Edinburgh
CHAMBER OF COMMERCE
Inspiring Connections

NON DOMESTIC RATES
A briefing paper
April 2010

Background

The Poor Law introduced in Scotland in 1579 provided for a poor rate to be levied to fund poor relief. The Poor Law (Scotland) Act 1845 modernized the system, and the Lands Valuation (Scotland) Act 1854 established the foundations of the modern system. The Valuation and Rating (Scotland) Act 1956 established a system of five-yearly revaluations, undertaken by an Assessor appointed by the local authority. In 1989, domestic properties were removed from the rating system with the introduction of the Community Charge in Scotland, later to be replaced with Council Tax, to all intents and purposes a reversion to property tax in the older form.

In 1985 Environment Secretary Kenneth Baker sold to the Tory Cabinet the idea of nationalisation of the business rate. This remained as a system whereby properties were revalued at five-yearly intervals (Rateable Value or RV), and the rates payable assessed by an annual 'poundage'. Payable rates are derived from multiplying the RV by the poundage. When enacted this meant that a single country-wide poundage was established for what was now known as 'Non-Domestic Rates' (still known by most people as business rates).[1]

Previously, local authorities had decided what proportion of rateable values to charge; the new system featured a centrally-set multiplier, often referred to as the Uniform Business Rate, by which the basic bill was calculated. The bill could be further modified by various reliefs, including the newly-introduced transitional relief, which was designed to smooth large changes in liability due to revaluations. The multiplier was calculated to ensure that, on average, bills rose by no more than the rate of inflation. In this regard the Scottish system emulated the English and Welsh provision although fundamentally the legal basis remains distinct.

The Local Government Finance Act 1988 amended the existing rating system in Scotland from 1990 at the same time as introducing a new system of business rates in England and Wales from 1990, and the Local Government Finance Act 1992 made further changes. While the latter two acts applied to the whole of the United Kingdom, as the Scottish system is based on Scots law, it remains fundamentally different from the system in England and Wales.

In 1999 as Finance Minister in the new Scottish Government, Jack McConnell cut Scotland's 'poundage rate' adrift from that of England and Wales. Only after a highly

[1] See Andrew Marr 'A History of Modern Britain' 2009 pp467 et passim

focussed campaign, *'Level the Playing Field'* by Edinburgh Chamber of Commerce in 2005 was the parity with the rest of the UK restored over two years, starting in 2006.

Honouring a manifesto commitment when elected in 2007 the new SNP administration set about freeing up smaller properties from Non-Domestic Rates (see The Small Business Bonus Scheme below).

A considerable range of allowances are available for different circumstances, meaning the rating system is now extremely complex for the average Small to Medium sized Enterprise (SME) to navigate.

Every five years all non-domestic (business) properties are assessed, and given new rateable values that reflect more up-to-date rental levels. The latest revaluation came into effect on **April 1, 2010** and all business properties will have their rateable values reassessed.

The last revaluation was based on values at 1 April 2008, put online in December 2009 and informed to rate payers in February/March 2010, becoming payable, as stated, from 1 April 2010. In previous times Scotland had used the mechanism still favoured in England and Wales called 'transitional relief', limiting annual rises to (for example) 12.5% so that more significant increases could be adjusted to over time. With this 2010 revaluation the Scottish Government has abandoned the practice.

Rate Distribution Grant Mechanism (RSG)

The misnomer 'business rates' would lead you to believe that somehow this is a charge levied for a service, that businesses pay rates for their local authority to provide them with something. The reality is that non-domestic rates are in fact a government tax administered by local authorities on behalf of the government.

A proportion of the tax take is returned to each local authority by choice of the government.

The Oxford Dictionary of Economics[2] defines Rate Support Grant as:

A UK system of grants from central government to local authorities. As the name implies, these grants were to supplement the revenues of local authorities, which were not able to raise enough local taxation from rates to pay for their expenditure.

In fact in Scotland the system is such that RSG is funded *from* the Non-Domestic Rate, so that in Edinburgh for example, in excess of £1 billion has been taken from the City's business rate take in the last ten years to fund matters in other parts of the country. Far from RSG being a support mechanism to assist a City that cannot fund itself it is further penalty on businesses for choosing to site themselves in a City which they have helped become more prosperous. We will return to RSG later.

[2] http://www.enotes.com/econ-encyclopedia/rate-support-grant

Some summary definitions: [3]

Non-Domestic Rates

Non-domestic (business) rates are a property based tax. They are (mostly) based on the rateable value of a non-domestic (business) property, multiplied by a poundage factor set nationally by Scottish Ministers, less any relief to which a ratepayer may be eligible. However for some sectors (hoteliers, playhouses and cinemas) the rateable value is based not on bricks and mortar, but on turnover.

What is rateable value?

