EIC0869

Written evidence submitted by the Federation of Small Businesses

Firstly, thank you to individual members of the Committee for their engagement with us to date, and those who work for it for all of the time and focus that you have put in to the very serious economic – and social – situation facing us all as a result of coronavirus.

The Government's response to the crisis is probably the biggest practical restriction on the freedom of businesses to operate in our history, at least in peace time. The public health measures put in place by Government have put extraordinary pressure on businesses, jobs and the day-to-day lives of people throughout the country.

This has all, of course, happened for a very good reason – to protect the health of the population. The challenge for Government is to limit the economic consequences, and all the distress and harm they have and could bring, as far as is possible. In a collective national effort to protect the health of the population, we believe a collective effort to support people suffering the economic effects is the right thing to do both in principle and practice.

In principle, because it should not be the case that the cost of collective pressure is borne by some far more than others, and in practice, because Government intervention is necessary to reduce the short and long-term negative economic consequences we will face of such unprecedented limits on practical economic freedoms.

Among small businesses, the innovation, effort and creativity that has gone into trying to get through the turmoil of the crisis to date is something we are very proud of at FSB. The personal and business stories are as numerous and diverse as small businesses themselves. We have focused this submission in what Government can do to help.

While the challenges are huge in scale, we would not counsel despair. Small business owners are often optimists, because the challenges of running a small business at the best of times can necessitate it. Much action has been taken by Government already. More is needed, and there are significant gaps, but the principle that something can be done, and that people do not have to deal with this alone, has been proved.

In particular, we have focused below on the immediate challenge of the lockdown, what needs to be put in place to facilitate adjustment, to deal with the spectre of unemployment, potentially reduced demand, and balanced sheet impacts, as well as options for other stimulus and infrastructure spending.

We have not focused on every aspect of this crisis in this response, and would welcome the chance to give further evidence in person at the committee.

<u>Immediate lockdown challenge of cashflow and Government support schemes.</u>

CJRS and SEISS

For the majority of employers, their focus currently is on keeping their businesses alive and as many of their current staff as possible employed. The Coronavirus Job Retention

Scheme has undoubtedly kept many people attached to their firms and clearly averted mass job losses.

Similarly, those helped by the Self-Employment Income Scene (SEISS) will have had their incomes supported and thus maintained their attachment to the labour market. Although their employment takes a different form, in theory and in practice the need to maintain labour market attachment for this group is the same.

Flexibility in the CJRS is a welcome further innovation, which will enable a resumption of business activity in tandem with levels of demand as the economy unlocks. This will save jobs, allowing people to return to work part-time, and should enable a greater pace of recovery as activity resumes gradually.

Of course, the CJRS does not itself assist with the cost of work carried out.

Limited Company Directors

Many limited company directors and freelancers have been forced as a result of Government measures not to operate, or have otherwise found themselves unable to generate revenue given the limitations placed on the economy by Government, but have not received support for the income they would have otherwise received through dividends.

Government can and should make provision for limited company directors. It is not right that anyone who is suffering financially as a result of the public health measures should be left out of support, and it is also not wise from the standpoint of economic recovery. The UK relies on an army of limited company directors and freelancers for economic growth, they already face more uncertainty, risks and a lower level of protection than other workers, and recovery will be slower if so many are in a difficult financial position.

There is no shortage of practicable options for administrating this support, as both the Committee and FSB have put to Government. It should also be noted that many of this group don't operate out of premises eligible for grant support, but still face high costs – whether in equipment and, very expensive, insurance for those working in TV and live events, or a thousand other examples.

Grant support

Grants have provided significant protection for viable small firms who qualify for them – helping them combat the severe hit they have taken to their balance sheets for a crisis which was not of their making. But there are still many good businesses who cannot generate significant revenue and remain in need of more support. Many small businesses have fixed non-labour costs in the tens of thousands each month, so while very welcome, the support even for those who qualify for the grants, should not be overestimated.

Digging into the sectors, there are many small businesses who are suppliers to hospitality, tourism, or events and mass gatherings, who have been particularly hard hit and will not have benefited from grant support. Many businesses – such as those based on boats – have not benefited from grant support despite the large fixed costs and charges which they have no way of escaping.

