in that area where the local authority could be able to say, “We do want to boost manufacturing engineering in our community and as such we are going to use the rating system to attract investment or expansion”? Would you not welcome that as a direct relationship?

**Mike Cherry:** We welcome the fact that the local authority should be totally devolved and has the opportunity to reduce the amount that a business pays. All the main business organisations are totally opposed and the Government recognised this in its announcement of the Budget that it should not be used to re-localise business rates.

**Q172 Mary Robinson:** Earlier on there seemed to be some comment about the inclusion of plant and machinery in the ratings and how that would affect you. Then we have had a discussion about the possibility of wanting to see a business tax road map. In terms of plant and machinery, there have been announcements and Government announcements that have given that additional relief to it and increases.

**Chris Richards:** The last full review of the plant machinery orders that governs what is and is not within plant machinery for rateable value was done in 1993, before the dawn of the internet and before any substantial work was actually done. Back then, the situation within British industry was completely different. Fundamentally for us—and again it comes back to this international competitiveness argument—other countries have looked to change their system. France, for instance, in 2010 removed plant and machinery from their system of local taxation on the basis, and I am quoting President Sarkozy here where he said, we actually want industry to sustain France by stripping out plant and machinery. In fact, they went even further and gave a 30% discount to factories within France. Looking internationally, the system, including plant and machinery, does not make it internationally competitive. That is why we were arguing quite strongly for it to be stripped out. We will continue to make that argument as well.

**Mike Cherry:** Not just plant and machinery: it also applies if you are putting in security—so, CCTV and other protective measures for your property. It is a disincentive to invest, basically.

**Q173 Mary Robinson:** The Government have been generous in the tax reliefs in terms of plant and machinery. In terms of the road map, is this relationship doing what we want to happen locally and also what the Government are capable of doing in terms of the national tax perspective. Can you see that working? I was puzzled that was not included in your thinking.

**Chris Richards:** Do you mean in terms of the capital allowances regime and how that has changed? We would not marry the capital allowances regime with the plant and machinery because, in a sense, the plant and machinery, which is rated, is quite specific set of different items. Obviously some companies will be looking at how capital allowances works within that. We can have a wider discussion around whether or not the capital allowances regime in this country is actually internationally competitive as well. Some people might argue not. Looking specifically at this as a property tax, it does not make sense for plant and machinery to be included within a property tax.

**Q174 Helen Hayes:** Most councils spend around three quarters of their budgets on children's and social services, and adult social care. Do you think there is an accountability problem with businesses becoming the majority funders of local authority but not necessarily the majority beneficiaries of services?

**Chris Richards:** You are always going to have that challenge. Any kind of tax system is meant to have that balance these things. Even at a national level, there is always going to be that accountability problem in terms of who pays the most. It is not necessarily something that businesses are particularly worried about. What we would like to see is any surplus in business rates revenue going back to local business environments so businesses can generate the jobs that they need to.

**Q175 Helen Hayes:** That was going to be my next question. What do you think the guide or the framework should be for local authorities to decide how they spend any additional revenue that is raised through business rates?

**Tom Ironside:** We would echo what we have just heard, in which the idea is that you get a virtuous circle for any surplus that focuses on economic development. The experience that we have from business improvement districts is that sort of positive engagement generates the right partnership between local business interest and local authorities.

**Mike Cherry:** We would see it as adding economic growth to the local area. We would see things like broadband, skills, transport, infrastructure and things like that almost having that money ring-fenced to make sure that economic can occur.

**Q176 Helen Hayes:** Do you think councils should have that responsibility for things like skills and transport? Many councils have told us that they would like to have that responsibility and a corresponding relationship between additional funding and those areas of investment that, as you say, contribute towards economic growth very directly.

**Mike Cherry:** There is certainly a cause for that to happen. You also, though, have to be mindful particularly when you look at infrastructure projects that goes across the cross boundary and the LEPs would have to be involved with that. Let's also not forget that the LEPs are going to probably be tasked with looking at the whole skills agenda and business support agenda as well. As long as people are prepared and are going to work together on all of this and it is going to benefit small businesses in their localities, we would be in favour of that.

**Tom Ironside:** We would tend to agree on transport. We can absolutely see the case that was just set out. On skills, we already have a very complicated landscape and we are only talking at a national level. One of the key areas that we are focusing on, as the apprenticeship levy moves forward, is how we can ensure simplicity to enable the maximum return on investment. There is a degree of trepidation about the idea that you could get more complexity arising from a localised arrangement, and it is about how that would be balanced as we move forward.

