Business rates review
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

By email: businessrates.review@hmtreasury.gsi.gov.uk

12 June 2015

Dear Sir or Madam,

Re. Business rates review: terms of reference and discussion paper

The British Private Equity and Venture Capital Association ("BVCA") is the industry body for the private equity and venture capital industry in the UK. With a membership of over 500 firms, the BVCA represents the vast majority of all UK based private equity and venture capital firms, as well as their professional advisers. Our members have invested £30 billion in over 3,900 UK-based companies over the last five years. Companies backed by private equity and venture capital in the UK employ around 790,000 people and almost 90% of UK investments in 2013 were directed at small and medium-sized businesses.

At a time when many others have abandoned High Streets across the country, private equity has invested about £1.255bn into retail and high street businesses in 2013 alone. So we are very pleased to see a business rates review launched, and believe that such review should prioritise assisting cities with the re-occupation of vacant sites. As highlighted by the City Growth Commission[1], which the BVCA co-sponsored last year, cities not only drive most of the UK's economic activity, but shape how we live and work. City centres matter to all, with their reach extending to suburbs and surrounding areas as places of leisure and retail, to rural businesses for accessing urban markets, customers and the connectivity cities provide.

We therefore welcome the opportunity to respond to the government's discussion paper on business rates reform. Business taxes are a key consideration in our members' investments, particularly for those in the retail and property markets. Over the last couple of years, we have recorded a common sentiment among our members that the business rates system, which has been in place since the early 1990s, no longer reflects the needs of retail investors. Given how many people are likely to comment on this paper, we have limited our responses to those issues that we believe are of particular relevance to our members.

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[1] Metro Growth: The UK's Economic Opportunity, City Growth Commission, RSA, February 2014

Background to Private Equity and Venture Capital

Private equity and venture capital firms are long-term investors, typically investing in companies for around 5-7 years. This means a commitment to building lasting and sustainable value in the businesses they invest in. Typically, firms will sell their stake in a company by listing on the public markets or selling to a strategic buyer.

Private equity and venture capital firms raise capital to invest from sources such as pension funds, endowments, insurance companies, banks, family offices/high net worth individuals and sovereign wealth funds.

Trends in the use of non-domestic property

Indisputably, the face of the UK high street is changing, with the rise of internet shopping affecting physical retailers, most of whom are now over-spaced and seeking to reduce physical footprints as well as looking for innovative solutions to make use of excess capacity. The business rates system has not kept pace with the change taking place on the UK high street today. In the early 1990s, when current business rates system was introduced, many people and businesses used offices, shops and warehouses in a completely different manner.

The discussion paper suggests that changes to the way we work, shop and socialise has no effect on the overall trend in the use of non-domestic properties. Data provided by the Valuation Office Agency ("VOA") shows that the amount of property used for non-domestic purposes has remained relatively stable between 2000 and 2012. Total non-domestic property floor space has actually increased alongside an increase in total property numbers, according to the VOA. This paints a picture of a tax base as a stable revenue stream for central government.

We believe the assumption that the tax base is changing in nature rather than declining overall to be inaccurate based on more recent experience which data up to 2012 fails to account for. The trend to "de-space" that our members observe in the UK retail and property investments has in fact accelerated in the years between 2012 and 2015. Trends in digitalisation and technology have accelerated, thanks in part to the funding provided by our industry, which makes starting and running a business ever more likely without the need for a physical presence. We would therefore ask the government to **consider more recent data to inform its view on the trend in the use of non-domestic properties**.

Unless the reduction in real space can be replaced by alternative use, our prediction is that the tax base is likely to decline in the coming years. Absent a revision of the calculation of business rates, a greater burden will fall on the remaining retailers and owners of properties. This could potentially accelerate the demise of additional taxable properties and create a vicious cycle.

Additional measures to help small business on the high street

We welcome measures already undertaken by the government to reduce the tax burden for small business. We also recognise the wider reforms to business taxes that the government has achieved,

including the further reduction in the corporation tax from 21% to 20%. In addition to the measures already implemented, we suggest the following:

- **A more generous programme of Capital Allowances** for high street investment, similar to those available in enterprise zones, to help bring forward new projects. These should be available to businesses of all sizes;

- **Require local authorities to set out their strategy** in response to a likely reduction in the amount of retail space and consider how planning will be used to achieve this cohesively. This would be complementary to the business rates retention scheme under which local authorities retain a large proportion of locally collected business rates;

- Additional support for landlords of unoccupied premises by **extending the current empty buildings relief**. Based on our belief that void rates will continue to rise, the current rules forcing landlords to pay 100% of rates on vacant properties (after an initial 3 month period) will become unsustainable and needs to be looked at urgently.

Changes to the business rates system

We recommend **reforming the business rates multiplier**, preferably changing the link of the multiplier from the current Retail Price Index (RPI) to the Consumer Price Index (CPI). Research has shown that linking the multiplier with CPI-inflation would lower the cost of doing business and make future business rate rises more affordable, transparent and predictable for retail investors. Although we understand that the change from RPI-inflation to CPI-inflation could create an initial funding shortfall, we believe the loss in tax revenue would be compensated in the longer term through additional investment in floor-space of non-domestic properties.

Ultimately, however, we believe the government should consider intervening in abolishing upward-only rents, by **linking the business rate multiplier to the rateable value of non-domestic property**. This would have the effect of creating a direct link between business rates and wider economic conditions. Allowing rents to fall as well as rise could potentially allow many retailers to continue to operate on the high street and/or allow assignment of those leases to people who can make it work at that rent level. Using rateable values to calculate business rates is also a relatively basic method of estimating a business' ability to pay, with the advantages of being simple to collect and its relative certainty in quantum.

For the rateable value of non-domestic properties to reflect wider economic conditions, the government needs to make **revaluations to take place at much shorter intervals** than the current 5-7 year period. We currently have the unfair and unsustainable situation that businesses pay rates based on the value of their properties in 2008, taking no account whatsoever of the impact of the financial crisis on property values. Business rates need to be more responsive to economic growth, and basing the multiplier on rateable values could allow businesses to survive and enable underperforming towns and cities to attract investment they need to grow. This move should be

made a priority under the government's regional growth agenda and commitment to create a 'Northern Powerhouse'.

One way to enhance the feasibility of more frequent revaluations would be to **reduce the number of businesses that need to pay business rates**. As it is well-known, small and medium sized enterprises represent two-thirds of the properties but account for just 6% of rental income. Over 300,000 businesses already benefit from the doubling of Small Business Rates Relief but costs to administer these exemptions are spiralling. Taking these businesses out of paying business rates altogether would reduce the administrative cost associated with moving to a system of more frequent revaluations.

Yours sincerely

Tim Hames

Director General, British Private Equity and Venture Capital Association