The Discretionary Grants scheme could offer a solution. FSB wishes to see local authorities both encouraged to reach the 95 per cent mark of non-discretionary funding allocated, and empowered to use underspend, as well as top-up funding, to support small businesses struggling in their areas.

Local authorities should reach a baseline of 95 per cent allocation, of the number of businesses identified as being eligible for the grants under non-discretionary powers. Once this target is reached, HMT should then underwrite any overspend, up to a maximum of 5 per cent of each local authority's original allocation. This allows local authorities to use their top-up funding, as well as up to 5 per cent of their underspend from their original funds, without fear that they may be left with the costs, should those businesses claiming under the original system do so at a later date.

Late payment – a huge cash flow challenge

We are receiving increasing reports that smaller suppliers are being told they will not receive payment for work already having taken place. In some cases, work as far back as January has not been paid for.

The majority of small businesses (62%) have been subject to late or frozen payments in the wake of the COVID-19 outbreak, according to our latest study of more than 4,000 firms.

We are shortly to release a set of recommendations on this subject, which include:

- Make any big corporation that receives state or Bank of England-backed finance to help it through the current recession sign a supplier charter committing it to payment of small firms within 30 days without exception, while working with the BoE to shore-up supply chain finance and ensure said finance is used to pay small businesses swiftly.
- Give the Small Business Commissioner additional powers to investigate and fine repeat late payment offenders and make 30 days the standard definition of prompt payment as set out in the Prompt Payment Code.
- Establish a centralised relief pot for small firms within government supply chains that have seen payments frozen and, over the long-term, work to ensure 95 per cent of public sector invoices are paid within 30 days.
- Only hand work to Tier 1 contractors if bidders can demonstrate full compliance with the Prompt Payment Code or, failing that, establish Project Bank Accounts.
- Amend Financial Reporting Council guidance or legislate to force Audit Committees to appoint a dedicated non-executive director with responsibility for reporting on payment practices within annual reports.

At a time when Government has taken such significant measures to assist with cash flow, it would be remiss of Parliament and Government not to include measures to clamp down in bad payment practice in its response to the pandemic.

<u>Adjustment</u>

Covid-secure operation

While firms have absorbed large losses to date, it is likely that many will have to incur larger costs to continue trading in a "Covid-secure" way. 60 per cent of firms have said it would cost up to £1000 in terms of the set-up costs to comply with government guidance on working safely. However, 28% said it would cost between £1- £10k in terms of setup costs alone, and some hospitality businesses are reporting potential costs to re-open of between £15-20K. Grants linked to high "Covid-secure" costs, would help firms restart earlier, and prevent a situation where there are too many needless delays to re-opening.

SSP and isolation

We have welcomed the rebate of SSP costs for up to 14 days for employers with below 250 staff, in the event a staff member has to self-isolate because of COVID-19. However, we think new reinforced provisions need to be put in place given the vital importance of self-isolation to the effectiveness of the track and trace strategy. There are also the additional challenges of supporting people who have had COVID-19 and now developed secondary health conditions or who have to self-isolate more than once or who may continue to need to self-isolate/shield for a further number of weeks/months. Options should include ensuring employers with below 50 staff, having a full SSP rebate in all instances or else developing a new funding mechanism for those that need to self-isolate. Any such separate funding pot could also support the self-employed, if and when they need to self-isolate.

Commercial landlords

In terms of other adjustments that may need to be made, perhaps the largest is in property.

Many small businesses have found their landlords unwilling to negotiate on rent holidays in the current time. For businesses that rely, for example, on lunchtime office trade, this is a punishing cost that is impossible to meet.

Additionally, if there is a largescale reorganisation of where we work, including from home, many small businesses are tied to long leases, with high penalty clauses, and often personal guarantees. There are options, including fiscal options, to encourage more constructive outcomes.

Skills

New to firm digital innovation will be even more important to enable smaller businesses to adapt to social distancing and to recover. We need to see both a widening of the definition of the scope of 'development' within R&D tax credits and the introduction of digital vouchers for smaller businesses.

Helping small businesses with reskilling, retraining and upskilling their staff quickly will be important for rapid economic growth. The government should support small businesses through the National Skills Fund and allow the workforce to quickly acquire new skills, including digital skills.