The Scottish Assessors give all non-domestic property in Scotland a rateable value, which is a legally-defined valuation of a property, broadly based on an analysis of annual rental values (with the exceptions given above).

What evidence do Assessors look at in determining rateable value?

The Assessor will compare a range of property information and study the rental market in depth to ensure that rateable valuations are accurate, consistent and reflect the individual characteristics of each property. Further information on the principles of valuation and practice notes which will help explain how the rateable value for your property(ies) has/have been set can be accessed via the Assessor's website at www.saa.gov.uk

A range of reliefs exist, not all covered exhaustively here:

The Small Business Bonus Scheme

From 1 April 2010 the thresholds of the Scheme will increase. The Scheme will provide relief to businesses with properties in Scotland with a combined rateable of £18,000 or less. In addition, the Scheme has been expanded and, where the cumulative rateable value of a business's properties falls between £18,000 and £25,000, the Scheme will offer 25% relief to individual properties with a rateable value of up to £18,000.

The Scheme provides the following reliefs from 1 April 2010:

Combined rateable value (RV) of all business properties in Scotland:	**2010-11**
Up to £10,000	**100%**
£10,001 to £12,000	**50%**
£12,001 to £18,000	**25%**
Upper limit for cumulative (RV)* £25,000	**25%**

[3] Largely derived from 'A Brief Guide to Non-Domestic Rates' Scottish Government website: http://www.scotland.gov.uk/Topics/Government/local-government/17999/11199/brief-guide

*This will allow a business with 2 or more properties with a cumulative rateable value of under £25,000 to qualify for relief at 25% on individual properties with a RV less than £18,000.

Further reliefs exist for:

- Renewable energy producers
- Rural Rate relief, covering isolated lifeline services to communities, such as garages and shops
- Empty Property Relief
- Charity Relief

What is the poundage?

The poundage rate for Scotland in 2010-11 is 40.7 Pence. This is a fall from 48.1.Pence in 2009-10. Larger businesses in 2010-11 (rateable value in excess of £35,000) will pay a poundage supplement of 0.7 pence, which contributes towards the cost of the Small Business Bonus Scheme.

A fall in poundage sounds like a good thing for businesses. However, to fully understand the effects of the revaluation it is necessary to look at examples of individual properties and see what are the actual amounts payable.

So why isn't everyone happy?

The changes brought about in the late eighties divorced local authorities from the ability to set their own rates, and therefore broke the direct funding connection with the local communities they serve. It denied local authorities the ability to set their own rate. In fact this element is favoured by businesses. The Lyons Enquiry in England (2007) has responded to many local authorities calling for the rate to be increased, and for the power to set the multiplier to be returned to local control; both suggestions have been opposed by business organisations.

However the Rate Support Grant mechanism means that businesses (usually in Cities) are subsidising poorer local authorities (usually in rural areas). This is perceived as an inequality and prejudicial to the success of businesses in City Regions which are proven to be principle drivers of national economies:

Across the country, GVA data now show that the major City-Regions outperform their regions and show higher rates of growth in GVA, Strong City-Regions are a necessary – even though they may not be a sufficient – condition for ensuring optimal economic growth.[4]

Cities play a fundamental role in the global economy. Urban-based economic activities account for up to 55% of gross national product (GNP) in low-income

[4] A Framework for City Regions – Office of the Deputy Prime Minister 2006 http://www.communities.gov.uk/publications/citiesandregions/framework

countries, 73% in middle income countries and 85% in high income countries. Global economy is 'produced' in cities, by international companies. Cities are increasingly linked and interdependent through flows of global activity.[5]

Under the new revaluation there are some winners and some losers. The Scottish government's view is broadly that 'as things are the same overall there is no cause for complaint'. To quote[6]:

Will you be having a Transitional Relief (TR) Scheme?

No. Transitional Relief works by taking money off business who should see savings to subsidise those who see a rise. This is unfair and we want to pass on full savings to businesses.

Has account been taken of the recession?

Rental values in 2010 may be lower than they were in 2008, but that does not mean the Government will be collecting extra revenue.

Your new rates bill will depend on how your rateable value has changed relative to all other rateable values since the last revaluation, not on any changes in the rental market between 2008 and 2010

*Additionally the Finance Secretary **John Swinney** remarked in the Scottish Parliament*[7]*:*

"Central to our consideration has been the question of transitional relief. Evidence shows that a transitional relief scheme would increase the rates bills of most small and medium-sized private sector businesses, which are at the very heart of our economy. Eight out of 10 properties that would have seen bills fall would be worse off. The retail sector alone would lose £25 million. Another consequence of a transitional relief scheme would be that the public sector would benefit at the expense of the private sector. Such outcomes are not desirable, so I have concluded that there will not be a transitional relief scheme to accompany the revaluation.".