**Chris Richards:** We would echo that as well. When we survey our members, the number one issue that comes out is the issue of local transport networks. It needs to be addressed as an initial down payment for devolution. On skills, local authorities bandy around this term "skills", but they need to be quite specific about what they are trying to achieve. To some extent—and a lot of our members do echo these concerns—that they see a big budget attached to things like apprenticeships and think, "We need a chunk of that." Be quite specific about what you are trying to achieve, particularly when you think the more high skilled people get the more likely they are to be mobile and you lose that local connection anyway.

**Q177 Chair:** Is it quite possible that anyone could manage the Work programme a little better than it is managed now?

**Chris Richards:** I do not have a view on that, sorry.

**Chair:** That is one of the things the local authorities have suggested—that they might be involved in commissioning the Work programme.

**Tom Ironside:** We do not have a formal position on that. Our focus has been very much on the apprenticeships equation.

**Q178 Jim McMahon:** We verge in and out of the relationship between businesses paying to trade and the need to generate tax to fund public services that we all require. There is always a balance and we have



talked about that before. Really good businesses—not just good employers—that are forward thinking recognise the way they treat their work force has direct dividends back in terms of productivity. Surely you recognise and support the need for taxation to fund really decent childcare, education, skills and higher education because it is not just good for society; it is good for business too.

**Chris Richards:** Absolutely. If you think about the manufacturing sector, it pays above-average wages compared to the rest of the whole economy and has productivity levels above the whole of the economy average. It is not the case that manufacturers are looking for ways to squeeze their costs in that sense. Manufacturers are more likely, as well, to tend to operate and site themselves within an area for a very long period of time. Like you said, it comes back to stability. If they know what their costs are going to be going forward, they can make an investment and look at the return on that investment over a 10-year cycle, rather than having to manage this on a year-by-year basis if their tax burden is going to be shifting in that direction.

**Tom Ironside:** We recognise that a property tax has a clear place within the overall range of approaches that are needed in order to generate the funding that is needed for all the things that you just described. We have got to a place where there has been a distortive effect on our industry as a result of the burden, or the proportion of that, that sits with business rates. That is the nature of our concern. We think it has got out of kilter; it has got out of sync, effectively. That is where we are coming from. We fully recognise that businesses have a duty and a responsibility to pay tax on a whole range of different things, hence we do.

**Mike Cherry:** I would agree with what Tom has just said. There needs to be far more engagement between the skills agenda, the education system and small businesses. It opens up a whole new arena whereby we need to be making sure that our young people are indeed trained for what we need for the future. Let us be absolutely clear about this: we are not saying we should not be paying business taxes; what we are saying is—and Tom has alluded to this—that the business rates system now is so complex, so convoluted and so unfair that we need to have some fundamental reform to this as well. The announcement in the budget we very much welcomed but that is on a basis that when you have got 64% of payers only generating 6% to 8% revenue and you now have proposals for the appeal system to make it even worse for small businesses to actually make an appeal, surely transparency—as the previous panel were saying—has to also be part of this agenda.

It is fundamentally wrong that a business does not know the basis on which its rateable value is made so it can make an informed judgment and decision before it even either has to use a third party, and we know

there are some not-so-well valued third parties at the moment who will take small businesses for a ride. If small business could actually see that valuation, it would not necessarily either have to use a third party or could actually say, "I do not need to put an appeal in. I know it is fair; it looks fair compared to other competitors who I am maybe trying to compete with," and you have actually got that information to hand. That will be far more beneficial, not just for business, but also it would save the number of appeals that are currently clogging up the system; it would save the valuation office an awful lot of time and money, and, therefore, the Government. That, surely, should be the route map that we should be taking.

Alongside all of this, you should not just be looking at business rates; you should be looking at the overall way business taxes are dealt with. You have got to the stage now where you should not really be looking at any one piece in isolation.

**Q179 Kevin Hollinrake:** On that point in terms of transparency, I totally agree with you. I know it has been in an FSB manifesto as one of the policies you would like to see brought forward as well as the one you had in the budget last week. In the Enterprise Bill, you have this "check, challenge, appeal". Does that go anywhere near where you would like it to go in terms of transparency?

**Mike Cherry:** No. Until you get fundamental reform of ensuring that the business is allowed to know the basis on which its rateable value is raised in the first place you have a situation at the moment where the only way the business can actually find that out is once they have put the appeal in. It is very often when you have got to the doorstep for the appeal hearing. That is not transparent; it is not helpful; and it is costing everybody time and money.

