All Party Parliamentary Group for Hospitality

Business Rates and the Hospitality Sector

A Report from the All Party Parliamentary Group for Hospitality

Wednesday 9th October 2019

All Party Parliamentary Group for Hospitality

A Report by the All-Party Parliamentary Group for Hospitality

- Chair: Steve Double MP
- Vice Chair: Michael Tomlinson MP
- Treasurer: Scott Mann MP
- Secretary: Luke Pollard MP

Secretariat for the All-Party Parliament Group for Hospitality is provided by UKHospitality.

This report was produced following the meeting of the All-Party Parliamentary Group on the 14th of May 2019. We are grateful to Jim McMahon, Shadow Minister for Communities, Jerry Schurder, Head of Business Rates at Gerald Eve and David Sheen, Head of Public Affairs at UKHospitality for their contributions.

Thank you to all businesses and organisations that attended the roundtable session.

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Steve Double MP: Chair of the All Party Parliamentary Group for Hospitality

This year, the APPG will be hosting five roundtables on key topical issues in the industry. These topics will be the 'tourist tax', business rates, home sharing, apprenticeships and migration and the workforce needs of the sector. For each of the roundtables we will be selecting expert speakers from across the political spectrum to put forward their different points of view. We want to maintain the APPG sessions as a robust forum for discussion.

This report will focus on business rates following the roundtable on the 14th of May. The current system of business rates is also under review by the Treasury Committee. Our work is designed to complement the business rates inquiry and provide a summary of the key concerns of the hospitality sector. This report predominantly focuses on the English business rates system unless other geographical areas are referenced.

The hospitality sector is incredibly important to the UK's economy; it is the third largest employer in the UK, with over 3.2million employees. This is 9% of the total jobs in the United Kingdom and the sector is a top 7 employer in every region. With its importance to the economy of the whole of the UK, we must ensure that the needs and the concerns of the sector are properly considered and addressed

I would like to thank all of those that gave evidence to the APPG on this subject. The contributions from all in attendance were welcome. As Jim McMahon suggested in his evidence to the group, it is important that this issue is examined without party affiliation getting in the way. The health of the high street is a cross-party concern. Finally, I would also like to thank UKHospitality, the Secretariat of the APPG for their help in producing this report.

I hope that you enjoy reading the APPG's report and do hope to see you at our sessions in the future.

Steve Double MP
Chair, All Party Parliamentary Group for Hospitality

Kate Nicholls, CEO of UKHospitality, Secretariat of the All Party Parliamentary Group for Hospitality

UKHospitality is delighted to be the Secretariat for the All Party Parliamentary Group for Hospitality. Members of Parliament will all be aware of how important the sector is to the economies of their constituencies.

I would like to thank all the APPG members for their efforts so far this year. The APPG's programme has been devised to address the key challenges that our industry faces. While UKHospitality is vocal in defending our members' interests and is on the record with its position on all of these areas, we welcome the opportunity to support the APPG to be a forum for real debate and to hear the views of a wide range of stakeholders.

The current business rates regime clearly discriminates against the hospitality sector, which overpays by over £2 billion per year, relative to its turnover. It has become clear that business rates is a major contributor to the distress being felt on Britain's high streets and action is needed to ensure these can return to being thriving community hubs. I welcome the cross-party commitment demonstrated at the APPG roundtable for reform of the current rates system, as it was in party manifestos. I would like to thank all of those that spoke at the recent APPG meeting.

I hope that you find the report that UKHospitality has produced for the APPG to be both informative and useful.

Kate Nicholls
CEO, UKHospitality

Executive Summary

- Business rates are taxes paid on non-residential properties, such as shops, offices, factories, and pubs. If you occupy a building, or part of one, that you use for non-domestic purposes, then you'll probably be liable for business rates. There are around 1.8m commercial properties that are eligible to pay business rates in the UK.

- The Hospitality sector is hit disproportionately hard by the current system of business rates. The sector generates £39 billion each year in total tax receipts, which is greater than the UK's annual defence budget. However, despite generating 2.2% of total economic activity in the UK, the hospitality sector pays 13% of total business rates – leading to an equivalent overpayment of £2 billion.

- The 2017 Revaluation hit the sector particularly hard. The increase across the hospitality sector was far greater than the national average for England which was at 9.6%. Hospitality businesses of different types saw significant raises. Hotels of 3 stars or above saw their rates increase by over 50%, pubs rates went up by 14.7% and the rates for tourist attractions rose by 38.2%.

- The crux of this is that hospitality is not an 'efficient' user of property. However, this does not recognise the importance that space plays for hospitality businesses, offering people a relaxing environment in which to enjoy themselves. Nor the need for space for reasons of food hygiene and customer safety.

- In the October 2018 budget, the Government announced a business rates discount scheme for small-sized high street properties in England that have a rateable value below £51,000. Under the plan, 'small businesses' will receive a one-third discount on their rates bills from 1 April for the next two years, which then-chancellor Philip Hammond said will help "up to 90 per cent of all independent shops, pubs, restaurants and cafes. While welcome the reliefs do not support the vast majority of high-street businesses that are either multiply operated or have a higher rateable value due to their location. Further to this, EU state aid rules prohibit effective reliefs going to businesses with a large number of sites across the country.