As we will see later, these remarks do not accord with the experiences of many business people badly affected by the rate revaluation and lack of transitional relief in particular. Local politicians struggling to maintain and develop infrastructure in the wake of the most devastating recession in living memory may well also differ as to what constitutes fair or unfair.

[5] Greg Clark, Mega Trends & The World's Cities & Regions 2006
http://www.gregclark.net/writer.html
[6] Non-Domestic Rates: 2010 Revaluation
http://www.scotland.gov.uk/Topics/Government/local-government/17999/11199/revaluation
[7] Parliamentary Proceedings

Local Authority loses out

If we take the example of City of Edinburgh, which lost in excess of £100m from its NDR take last year to central funds, we can see that the last ten years take would have paid for:

- The Tram network (£500m +)
- A complete catch up of the road resurfacing backlog (£60m +)
- Festival subsidy (£??m)

With change left over, to create the infrastructure for cross-Forth ferries and hovercraft, renew the lock gates at Leith harbour and prepare a liner terminal. Given that such a large investment as the tram system would normally be amortised over at least twenty years, we can see a considerable opportunity is being lost for Scotland's major wealth creators to increase their ability to benefit the whole nation.

Businesses lose out

We follow with some individual case studies and comments from business executives. In summary, the individual businesses who have lost out in the rates revaluation get no comfort from the fact that others have benefitted, and indeed in some cases, where increased demands exceed their existing profit level are faced with having to make staff redundant or at worst pending failure.

Hotels in particular have been major sufferers.

Far from the claims that 'recession has been taken into account' a revaluation based on rental potential at 1 April 2008 was at the top of the market, and few businesses have not faced challenging times since.

The concept that rates rises are not fixed to absolute rental values but to some relative measure compared to other businesses is easily gainsayed by the individual cases in Stafford Street Edinburgh where the shops have seen payable increases between 19 and 177% (the majority around half as much again) whilst office ratings have mostly fallen. In reality, shops have been renegotiating leases (on which reviews were due) at previous rates as landlords recognise the difficulty of present circumstances in a recession, exacerbated by continuing tram works.

Edinburgh Chamber of Commerce holds similar analyses for a number of streets across the City, which show this is not an isolated example.

Analysis of Stafford Street figures follows.

Stafford Street - All businesses incl Offices Analysis March 2010[8]
(see Appendix 1)

Shops - Average RV increase is 58%, but generally speaking most have an increase of 71%.

The Amount Payable INCREASES by an average of 38.9%, with most shops around 44%. Three premises in particularly have been very hard hit due to their RV % increases being well above the SBBS % increase. These premises either completely lose their current SBBS reduction of have it significantly reduced.

Both House of Hearing and Frontiers (No 10) completely lose their current 25% SBBS reduction, therefore their Rates Payable will INCREASE by 93%!! Studio One is even worse hit as this premise's SBBS reduction goes down from 50% to 25%, resulting in the amount payable INCREASING by 117.8%!!

Offices - *By comparison with shops average RV increases are 26.2%. With the beneficial effect of the SBBS most offices will either continue to pay no Business Rates or a reduction from the current year. Those that will still pay rates have an average INCREASE of 8.9%, but this percentage is inflated by one office's increase of 77.7%.*

The move above SBBS rates or into less generous categories has hit many retail businesses across the City.

One example is typical:

The facts[9] as reprted by Julian Darwell-Stone, Managing Director, Tangram Furnishers Ltd, 33/37 Jeffrey Street:

	2005 - 2010	2010 +	Change
Rateable value	£13,200	£21,800	+65%
Rates payable	2009/10: **£4761** (@48.1p) (£6349 minus 25% small business bonus scheme)	**£8,872** (@40.7p)	**+86%**

The business had a 10 year lease from 1999 with a 25% uplift in rent from 2005 – 2009. We signed a new lease at the end of 2009 with a starting rent at the same level as 2005-2009.

[8] Analysis my Edinburgh Chamber staff, March 2010
[9] Evidence direct from store owner

An increase in rateable value of 65% seems unjustifiable in relation to rental values. The pain is increased significantly because the increase in rateable value takes us beyond the £18,000 limit for the Small Business Bonus Scheme; so despite the fall in poundage the rates payable now increase by a massive 86%!

How can the Scottish Government expect business to keep their heads above water in the current economic climate, let alone have the chance to grow, when such penalising and unfair increases are levied?

Chamber response

Edinburgh Chamber of Commerce wanted to check the facts further and so ran an **online survey** on its website for 14 days from 11-25 March 2010.