As the whole committee will be aware, the UK has a long-running problem with lower than desirable levels of leadership and management skills. In many ways, on a practical level, the current situation is very much a management challenge. We think it would be a mistake and a missed opportunity if improving management skills was not a central part of the Government's response to coronavirus.

Parking

More people are being asked to use their cars rather than public transport, and at the same time we have worrying report from all over the country of parking charges being brought back. This is the last thing small businesses need. A two-hour free parking policy should be implemented or maintained to help boost local commerce as we reopen.

Employment

9 out of ten of those who enter private sector employment after being out of work do so in an SME, including a little over a third of those who start work for themselves.

It is crucial this reality is fully understood in measures to promote jobs.

Jobs

We welcomed the increase in the Employment Allowance to £4,000 promised at the last budget and believe that in the current context this direction of travel should be accelerated. Reducing the costs of employment further, either by raising the allowance, or lowering the level of tax charged, would in our view be very beneficial at the current time, in helping firms reduce wage costs without necessarily reducing headcount.

We have for a long time been champions of employer national insurance holidays for groups that need particular help to return to the labour market. It is a useful signal to employers which will help put those most at risk from long-term unemployment to 'the front of the queue' – and help firms which disproportionately employ from those groups. We appreciate that in the current climate that group may be particularly wide, but at a time when jobs will be especially needed, reducing the amount Government charges employers to employ somebody seems a very sensible course of action.

In terms of those most at risk, including in particular young people entering the labour market for the first time, we think it is also wise to look at models along the lines of the previous Future Jobs Fund. Given the probable state of the economy and the labour market in the wake of this crisis, the proportion of labour costs such a scheme would need to cover to ensure take-up, should not be underestimated. Small businesses as a whole, including but not limited to some of the most clearly affected sectors such as retail, hospitality and leisure, play a hugely disproportionate role in transitions into work, so making sure any such scheme works for small businesses is crucial.

Encouraging self-employment

Helping new firms to start will be essential given the need for new businesses and new jobs. Many existing entrepreneurs will struggle to restart their lives, take loans and start new businesses.

The government should encourage and incentivise the unemployed and those who may have lost a business over the course of the lockdown, through regulation, taxation and access to external finance to become self-employed.

The New Enterprise Allowance and the Start-up Loans Schemes are both excellent schemes which should be expanded.

Apprenticeships

Our research shows that 92% of the apprenticeships that small businesses offer are held by 16-24 year olds. We would be supportive of an apprenticeship guarantee, which we suggest should provide support for those whose apprenticeships have been interrupted, or those unable to progress to a higher-level apprenticeship as previously planned, as well as those seeking to start a new apprenticeship. As part of any intervention on supporting apprentices – reducing the costs of apprentices may have to extend beyond training costs and also help mitigate some of the wage costs incurred. Again, we would emphasise that significant help is probably needed for employers to facilitate this. Restarting apprenticeships will be critical to the rebooting of our economy.

IR35

A flexible labour market will be crucial to recovery. We welcomed the decision to delay the extension of IR 35 rule changes to the private sector by a year. The strong headwinds the UK economy is experiencing, as well of course of the lack of provision for limited company directors in some of the support schemes, suggests there is a case for further extending the delay to the implementation of IR35 rule changes to the private sector.

<u>Encouraging demand and restoring balance sheets</u>

We don't yet know what level of demand will return once lockdown measures are eased. Some of our businesses remain closed, others are now allowed to open but, for example, rely on passing trade from those going to other businesses, from nail bars to cinemas that are currently closed.

We do, however, know that many businesses have suffered severe balance sheet losses as a result of the crisis to date, and that, taken across the economy as a whole, this could herald a slower recovery as firms focus on paying down debt rather than investment. There are numerous options for addressing this, some of which we have addressed below.

VAT

We will know more in the coming days about the initial reactions from consumers once more retail businesses reopen. If demand is weak, it may well be that direct stimulus, such as VAT or other duty cuts, especially to mitigate price rises in socially distant settings, are necessary - certainly in the most affected sectors.

Deferral of VAT due between 20 March 2020 and 30 June 2020 was perhaps a measure introduced when it was hoped the present situation would be resolved before June, so we would suggest there is a case for extension of this measure. There could also be a case for allowing small businesses in extremely hard-hit sectors, for a time limited period, to retain a proportion of their VAT from sales, thus effectively acting as a form of grant.