- The tax burden that is placed on the hospitality sector is a key cause of the so called 'crisis of the high street.' Squeezed incomes, online shopping, changing consumer trends and rising overhead costs are having a significant impact on the hospitality sector. As of March 2019, Britain had 117,909 pubs, bars, restaurants and other licensed premises—2.3% fewer than a year before, and 4.3% fewer than five years ago.

- The fairness of the system is further undermined by the poorly functioning appeals system. The valuation of a property can be a critical element in how successful a business is. While efforts have been made to make simple changes to the system easier through the ‘check’ process it is clear this is not working effectively enough. More complex ‘challenges’ are often held up in the system for years and can quite literally lead to business failure.

- A potential improvement to the current system is to have more frequent evaluations. This is the approach used in the Netherlands. The rationale is that the taxpayer will have greater trust in the process if they see that their rate is in line with those of other properties. More frequent revaluations could, however, lead to additional uncertainty.

- Reliefs need to be more targeted on sectors that currently overpay – and Government should reconsider the application of State Aid rules. If State Aid rules are applied to reliefs, then the Government should consider differential multipliers for certain sectors.

- A Royal Commission, with representation from all sectors of the economy and other stakeholders, could be a potential option to develop a new system that is more attuned to business in the modern era.

1. Background

What are Business Rates?

Business rates are taxes paid on non-residential properties, such as shops, offices, factories, and pubs. If you occupy a building, or part of one, that you use for non-domestic purposes, then you'll probably be liable for business rates. There are around 1.8m commercial properties that are eligible to pay business rates in the UK. The current rating system is designed to create a fair measure, whereby properties are all valued on a common measures of market rental value at a fixed point.

As of March 2018, business rates raised £23.9 billion in England annually and act as an important source of funding for local services.[1] In the UK, there has been a long precedent of equivalents to business rates. While they were introduced in their current form in the 1990s their lineage can be traced back to the Poor Law of 1572, and later the Poor Law of 1601.[2] Each year, councils will send out business rates bills in February or March. The amount owed on a property will depend on the "rateable value" (RV) of the property, the appropriate tax rate and any reliefs to which they are eligible. The RV is a measure of the annual market rental value of the property and is determined by the Valuation Office Agency (VOA), generally using other rents in the local area to work out an average.

For some businesses with a licence to sell alcohol the system is slightly different. For pubs in England and Wales, the VOA works out the rateable value based on the annual level of trade (excluding VAT) that the business is expected to achieve if it is operated in what is deemed to be a reasonable and efficient way. This is called 'fair maintainable turnover' (FMT) and is based on criteria like the type of venue, the area that it is in and the services that it offers (for example food, gaming or sports screenings.) The VOA looks at 'clean' rents and turnovers to derive a methodology to work out the FMT figure for the wider trade, then applies a percentage to work out the rateable value.[3]

Hotels are calculated on a turnover based method linked to the profitability of the business. The VOA takes a very collaborative approach in developing the valuation methodology, employing experts to support the process. There is usually a substantial lead-in time to the methodology process (for 2021 revaluation it is expected the guide will have been completed by September 2019). This allows business an opportunity to estimate their likely valuation in advance.

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[1]Business Rates Delivering More Frequent Revaluations". Assets.Publishing.Service.Gov.Uk, 2019, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/689236/Business_rates_revaluations.pdf. Accessed 4 July 2019.

[2] Farma Understanding Business Rates". Farma.Org.Uk, 2015, http://www.farma.org.uk/media/originals/0/505/business-rates.pdf. Accessed 8 July 2019.

[3] Business Rates Delivering More Frequent Revaluations". Assets.Publishing.Service.Gov.Uk, 2019, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/689236/Business_rates_revaluations.pdf. Accessed 4 July 2019

For hotels in England there are three rating categories that are categorised by their star rating, as well as their budget. The overall rating of a hotel is a proportion of turnover based on size, yield and the class of hotel.

Self-Catering properties and holiday let accommodation also have slightly different valuation rules. If your property is in England and available to let for short periods that total 140 days or more per year, it will be rated as a self-catering property and valued for business rates. If your property is in Wales, it will be rated as a self-catering property and valued for business rates if it's both available to let for short periods that total 140 days or more per year or actually let for 70 days.[4]

Business rates are popular with a number of economists who believe that they are the best way to tax land in the UK. As Jerry Schurder, Head of Business Rates at Gerald Eve told the APPG, the economic theory behind this is sound. 'Business rates are difficult to avoid, given they are a tax on land can't be avoided by basing a business offshore.'[5] The economic theory on which rates are based predicts that in the long run, higher business rates will be reflected in lower rents. This should, in theory, see a shift in the burden of tax from the property's occupiers to its owners. However, this theory is questioned in practice by hospitality operators, particularly those on longer leases.

Another supposed benefit of business rates is that they are politically more expedient than the introduction of a pure land tax, which would create both significant winners and losers.

The general principles of an effective tax are outlined by John Webber, the Head of Rating at Colliers:[6]

- Relative to the ability to pay
- It should be easily understood
- It should be administratively efficient
- It should be difficult to evade and avoid
- It should be impartial
- It should benefit those who pay

There are several debates relating to some of the above criteria and business rates on the hospitality sector that this report will reflect.