Respondents were asked (with replies):

1. What is the CURRENT rateable value of your premises (2009)?

2. What is the NEW rateable value for your premises from April 2010?

3. Was the change in rateable value:

Alternatives	Percent	Value
1 more than you expected	81,5 %	22
2 what you expected	11,1 %	3
3 less than you expected	7,4 %	2
Total		27

4. What impact will the change in rateable value have on your business?

Alternatives	Percent	Value
1 significantly increase overheads to level affecting viability of business	40,7 %	11
2 increase overheads but within acceptable limits	40,7 %	11
3 no impact at all	7,4 %	2
4 will reduce overheads and help cash flow	11,1 %	3
Total 27		

5. As a result of the new rateable value will you:

Alternatives	Percent	Value
1 be looking for smaller premises for your business	29,6 %	8
2 close your business premises and start working from home	3,7 %	1
3 make no change in premises used by your business	66,7 %	18
4 be looking for larger premises for your business	0,0 %	0
Total		27

6. Do you qualify for Rates Relief with the small business bonus scheme?

Alternatives	Percent	Value
1 yes	48,0 %	12
2 no	52,0 %	13
Total		25

7. Will you be lodging an appeal against the new rateable value?

Alternatives	Percent	Value
1 yes	79,2 %	19
2 no	20,8 %	5
Total		24

Questions 8-11 invited comments back, and asked for postcode, type of business and sector.

12. Please select which category of your employee size

Alternatives	Percent	Value
1 1 to 3	0,0 %	0
2 4 to 10	55,6 %	15
3 11 to 50	29,6 %	8
4 51 to 100	7,4 %	2
5 101 to 250	0,0 %	0
6 251 to 500	7,4 %	2
7 500 plus	0,0 %	0
Total		27

As a snapshot of feeling amongst member businesses various interpretations could be applied. What is clear, however is that 82% of respondents felt rate rises were higher than expected and 79% will be appealing. All of these businesses are multiple employers, and so there is also the risk that jobs are under threat.

Appeals process

Rates revaluations are subject to a statutory right of appeal. Appeals must be lodged by 30 September 2010. Meanwhile businesses are expected to pay their rates at the new level, and concerns have been expressed that appeals can take up to eighteen months to be heard.

Hotels

Hoteliers in particular have expressed concern, with both the BHA and EHA expressing worries over the level of increases (see Appendix 2).

Again we have taken one example to illustrate the point.

RATING REVALUATION 2010
Evidence from: Stobo Castle, Stephen Winyard **Managing Director.**

Along with the rest of the hospitality industry, Stobo's rateable value is assessed as a percentage of turnover.

For the record, Stobo's audited turnover for the past 5 years is as follows:

2005	2006	2007 (£'000)	2008	2009
5,834	**6,590**	**6,759**	**6,552**	**6,083**

In calculating Stobo's rateable value for 2010, the Assessor has taken the turnover generated in 2007 (nearest year to the "tone" date of 1 April 2008) of £6.75 million x 8% = £540,000. This reflects an increase of 32.5% on 2005's rateable value of £407,500.

The removal of transitional relief means that Stobo's rates bill will increase by 13.1%, based on the following calculations:

2010/11	**£540,000 x 41.4p**	**=**	**£223,560**
2009/10	**£407,500 x 48.5p**	**=**	**£197,637.50**

However, with the economic downturn, Stobo's turnover in 2009 fell 11.1% from the peak turnover in 2007 used by the Assessor in calculating our rateable value for the next five years.

To summarise, turnover is down by 11.1% from 2007 yet our rates bill in 2010/11 will increase by 13.1% over that paid in 2009/10.

As the only destination spa in Scotland, Stobo's rateable value is assessed by comparing the VOA's assessment of our English counterparts. Stobo is therefore clearly disadvantaged as a result of transitional relief continuing to be applied to our competitors in England when this relief has been abandoned in Scotland.

Do Turkeys Vote for Christmas?

One assumes not. And neither is it surprising that individual businesses do not volunteer to pay higher taxes or ask to have their rates bill increased.

That is not the issue at stake here. Member companies exhibit genuine concerns. From anecdotal feedback, detailed analysis and constant contact with members it is clear to Edinburgh Chamber of Commerce that:

1. The recent rates revaluation is flawed in that valuations made at the top of the market (1 April 2008) do not reflect a depressed market where commercial property prices have fallen as much as forty per cent.

2. Where turnover is the criterion for RV, increases are being assumed on the basis of growing markets which have shrunk since the 'tone' date.

3. Individual business survivals are threatened and their owners cannot expect to be mollified by the fact that 'others have done alright'.

4. The appeals process does not allow for the urgency of the situation.

5. Jobs will inevitably be lost if action is not taken soon.

6. The Capital's economy will suffer as will the whole country's.

7. The longer term tax paying capacity of the City and the country's businesses will suffer.

8. Inward investors will be deterred.

9. The Rate Support Grant mechanism invites review.

10. A debate might be had about who decides what is 'fair' or not?