**Q180 Kevin Hollinrake:** Would the owner/occupier register that one of the previous witnesses was proposing be a partial solution or a full solution to what you need?

**Mike Cherry:** It is something I am not aware of. It makes sense but it would obviously need to be looked at. If it stops people paying more in rates than rent it has got to be beneficial.

**Q181 Kevin Hollinrake:** It stops appealing because it costs everybody money. All valuations, rateable values and rents are based upon comparable market data. This would then bring all that information out in the open rather than having to ring round various agents to find that information.

**Mike Cherry:** Anything that brings transparency and reduces cost for both business and, by default, the valuation office has got to be welcome.

**Chris Richards:** The challenge—and I alluded to this earlier—within the manufacturing sector is the owner/occupation aspect of the sector. Primarily the issue there is around what is a hypothetical event. We are talking about sites that are going to be quite unique, usually quite geographically remote and trying to find a comparison is quite difficult. They will be going out and they do use rating assessors—that is the feedback we have had from members—to try and understand a bit more about how that hypothetical rental value has come up.

If you then go to the other end of the extreme, which is about 250 sites in the UK, which is the contractors valuation method that is an even more complex system that looks at what the cost is to replace the building and then trying to work out depreciation rates off the back of that. It is quite a complicated system when it comes to you actually owning the site. Anything that can improve that, like Mike said, and improves some transparency around what is included within that will definitely help.

**Tom Ironside:** To build on Mike's point in relation to transparency, if you take everything that he described then you place it alongside more frequent valuations you could get to a very positive dynamic, both in relation to appeals, relation to agents who maybe were not approaching things in the right way and also in relation to the relationship between rate payers and those flipping the rates. It seems like a very sensible way forward.

**Q182 Helen Hayes:** I have a couple of questions about the reset/revaluation period. What evidence is there that the current reset period influences economic development?

**Tom Ironside:** We do not have good visibility on the research. I was learning as much as anyone, I suspect, in the last session. We do not have good visibility on how it impacts. The only thing I could say is that you can see that there could be distortions as you approach a reset period as to decisions that are taken in individual local authorities or within combined authorities.

**Q183 Helen Hayes:** We have received some evidence that a lengthier reset period that perhaps rides out economic cycles can result in disproportionately high levels of payment during a recession period, for example. Do you have any evidence of the impact that that kind of situation has on rent payers?

**Chris Richards:** Between the resale or the revaluation period?

**Helen Hayes:** The revaluation period.

**Chris Richards:** We are probably slightly different to other sectors, in that the feedback from members was that long revaluation periods are preferable, primarily because then they understand what the rateable value is going to be for a longer period of time. As a result, they can plan and make their investment with a bit more certainty. The worry they have is if you have a more frequent valuation period, you start to introduce shifting rates that build almost year on year if you go to an annual revaluation, for instance. That is the level that they would prefer not to get to. I appreciate this might be quite unique to manufacturing but it is something that we made clear to the Government that five years makes sense. A lot of the members said even longer would be better.

**Mike Cherry:** We would slightly disagree with that for the majority of our members, insofar as more frequent revaluation would actually be more beneficial. It would bear more relationship to the economic cycle. It would also then stop any very significant hikes or, indeed, decreases that you get into the transition complexity of things.

**Tom Ironside:** We would agree with much of that. I would only add to it that with a dynamic property market within the industry actually having something that is more responsive along the lines of what has just been described is beneficial.

**Q184 Helen Hayes:** In the Budget, the Government announced they will introduce more frequent revaluations; at least every three years. For manufacturing is that too short of a period?

**Chris Richards:** We talked about the economic cycle. If you look at the last revaluation period in 2008 in the run-up to the 2010 rating list, now we had quite a significant event happening in 2008. If it had been a year earlier or a year after we would be talking about a completely different set of scenarios. Three years hopefully will not create that instability, particularly if you do have these economic shocks. If we are moving towards anything close to one year that is definitely something that would not be appreciated by the sector.

**Q185 Jim McMahon:** I am thinking slightly differently to the reset period. In just a couple of weeks, council tax valuations will be celebrating their 25th birthday. It would have been to university, got a job, got married and had kids by now. From what you are saying, would there be broad support for having different reset periods for different types of

uses? You would not have an all-out revaluation; you might have an eight to 10-year revaluation to manufacturing, you might have a different valuation for supermarkets, for instance.

**Tom Ironside:** That would add to the complexity of the system. That is my gut reaction. We have not thought carefully about what the ramifications of that would be, but I can imagine it would lead to less visibility rather than more so I doubt we would be that supportive of that.