Business rates values have historically been reviewed every five years, with the most recent revaluation being introduced in April 2017. The last revaluation was following a seven-year gap and Government has announced three-yearly reviews in the future, though the current period will last for four years. The reason for revaluations is to ensure that the rates that are paid remain broadly in line with the annual rental value of a property and reflect sectoral and regional changes over time. The revaluation in April 2017 caused much consternation in

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[4]Business Rates Delivering More Frequent Revaluations". Assets.Publishing.Service.Gov.Uk, 2019, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/689236/Business_rates_revaluations.pdf. Accessed 4 July 2019.
[5] Jerry Schurder to the All Party Parliamentary Group for Hospitality 14th of May 2019 accessed 4th July 2019
[6] John Webber (2017) Property Journal London, 'Going Dutch' October 2017 accessed 5th July 2019

the hospitality industry. Many businesses within the sector were hit with a huge rise in the rates that they paid. To cushion the blow for businesses across the economy, the Government introduced a transitional relief system (paid for by those receiving a decrease in their rateable value) in order to limit the increase that any one business would have to bear in any one year.

Following the revaluation, further reliefs have been announced, the most recent of which was introduced in last year's Autumn Budget. The need for reliefs reflect the failure of the system to fairly tax different sectors and sizes of business. In the October 2018 budget, the Government announced a business rates discount scheme for small-sized retail-focused properties in England that have a rateable value below £51,000. Under the plan, small firms will receive a one-third discount on their rates bills from 1 April for the next two years, which chancellor Philip Hammond said will help up to 90 per cent of all independent shops, pubs, restaurants and cafes.[7]

Despite attempts to relieve the burden on businesses, the current system of rates remains unpopular across an enormous range of stakeholders. There is an argument that the current ratings system has failed to keep up with business trends. In recent decades there has clearly been a shift in the way of doing business with property size no longer being emblematic of business performance. As stated by Jim McMahon at the roundtable, 'property is no longer as important for the conduct of business, yet the UK's tax system has not evolved.[8]'

This March, the Treasury Select Committee launched an inquiry into Business rates. At the launch of the inquiry, Chair Nicky Morgan said 'high street businesses are struggling to remain competitive. It has been estimated that 10,000 shops will close this year. Unless action is taken, closures could continue, and job losses may soar.[9]'

This report strives to build on the current analysis that is being carried out by the Treasury Committee and examine the current business rates system, specifically its impact on the hospitality sector. The report will then look to make recommendations to the Government on business rates reform.

[7] "£500M Cut To Business Rates For Pubs And Shops". The Independent, 2019, https://www.independent.co.uk/news/business/news/business-rates-cut-uk-high-street-shops-pubs-tax-a8848831.html. Accessed 6 July 2019.

[8] Jim McMahon to the All Party Parliamentary Group for Hospitality 14th May 2019

[9] https://www.parliament.uk/business/committees/committees-a-z/commons-select/treasury-committee/news-parliament-2017/inquiry-launch-into-the-impact-of-business-rates-on-business-17-19/

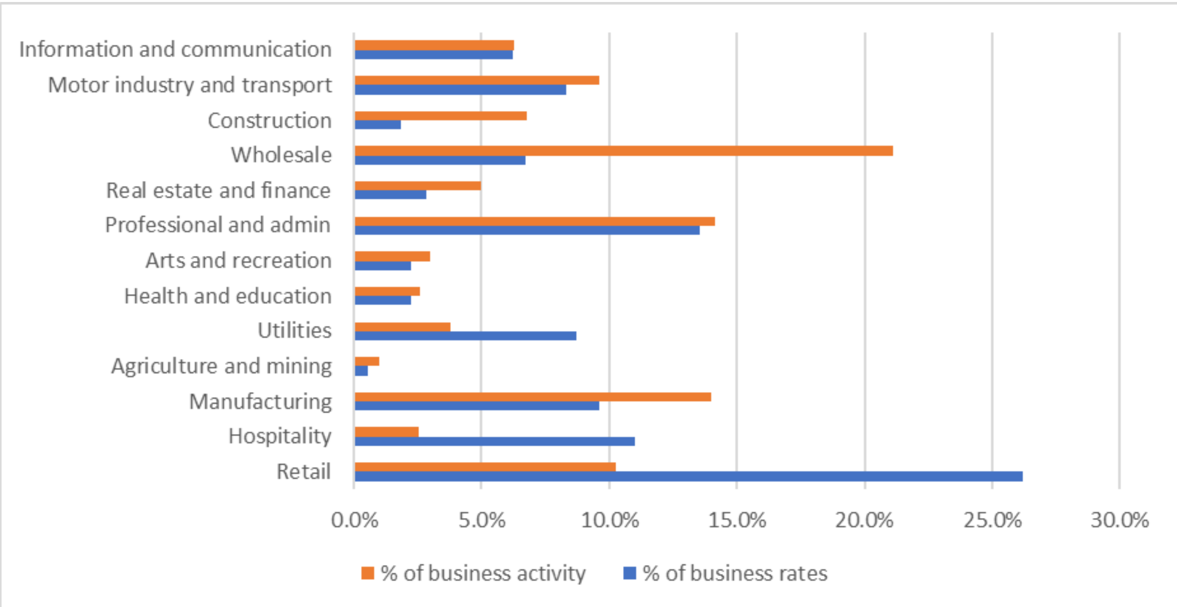
The Hospitality Sector and Business Rates

