Business for Scotland Submission to Economy, Jobs and Fair Work Committee

1. Business rates are a tax that is applied to an owner, tenant or occupier of a non-domestic property. A non-domestic property is a facility that people do not live in, instead the asset is used for either commercial reasons such as a shop, pub, hotel or office, or for industrial reasons such as a factory or warehouse. On the 1st of April 2016, the empty relief rates for non-domestic properties were altered. This has led to several undesired affects which will be discussed.

2. According to the Scottish Retail Consortium (SRC), one in every eleven properties (9.09%) in town centres in Scotland are empty\(^1\). SRC explains that this is the result of rising property costs. This has happened at a time when high street sales are under pressure from increasing online sales. This pressure may lead to a drop in property prices, but that correction has yet to happen. Although retail is the largest private sector employer representing 13% of the private sector work-force (253,000 people), it has seen a significant decrease of 10,000 posts in the past seven years\(^2\). Forecasts by the British Retail Consortium (BRC) anticipate a further 23% drop in Scottish retail over the next decade\(^3\). Business for Scotland notes the importance of creating a rates system that both discourages long term disuse of buildings but does not penalise property owners who's premises are left empty for longer periods than would be desirable due solely to market forces.

Problems with the Changes

3. We accept the good intentions behind the change and acknowledge that 100% rates relief can lead to some properties being left deliberately empty and that this is a problem for many high streets. We also accept that in the face of cuts to the Scottish block grant from Westminster that savings must be made, but we believe that without certain exemptions and tweaks to the proposed policy that the changes will be counterproductive. The current system can create the following negative consequences:

(a) End speculative building of new industrial infrastructure. Evidence of this has been seen across Scotland where various companies are less inclined to invest in developing new industries. For instance, the commercial property adviser Ryden wrote in their report ‘Understandably, developers are reluctant to commit, particularly in areas where markets are struggling, if there is little prospect of a pre-let prior to completion. Many are simply not prepared to take the risk of a recently completed property being left vacant.’\(^4\)

(b) Make it cheaper to demolish unused industrial buildings than to leave them empty and pay full rates. This reduces vital industrial infrastructure that will be needed to service demand when economic growth conditions improve. In the same report by Ryden, the Rating Partner Tim Bunker said; ‘This increase in vacant rates liability on developers and
landlords will deter any future new development and lead to the demolition of older property, which will reduce industrial stock throughout Scotland.\(^5\)

(c) **Damage the financial viability of industrial development and upgrading works.** This in particular where the premises are unused during re-development and empty or only partially let for between 12 - 24 months as tenants are found.

(d) **May be difficult to find tenants quickly in rural areas.** Letting times vary by region and more rural areas which desperately need jobs and business to return will be hit hardest.

(e) **The reform came as a sudden shock to several small businesses who have not financially planned for the new empty property relief rates.** Several small development firms whose investments are bank financed on the understanding that there will be 100% rate relief may find themselves with hundreds of thousands of pounds extra costs with no ability to borrow to cover the additional costs eg:

(f) **Rents will be likely to increase in the long term for tenants.** Given the extra costs involved in property ownership it is likely that this change will drive industrial and retail rents upwards in the long term to address the additional cost. Consequently, this will increase costs to many small businesses. The counter argument is that rents will decrease in the short term as property owners seek to fill properties at lower rents. This may happen but a drastic reduction in speculative build and in some case demolition of property assets will create scarcity and rents will increase gain.

(g) **Will have a severe negative impact on small businesses.** The changes to retail rates relief will impact most on small properties that are owned by smaller businesses or handed down through families for generations will have to be sold to larger companies as they cannot be let under current market conditions.

(h) **Create a competitive disadvantage in property investment versus England in the development and upgrading of industrial premises.**

**Problems with the Timing of the Reform**

4. Furthermore the timing of this change is unfortunate for two key reasons: 1) Several projects funded under the old scheme that are currently under development will now become financially unviable. 2) Current rateable values are based on 2008 values at the height of the financial crisis when certain properties’ rateable values and rents were far higher than today. Properties should be revalued at regular intervals in order to ensure that bills are up to date.\(^6\)

**Evidence from Surveyors**

5. After speaking to various surveyors, many of them bring attention to the many disadvantages of the new empty property relief form. One of those that Business for Scotland spoke to was Brian Ronnie, a Partner at Ryden in Glasgow. In the interview, Brian Ronnie highlighted the detrimental impact the
reform has had on the market, especially in terms of the industrial and development sector. He explained that it has increased the costs for property owners across the country causing elevated uncertainty in the market. With higher expenses associated with holding stock it has resulted in buildings being demolished - a procedure which is costly as well. The development industry was just about to recover he highlighted, when the reform was implemented indicating that its improvements have now been put on hold.

Suggestions

6. There are many opportunities to cut costs and to discourage the deliberate mothballing of retail properties in particular. However, some of the following principles should be considered.

1) 100% rates relief on industrial premises should be at least six months as they are in England to maintain a competitive advantage and the increase in rates should then be phased in to 10% relief over one year - regardless of any future changes to English rates change.

2) New builds and redevelopments should be rates exempt for 18 months to reflect the average time taken to develop and let an industrial building.

3) Rural developments should be given extra rates relief in consideration of the additional letting lead times and importance of maintaining industrial infrastructure ahead of future rural development initiatives. This should also apply to community buy-outs which are less commercial in nature.

4) A grace period should be in place for all developments funded and possibly granted planning permission before the introduction of the policy in April 2016 so that they remain financially viable.

5) Taking into account that current rateable values do not reflect real market values the 100% rates relief should last longer and in all cases cuts in relief be phased in more slowly to reflect the over-pricing until 2022.

6) The revaluation of non-domestic property should be revised every 5 years. It is vital that the 2017 revaluation does not get further delayed. Ideally there would be interim reviews that will spot rapid valuation changes due to either recessions or rapid economic growth offering the opportunity for rates to be more flexible to market conditions.

7) The Scottish Government should work with local councils to create development zones where joint funding could offer rates relief over and above existing programmes. This is to encourage smaller business to expand, to utilise empty industrial and retail properties and protect them from potential demolition as well as encourage economic activity in rural or highly deprived areas.

8) Smaller companies developing property and those owned by pension funds under a certain value (TBA), should be exempt from the changes which would unfairly and disproportionately impact on their smaller more vulnerable businesses and investments.
References
Scottish Retail Consortium (SRC) ‘Submission to the Barclay Review of Business Rates in Scotland’ (October 2016)
British Retail Consortium (BRC) ‘Retail 2020: fewer but better jobs’ (February 2016)
Ryden ‘78th Scottish Property Review’ (April 2016) Page 4
The Scottish Government ‘Introduction - Business rates’