Debt

Many businesses have taken out loans to cover their costs during this period of restriction, including the welcome Bounce Back Loans and Coronavirus Business Interruption Loan schemes. These schemes have clearly been incredibly important in helping small businesses survive. Looking forward, there is clearly a danger that firms excessively focus on paying down debt, rather than committing investment. As such, we believe that proposals for a "student loans" for business or a Contingent Tax Liability style system to be available for repayment are worth very serious consideration.

There is value in doing so now, rather than at a later date, as firms may then prove more willing to invest.

Infrastructure and stimulus

Overall, when it comes to infrastructure, there has never been a better time to be ambitious. It is about accelerating those infrastructure projects already at an advanced stage that can have the most immediate effect, but also bringing forward as many elements of future infrastructure projects as possible - such as design, paying forward and ensuring robust systems to promote prompt payment within those projects, have a clear positive effect.

Broadband and mobile connectivity

A large number of small businesses have now proved, including to themselves, that remote working and digitalisation work. Broadband and mobile connectivity has long been a major concern for small businesses, and the commitments of the Government to date on this have been very welcome. There can be no better time for this investment, and we would be fully supportive of it, and we remain supportive of the idea of a shared rural network for mobile as well. We have long championed this need in reports on this subject since 2013.

Digital technologies

In addition to infrastructure, investment in digital technologies is key to boosting productivity in smaller businesses. Appetite for investing in digital technology is strong but currently for many smaller businesses the funds are simply not available to do this. Currently there are a plethora of initiatives to support new-to-market innovation such as the R&D tax credit and Innovate UK grant programmes; but very little financial support for new-to-firm innovation.

The Business Basics Scheme is a step in the right direction but the current crisis requires an intervention of a different magnitude. As our research shows, new-to-market digital innovation will be even more important to enable smaller businesses to adapt to social distancing and to recover. That is why we need to see both a widening of the definition of the scope of 'development' within R&D tax credits and the introduction of digital vouchers for smaller businesses seeking to enhance their adoption of digital technologies. On the former, the Government announced in March that it would consult on whether expenditure on data and cloud computing should qualify for R&D tax credits. Changes to the tax system are welcome but it is also essential that immediate support is made available to small businesses that need to adopt digital technologies, here and now.

Roads and electric vehicles

Investment in local roads is especially important for small businesses. We saw this in the March Budget and we must see more as we exit the crisis.

There are also certainly options for further stimulus whether in relation to creating green investment, and take-up of electric vehicles, for instance through a scrappage scheme. Both are clearly desirable in the commercial sector and, so long as incentives were sufficient in a time of economic pressure, measures such as increasing insulation in commercial buildings would likely lead to rapid progress.

Housing

On housing too, we would ask that Government considers making the most of small house builders. Small house builders have been in decline, but their different business model compared to large house builders mean they build faster than large house builders. We have previously suggested Government adopt a specific small house builders strategy in order to get houses built. In the context of a stimulus that works quickly, a focus on incentivising building on small sites, i.e. those building fewer than ten units, will lead to fast results.

Exports

In terms of fiscal measures which will help assist exports, we believe there is a strong case for supporting impacted small firms that trade internationally through the introduction of Export Vouchers, up to the value of up to £3,000. These vouchers would enable firms to access support they need, which ranges from assistance with any extra costs of trading with EU markets to re-orienting to trade with new markets overseas.

Crucially, vouchers – or other support designed to work in a similar way – would put decisions as to what support is most needed with those who know best what support is necessary – small businesses who are seeking to invest in expanding into overseas market. These vouchers, which we would expect to be small amounts, would help small firms on a range of costs from investments in translation services, additional market research, and finding new clients through attending overseas trade fairs - not only helping to grow individual businesses, but the economy as a whole.

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To conclude, much has been done, and needed to be done, to help support small businesses through this crisis. We are not without optimism for the future, the above is intended to spell out some of the problems our businesses are encountering and some of the options available to Government and Parliament to resolve these issues.

We would welcome any opportunity for an FSB representative to give evidence before the Committee.

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