This section of the report will examine the impact that the current system of business rates has on the hospitality sector, the key concerns of the industry and the pressure that business rates are putting on the high street. The hospitality sector accounts for £39 billion each year in total tax receipts, which is greater than the UK's annual defence budget. This is a significant sum for an industry that accounts for 2.2% of all economic activity in the UK.[10]

When it comes to business rates, there is a significant disparity in the amount that the sector pays in comparison to the money that it generates, as is highlighted below in Figure 1.1. When looking at the below table, it is clear that the only sector that overpays on business rates in a comparable way to the hospitality sector is the retail sector. If businesses within the hospitality sector were to be charged relative to the amount of business activity, the hospitality sector would only pay £713million, 4 times less than it currently pays.[11]

As mentioned in the introduction, business rates across the UK are based on the rental value of a property, a system that has been in place for hundreds of years and reflective of how business used to be done. There is a growing consensus that in recent decades the way of doing business has shifted to more online sales and services. Property, for so long an indicator of business size and success, is no longer as important. However, the UK's tax system has yet to evolve with the changes.

Figure 1.1 Percentage of Business Activity in Comparison to Percentage of Business Rates paid in UK



The crux of this is that hospitality is not an 'efficient' user of property. Many hospitality venues will be large spaces or will lie inactive throughout parts of the day or year. Offering a

[10] "Written Evidence - UKHospitality". Data.Parliament.Uk, 2019, http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/treasury-committee/impact-of-business-rates-on-business/written/98897.html.
[11] IBID

relaxing environment is a key for the hospitality sector. In hospitality businesses, areas will frequently lie idle throughout certain periods of the day or the year. Operators have made giant strides in addressing this in recent years, with a greater daytime offering but there is only so much that can be done. Therefore, basing a tax solely on property is always going to disadvantage hospitality. This position is reflected in the submissions that a number of representative bodies in the sector made to the Treasury Committee Inquiry. UKHospitality, the British Beer and Pub Association and CAMRA each stated within their evidence that for the above reasons the current system is unsuitable for the sector and neds instant reform.

Additional space is also needed for regulatory and safety reasons. Food preparation areas, cellars for drink storage and capacity limits to ensure a safe environment for customers also mean that hospitality businesses tend not to be property-efficient.

Similar concerns were articulated by the British Property Federation in their submission to the Treasury Committee where they stated that the business rates system is placing 'unsustainably high burdens on business, which are totally out of kilter with the true value of the space businesses are occupying. [This] emphasise[s] the urgent need for business rates reform.[12]''

A key challenge that the hospitality sector and the high street more generally has faced is the increasing popularity of online shopping. Jim McMahon, Labour's Shadow Housing, Communities and Local Government Minister suggested to the APPG that the market place has changed. In his oral evidence McMahon said, 'The new market place is the .com and efforts need to be made to effectively legislate this while providing reliefs to high street businesses.[13]'' While hospitality is less affected than retail by online sales (currently) a deteriorating retail performance has a knock-on impact in footfall in town and city centres that hits hospitality hard.

The revaluation of business rates in 2017 occurred after a period of seven years (two years later than it should have). This revaluation hit the hospitality sector particularly hard, increasing rates bills well above the national average and shifting the burden of business rates further onto businesses in the sector. Many businesses saw huge increases, particularly given the fact that the last revaluation occurred just after the height of the financial crisis. Figure 1.2 highlights the percentage increases that the hospitality sector saw in the 2017 revaluation.

[12] "Written Evidence - British Property Federation". Data.Parliament.Uk, 2019, http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/treasury-committee/impact-of-business-rates-on-business/written/103819.html. Accessed 4 July 2019.
[13] Jim McMahon to the All Party Parliamentary Group for Hospitality 14th May 2019

Figure 1.2 2017 Revaluation and the Hospitality Sector

Special category description	Percentage Change
England total	9.6
Night Clubs and Discotheques	10.1
Public Houses/Pub Restaurants (National Scheme)	14.7
Restaurants	23.7
Tourist Attractions	38.2
Cafes	14.6
Hotels (3 Star and Under)	50.2
Hotels (4 Star and Above) and Chain Op. 3 Star (National Scheme)	19.7

As will be discussed in greater detail in the relief's subsection, efforts have been made to address the cost pressures faced by businesses after the 2017 revaluation. However, these have generally been viewed by the sector as being skewed towards very small businesses and were described by UKHospitality in their submission to the Treasury Committee as 'sticking plasters to deal with a broken system.[14]'

Appeals

The cyclical nature of the rental market, and infrequent cycle of revaluations, can lead to significant changes to rateable values at revaluation, creating uncertainty for ratepayers. It can also mean that the bills which businesses pay do not reflect current economic conditions. Businesses frequently are charged based on incorrect valuations and are required to appeal them. As the APPG heard from a number of businesses present on the day of the inquiry session, the appeals system is widely considered to be slow, cumbersome and ill-suited to the reality of the business world.