**Q186 Jim McMahon:** I pre-empted that response slightly to arrive at the conclusion it would probably be a compromise somewhere in the middle.

**Mike Cherry:** A compromise is probably the best solution without adding more complexity to an already overly complex tax.

**Q187 Chair:** What is your opinion of the infrastructure premium, which elected mayors are going to be able to levy with the support of their LEPs, particularly the mechanism for getting approval for it?

**Mike Cherry:** We are in favour of it, so long as the small business community is engaged in this in the same way that they are with the bids. Some of those have been very well received. Our concern is, despite the announcements in the budget, that unless you have true representation around the LEPs, which are supposed to be the vehicle that decides on this, small businesses are going to be excluded and it is only going to be large businesses that actually make that decision. As long as they are involved, if it going to be capped at 2p in the pound, if it is going to produce some genuine benefits for small businesses, we would not necessarily be against it.

**Tom Ironside:** We are in a more sceptical place. We accept the proposal of the mechanism, but we have surveyed our members. There are seven retailers on LEP boards in the UK. We do not think they have a representative role, as in a clear representative mandate. The experience of what we have seen in business improvement districts is that having a much clearer business rate payer endorsement is desirable. 80% of business improvement districts move forward to successful operations. There would not be vexatious opposition, but there does need be a much clearer business rate payer endorsement than necessarily mediation through a local enterprise partnership.

**Chris Richards:** Similarly an infrastructure premium if absolutely the right direction to go down. We need to be spending more money on infrastructure in certain parts of the country. Anything that can add value to that and help businesses alongside that as part of economic development is something that we would support. The issue we have

with it, as has been discussed, is that if you are using local enterprise partnerships as the mechanism to give a sign off on that, is whether that is fully representative, particularly in areas such as the north east, which is going to be a massive area. Where do you decide to put the certain infrastructure that would benefit the entire north east rate payers?

That is why we suggest in our evidence it might be helpful to retain some elements of the current system where business might gain the right to call in a decision if they do not particularly agree with it. The current system is that local authorities can introduce a supplementary levy; they just have to have a business vote. No local authority has ever done that. Within London, it was introduced before that requirement was put in. If you had that better engagement and you were clear about what infrastructure projects will be funded by this, you perhaps would get a better relationship between businesses and local authorities.

**Tom Ironside:** That is a really good point. For us, it should be about the quality of engagement and the quality of trust between both businesses and local authorities.

**Q188 Chair:** The sceptic in me asks just one final question. Say a local authority wants to extend a tram system and put a new line in. It is then too big a scheme for a bid, but all the business that do not benefit from that particular line may well vote against it. Are you ever going to get agreement to spend money on quite a bit of important and costly infrastructure that will only service one bit of a wider city region?

**Chris Richards:** You might in that instance go for multiple projects instead or look at phasing the projects that benefit business over time. Particularly considering the way some business might choose to locate because of the infrastructure you might actually get businesses moving to that area to take advantage of that from another part of the levied area. It is not the case that business would vote against it; it is that the engagement needs to be there so there is understanding around why that project was chosen over another one.

**Q189 Jim McMahon:** That is LEP in most areas. The LEP will sign off the infrastructure development plans, even if they are not the decision-making body, although in many areas they have a role in that sense. Is what you are really pushing for better or more transparent representation?

**Mike Cherry:** That covers my point. You have not got small business representation within the LEPs that can get the cohesive view of the



small business communities to agree or disagree with that at the moment.

**Tom Ironside:** The same goes for the retail industry.

**Chris Richards:** Our worry is less on that side and more on the side that LEPs are not statutory bodies. If you get a disgruntled bunch of businesses, will they kick up a fuss and start forcing change on the LEP board itself? It is that background check that we are calling for; the right to call it in, not necessarily to say, "This is not a good idea," but just to call it in and try and get some engagement going forward.

**Q190 Kevin Hollinrake:** I can quite understand the need for engagement; it is so difficult. You talk about combined authorities that are potentially huge areas with a single elected Mayor. It is so difficult to engage with all those businesses across a place like Sheffield, Greater Yorkshire or Manchester. They are huge.

**Chris Richards:** Yes. It is going to be difficult. Different areas will tackle it in their own ways. From our point of view, we will be trying to encourage manufactures to engage with it not just on that regional level, but also the sub-regional level to look at what might be best for certain pockets of these different LEP areas.

**Chair:** Thank you all very much for coming in this afternoon and giving evidence to us. I appreciate it. That brings us to the end of the public proceedings.