The 'Check, Challenge, Appeal' process introduced in 2017 is signalled out for criticism by many within the sector. Recent figures from the Valuation Office show a 97% drop in the number of businesses challenging their rates bills in the last two years in England, compared to the two years following the previous revaluation.[15]

The VOA, the body that is responsible for dealing with challenges to valuations, has been singled out for criticism from people within the industry and is widely considered to be under-resourced to effectively carry out its role at valuation and through appeals. In their submission to the Treasury Select Committee the British Beer and Pub Association called for a faster, more transparent and responsive system, like that of The Netherlands.

[14] "Written Evidence - UKHospitality". Data.Parliament.Uk, 2019, http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/treasury-committee/impact-of-business-rates-on-business/written/98897.html.

[15] Business Matters "Business Rates Appeals Plummet, As Firms Deterred To Challenge Bills". Business Matters, 2019, https://www.bmmagazine.co.uk/news/business-rates-appeals-plummet-as-firms-deterred-to-challenge-bills/. Accessed 4 July 2019.

The criticisms that were lodged at the VOA were echoed in the APPG's evidence session on rates. The VOA received criticism for not having enough manpower to turn around submissions quickly enough. There is also the suggestion that the VOA is 'parking' some of the earlier submissions and concentrating on new ones coming in, so it appears to be more successful than it actually is. The insinuation is that the huge drop in challenges is due to the poor functioning of the system. This means that significant amounts of businesses within the sector are paying the wrong rates.

There were also issues with the roll out of the IT system for Check, Challenge, Appeal. This was not tested properly prior to going live on 1 April, meaning that the system was unworkable for the vast majority of operators, and problems continue to this day.

The Chief Executive of the VOA, Melissa Tatton, wrote to the Chair of the Treasury Select Committee Nicky Morgan and also appeared for questions in front of the committee during the inquiry into business rates.[16] Tatton has said that recruitment remains a priority for the organisation and that staffing levels are monitored against the work plan. As part of the letter to Nicky Morgan, Tatton outlined the number of active challenges that the VOA are currently dealing with.[17] Challenges by their nature take longer to resolve than checks and as such the progress will be slower. The remaining number of challenges are summarised in figure 1.3. [18]

Figure 1.3 VOA Outstanding Challenges

Year and Quarter	Outstanding Challenges
2017 (All Quarters)	4%
Q1 of 2018-19	9%
Q2 2018-19	15%
Q3 2018-19	22%
Q4 201819	50%

There is frustration with the VOA, but this is probably largely due to the resources available to the organisation to deal with the system, and a hastily introduced new system. With more resource it is possible that challenges can be addressed faster.

As will be discussed in greater depth in the alternatives section, in the Netherlands, there has been a push towards a computerised system of valuations. This according to John Webber, business rates lead from Colliers, allows them to value 8 million properties annually at a reduced cost.[19] Webber suggests that replicating this in the UK would not only

[16] Tatton, Melissa. Parliament.Uk, 2019, https://www.parliament.uk/documents/commons-committees/treasury/Correspondence/2017-19/Chief-Executive-of-the-Valuation-Office-Agency-to-Chair-relating-to-Business-Rates.pdf.
[17] IBID
[18] IBID
[19] Better Rates For Better Business". Bpf.Org.Uk, 2019, https://www.bpf.org.uk/sites/default/files/resources/Better-Rates-for-Better-Business-full-report.pdf. Accessed 6 July 2019.

made the administering of rates more effective but could also reduce the administration costs by rates by £50m a year.[20]

Impact of Cost Pressures on the Hospitality Sector

The Hospitality sector pays a significant amount of tax to the Treasury, amounting to £39 billion each year. Businesses face significant overhead costs from employment, including national insurance and increasing minimum wage levels, alongside rental costs and business rates. The impact that these costs are having on the high street is well-documented. These costs, exacerbated by squeezed incomes, increasing online shopping and changing consumer trends are having a significant impact on both the high street and the wider hospitality sector.

The impact across the hospitality sector is clear. For example, as of March 2019, Britain had 117,909 pubs, bars, restaurants and other licensed premises—2.3% fewer than a year ago, and 4.3% fewer than five years ago.[21]

Parliamentary focus on the threat to the British High Street has been led by the inquiry by the Housing, Communities and Local Government Committee. This inquiry heard evidence from a number of sector businesses over several months. The closure of high-profile chains like Jamie's Italian has also received national media attention. Business Rates along with employment costs are most frequently cited by businesses within the hospitality sector as the most significant burden that they face.

The importance of hospitality businesses to communities was also raised at the APPG for Jim McMahon MP, with a contradiction between rural and urban communities. McMahon said, 'Rate relief is in place for last pub in village but not in place for the last pub on the council estate.[22]' A review of business rates needs to review pubs and the positive role that they play. It is also important to do this for restaurants and wider hospitality. Hospitality venues form vital social hubs within communities across the country. Current cost pressures however are beginning to make their existence in some communities barely viable.

2021 Revaluation

As was announced in the April 2018 budget, the next revaluation of business rates has been brought forward to 2021. The methodology for this revaluation for pubs and hotels is already being negotiated, to set a framework for future valuations.

Business Rates Reliefs

Some businesses are eligible for reliefs from their local councils on the rates that they pay. Reliefs are devolved in Northern Ireland, Scotland and Wales. There are a number of different types of relief that businesses may qualify for, including small business rates relief, rural rate relief, hardship relief and transitional reliefs. The APPG was told that there is a

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[20] IBID
[21] "CGA Reports On The Out-Of-Home Food And Drink Market". CGA, 2019, https://www.cga.co.uk/report-tag/pubsbarsrestaurants. Accessed 13 July 2019.
[22] Jim McMahon to the All Party Parliamentary Group for Hospitality 14th May 2019

lack of consistency between different local authorities in terms of how these funds are allocated. This section will examine the different types of reliefs that are available while outlining certain issues with the reliefs that have been raised to the APPG.

Small Business Rates Reliefs

Some smaller hospitality businesses will be eligible for small business rates reliefs. These reliefs are applied if the rateable value of a property is less than £15,000 and if the business only uses one property. Full relief is available on properties with a rateable value of £12,000 or less. For those between £12,001 and £15,000, relief ratchets down gradually from 100 per cent to zero per cent.[23]

Rural Rates Reliefs

You could get rural rate relief if your business is in a rural area with a population below 3,000. You will not pay business rates if your business is in an eligible area and either the only village shop or post office, with a rateable value of up to £8,500, the only public house or petrol station, with a rateable value of up to £12,500.[24]

Retail Relief

Business in England can qualify for retail discount if the business is a shop, café**,** bar or pub and has a rateable value of less than £51,000. Eligibility for this relief can take up to a third of the business rate that a company pays. Retail discount can also be given on top of any other business rates relief that a business is eligible for. The rate will be available for the 2019 to 2020 and 2020 to 2021 tax years.[25]

Reliefs and the Hospitality Sector

While the reliefs are welcome for smaller businesses within the sector, a number of concerns were articulated to the APPG from businesses present at the roundtable. One of the concerns that was noted most frequently at the APPG was that reliefs tend to be based on the rateable value of a property and are designed to exclude businesses with multiple properties. The rationale behind excluding multiple sites is that they are not ‘small businesses’, however they are frequently run on the same basis as smaller businesses with similar margins. An operator with 30 pubs will be looking at which ones are profitable (in their current estate or any future acquisitions) and business rates will often be the determining factor between whether a property is viable or not. There exists a belief within the sector that the current reliefs system, much like the rating system as a whole, is largely arbitrary.

This is highlighted by looking at the most recent reliefs which were introduced from April, which offered a one-third discount to a specified list of business types. Obscurely this does

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[23] Business Rates Delivering More Frequent Revaluations". Assets.Publishing.Service.Gov.Uk, 2019, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/689236/Business_rates_revaluations.pdf. Accessed 4 July 2019
[24] IBID
[25] IBID

permit reliefs for some parts of hospitality but not for others. Businesses classified as hotels, for example, will not be eligible for the relief, but pubs and restaurants will be. Often a hotel can be a hybrid and will have a restaurant or pub as part of its consumer offering. Therefore, it will come down to a judgement call as to whether businesses receive or miss out on a relief. The effect of excluding accommodation businesses from the relief costs hotel sector businesses around £73million.[26]

The application of reliefs goes back to a fundamental flaw in the rates system, the ability to pay and the lack of reference to sales or profit. Business rates are paid regardless of whether the business is making any profit. As Jim McMahon articulated, business rates are a 'tax to exist' as a business.[27] It is a sunk cost that has to be recouped through the year, and in many cases cannot be.

There is an argument that business rates balance out rents, when one rises the other falls. This has not been the experience of hospitality businesses who have seen rental rises go hand in hand with business rates increases. This is particularly the case where investment takes place in run-down areas with consequential rental and rates hikes – largely undermining the business case for regeneration.

Some large retailers with multiple properties are eligible for relief that exceeds state aid rules. This is widely disagreed with by the hospitality sector with a strong desire that the Government should reconsider whether such rules should apply.[28] The consequence has been that many hospitality businesses have not been able to access the relief to which they were entitled. This has been the case with pub relief, local authority discretionary relief and high street support. In some cases, businesses have had to repay their relief where local authorities have allocated it and it has exceeded the state aid threshold.

There is increasing interest in the idea of introducing a rates holiday, exempting businesses from paying new rents for a set period of time following investment in their property. This would allow businesses to expand their sites and provide a better offer to their customers without the threat of an immediate rates rise.

[26] "Written Evidence - UKHospitality". Data.Parliament.Uk, 2019, http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/treasury-committee/impact-of-business-rates-on-business/written/98897.html.
[27] Jim McMahon to the All Party Parliamentary Group for Hospitality 14th May 2019
[28] http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/treasury-committee/impact-of-business-rates-on-business/written/103108.html

Possible Alternatives and Solutions

With clear enthusiasm for reform of business rates from within the sector, this section of the report will examine potential reforms to the rating system. The APPG heard from organisations who all suggested that the current system discriminated against the sector and needed reform.

Digital Goods and Services Tax – Potential Remedies?

A digital services tax to allow for a cut in business rates is often cited as the perfect means to allow the Government to maintain the revenue that it receives but also to shift the tax burden to the online sector.

The Government has announced its intention to deliver a 'Digital Services Tax' from April 2020, that will aim to ensure that online businesses contribute to the Exchequer. However, this will deliver only a fraction of the amount collected from property through business rates – at around 1.3%.

As Jim McMahon said at the All-Party Group roundtable: 'it is not the job of Government to save the High Street, but it is the job of Government to ensure that things for the high street are not harder.[29]'

There has however been no indication that a digital service tax of any amount would be used to reduce the burden that the sector faces. There remain concerns from within the sector that a new online services tax could be used as another revenue stream as opposed to reforming fundamentally the business rates system.

Further to this, the Chartered Institute of Taxation (CIOT) submission to the Treasury Select Committee looked to temper expectations that planned UK Digital Services Tax is a cure for ailing high streets. The CIOT have cautioned that 'the DST is about the UK getting what is sees as the right share of international tax on profits based on value added by users – and not a tax on online sales more generally.' John Cullinane, tax policy advisor of the Chartered Institute of Taxation expressed cynicism about the prospect of the Digital Services Tax as a way to help the high street 'hold its own better in the digital economy.[30]'

Despite this, with the current system of business rates hitting the high street hard, there will remain enthusiasm from within the sector to level the playing field with online businesses – and to reduce the overall tax burden it faces. A digital services tax that is used to provide effective reliefs will remain popular.

Digital Goods Tax

The Digital Service tax has been viewed as a potential source of revenue for the Government that would allow it to provide effective reliefs for the sector. However, as mentioned above this tax in its current format would fail to raise enough revenue to allow for large cuts in

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[29] Jim McMahon to the All Party Parliamentary Group for Hospitality 14th May 2019

[30] Press Release: Digital Services Tax Not A Panacea For The High Street | Chartered Institute Of Taxation". Tax.Org.Uk, 2019, https://www.tax.org.uk/media-centre/press-releases/press-release-digital-services-tax-not-panacea-high-street. Accessed 13 July 2019.

business rates bills. Broadening the scope of the Digital Services Tax, as the next subsection outlines, would help to generate greater revenue and crucially, could be used to reduce the overall business rates burden on sectors like hospitality that are currently overpaying.

Tesco, who pay around £700 million in business rates, suggested this idea in the evidence that they sent to the Treasury Select Committee. The supermarket suggests the government could raise £1.5bn via an online sales levy of 2% on physical goods, as defined by existing VAT regulations. Tesco says the government could use that revenue to fund a 20% cut in business rates for all bricks-and-mortar retailers. It says small businesses could be exempted from the online sales levy.[31]

Such an approach has been positively received by a number of businesses.

More Frequent Revaluations

One of the most commonly discussed options is to have more frequent revaluations of the rates that businesses pay. This April, Chancellor Phillip Hammond promised that the frequency of business rates valuations would change from five to three years.[32]

The decision to have more frequent revaluations was greeted warmly from within the industry. As Jerry Schurder said to the APPG, "Businesses have long been lobbying for more frequent revaluations so that rates bills are more closely related to property values and trading conditions.[33]"

More frequent business rates valuations would however potentially require greater funding and resources to be given to the VOA. The VOA is singled out for criticism for being under resourced and thus unable to cope with its current workload. If valuations were to become more frequent, ensuring that the VOA had the capacity to deal with its new responsibilities would be essential.

The Dutch Model

The system of business rates in the Netherlands is frequently cited as a potential and superior option to the current British rating system. Within the Dutch system, ratepayers and taxpayers are seen as part of the process of gathering and supplying information. They have carried out a study that suggests that the accuracy of the valuations is far greater as a result.[34]

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[31] Butler, Sarah. "Tesco Seeks Online Sales Tax To Fund Business Rate Cuts". The Guardian, 2019, https://www.theguardian.com/business/2019/apr/30/tesco-seeks-online-sales-tax-to-fund-business-rate-cuts. Accessed 14 Aug 2019.

[32] https://www.propertyweek.com/legal-and-professional/move-to-more-frequent-business-rates-revaluations-gets-a-mixed-reception/5095881.article

[33] Jerry Schurder to the All Party Parliamentary Group for Hospitality 14th May 2019

[34] Better Rates For Better Business". Bpf.Org.Uk, 2019, https://www.bpf.org.uk/sites/default/files/resources/Better-Rates-for-Better-Business-full-report.pdf. Accessed 6 July 2019

In the Netherlands, there is an annual revaluation of 8.5m domestic and non-domestic properties. As mentioned above, there are a number of benefits to having more frequent revaluations.

The manner of the appeals process in the Dutch model is also singled out for praise in comparison to its British counterpart. There is the suggestion that the VOA can be more antagonistic and looks to defend its figures. The Dutch process by contrast is far more open, with any interested party having access to the data behind the appraisals. This means that there is greater trust in the values of the appraisals themselves. In the UK, the current system was criticised at the APPG roundtable for appearing arbitrary.

Researchers believe that trust in the assessments can be cultivated by emphasising the accuracy of data used by the municipalities.[35] Empowering the taxpayer to register and update the data and explaining how the municipalities handle and process this information to arrive at an accurate assessed value, keeps ratepayers happier.

Turnover tax

Another potential alternative to business rates is the introduction of a tax on turnover to replace it. While there would be some opposition with what would be viewed as a tax on success, such is the opposition to the current system that this could be viewed as the preferable choice. As opposed to what the sector currently sees as a fairly arbitrary way of charging companies, a tax on turnover could be more palatable as more money would be charged only when the business was succeeding. This would be similar to a Digital Goods Tax.

Royal Commission on Business Rates

Royal commissions are ad hoc advisory committees established by the government - though formally appointed by the Crown, hence the "royal" - to investigate any subject the administration of the day sees fit to refer to it.[36] In practice, royal commissions have sometimes been established to deal with issues that a government feels may be too controversial for it to be seen tackling itself.

They are often used for non-party political issues, or for issues that a government is endeavouring to address in a non-party political way. As was highlighted by the APPG roundtable, there is clearly cross-party support for addressing the current impact of business rates, and a Royal Commission would be a useful exercise to do this. Introducing a Royal Commission for business rates should look at the holistic burden of tax that various industries face. This would be a useful way of working out potential alternatives.

[35] Better Rates For Better Business". Bpf.Org.Uk, 2019, https://www.bpf.org.uk/sites/default/files/resources/Better-Rates-for-Better-Business-full-report.pdf. Accessed 6 July 2019

[36] BBC News | UK Politics | What Is A Royal Commission?". News.Bbc.Co.Uk, 2019, http://news.bbc.co.uk/1/hi/uk_politics/258929.stm.

Conclusion

The hospitality sector accounts for £39 billion each year in total tax receipts, which is greater than the UK's annual defence budget. This overall tax burden that the sector faces is putting significant pressure on businesses, as has been seen with the closure of well-known brands over the past year.

When it comes to business rates, this is where the hospitality sector overpays most significantly. The Hospitality sector accounts for only 2.2 of all business activity in the UK yet contributes 13% of business rates. If businesses within the sector were to be charged relative to the amount of business activity, the hospitality sector would only pay £713million, 4 times less than it currently pays.

The cyclical nature of the rental market, and infrequent cycle of revaluations, can lead to significant changes to rateable values at revaluation, creating uncertainty for ratepayers. It can also mean that the bills which businesses pay do not reflect current economic conditions. There is also a strong argument that was put before the All-Party Parliamentary Group that the way of doing business has shifted to more online sales and services. Property, for so long an indicator of business size and success is no longer as important. However, the UK's tax system has yet to evolve with the changes**.**

The Government has looked to provide reliefs to businesses that are suffering in the wake of the 2017 revaluation, however this process is seen to be flawed. The reliefs are designed to assist smaller businesses but often limited support to owners of multiple sites or many businesses in town centres. For operators with multiple pubs, it is important to look at which are profitable and business rates can often be the determining factor between whether a property is viable or not. Within the sector, there exists a perception that the current reliefs system, much like the rating system as a whole, is largely arbitrary.

There are also a number of issues with the current system of appeals. The Check, Challenge, Appeal process introduced in 2017 is criticised by many within the sector. Recent figures from the Valuation Office show a 97% drop in the number of businesses challenging their rates bills in the last two years in England, compared to the two years following the previous revaluation. This means that many businesses are not paying the correct amount with very little immediate prospect of remedy.

The value that hospitality businesses have for the communities in which they are based in unquestionable. Rate relief is currently in place for the last pub in the village, but not got the last pub on the council estate. A review of business rates needs to review pubs and other hospitality businesses and the positive role that they play.

The VOA is also widely considered to be underfunded and under-resourced. The time that is taken to address appeals has literally put companies out of business as they were paying the wrong rate. A system of taxation that is putting companies out of business due to incorrectly charging them rates is clearly no longer fit for purpose.

There are a number of other options that have been suggested as replacements or changes to the current system of business rates. Within the sector, there is enthusiasm to transfer some of the burden to the online sector through both a digital services and/or digital goods tax. Another potential option is more frequent valuations, which would mean that property valuations are more closely aligned to economic conditions. The Dutch model is frequently cited as being superior to the current business rates model due to its administrative efficiency as well as its yearly valuations. To increase valuations would have to be accompanied by an increase in funding for the VOA, which as mentioned above is underfunded.

With cross party attention focused on business rates there is hope from within the sector that reform will be forthcoming and that steps will be taken to reduce the burden that the sector faces. This needs to be both short-term – in the form of reliefs, and long-term - in the form of a rebalancing of taxation towards the digital economy.

Recommendations

- A Royal Commission should be set up to identify systemic reforms to the current system and look to facilitate an overall reduction in the burden of taxation that the hospitality sector faces.

- A review of business rates must take into account the importance that hospitality businesses have within their communities. Changes to reliefs policy particularly should reflect the benefits that hospitality sector businesses have to villages and estates across the UK.

- The Digital Services Tax should be beefed up, and the proceeds of this tax should be used to provide reliefs to sectors like the hospitality sector, which are charged disproportionately by the current system. This should also be supported by a 2% tax on Digital Goods to ensure that local government is adequately funded.

- Short term measures should be taken to protect the hospitality sector including an expansion of reliefs. This should include an examination of state aid rules which prohibit business rates reliefs to multiple properties.

- More funding should be allocated to the VOA. The VOA is currently under-resourced and underperforming. In order to ensure that it is able to effectively function, more funds and staff should be allocated to it. Any reforms to businesses rates would be hamstrung if the VOA is not addressed.

- Consideration must be given to the current system of valuations including frequency and methodology.

- A business rates 'pause' should be given following investment in a property. The APPG would advocate a pause of 2 years for revaluation following an investment.

- The Check, Challenge, Appeal system should be reviewed. Under the current system many businesses are not paying the correct amount with very little immediate remedy