Rt Hon Rishi Sunak MP
Chancellor of the Exchequer
HM Treasury
1 Horse Guards Road
London SW1A 2HQ

Reply to: richard@pennycooks.net

25 February 2019

Dear Chancellor,

I would like to welcome you to your new post. I look forward to a positive working relationship between us in the coming years.

I am writing to you as the Co-Chair of the Retail Sector Council, and I write on behalf of the retail representatives on the Council.

The Council recently analysed the business costs faced by retailers and identified several cost pressures particularly faced by the sector and made consequent recommendations. I am in the final stages of drafting a report with these recommendations, which builds on a conversation that myself and Kelly Tolhurst had with the Financial Secretary in the Autumn. Some of the recommendations address the biggest tax faced by the sector, namely the business rate burden. I know you will be familiar with this through your Ministerial work at MHCLG.

We found that business rates account for the single largest share of tax paid by retailers - almost half of their total tax bill - highlighting just how important the issue is for the industry (more details in the appendix). As you will know, the Treasury Select Committee's recent report on business rates called it a 'broken tax' and raised concerns about the consistent above-inflation increase in rates revenue since 1990, resulting in the UK having one of the highest property tax burdens in the OECD.

Retail is the country's largest employer, and is a huge economic contributor to UK plc. The industry accounts for three million jobs and 5% of the UK economy, yet it pays 10% of business taxes and 25% of business rates. Without business rates reform, we will see an acceleration of job losses and store closures, with all the consequent impact on our high streets, a problem recognised by Government in its establishment of the £1bn Future High Streets Fund.

We therefore welcome the Government's commitment to a fundamental review of business rates. The Sector Council recognises the complexity of business rates and is keen to help the fundamental review and provide a sectoral understanding of the tax pressures and opportunities faced. Core to the review must be an acceptance by Government of what retailers, the Select Committee and many others say about the system: that the overall burden of rates is simply too high and must come down. If the review seeks a cost neutral outcome, as the last one did in 2015/16, then it will not tackle the present crisis on our high streets.

The terms of reference of the review must include the commitment to a lower rates burden across the economy and be open to options on how the reduced rates burden should be funded across broader business taxation. The Council is doing further work to explore recommendations for this.

The review also presents a fantastic opportunity to reshape the business rates system itself so that it is more responsive and supports, rather than hinders, economic growth. The Council makes recommendations to this end on:

- Removing the fixed income requirement from the business rates system;
- Scrapping downwards transition and centrally funding upwards transitional relief; and
- Supporting transparency in property costs.

More details of these can be found in the appendix to this letter.

I would particularly draw your attention to the proposal on making the property market more transparent. The domestic property market has a high degree of transparency with actual prices paid being publicly available. However, the commercial property market does not mirror this – whilst some lease and purchase data is available from the Land Registry, the lack of full transparency both hinders the smooth operating of the market by reducing the supply of information to landlords and tenants. It also hinders the ability of the Valuation Office Agency to produce accurate valuations of commercial properties, resulting in more appeals, adding to the overall administrative burden of the system for ratepayers.

We believe that, if implemented, these changes would:

- Provide a huge boost to business generally, and retailers particularly, by lowering their cost of doing business, enabling them to spend more on investing in their staff, stores, and communities;
- Enable the business rates system to be more responsive to economic conditions, so that it can act more as an automatic stabiliser and less as an economic drag, as it does currently;
- Support high streets and town centres in parts of England, particularly in regions in need of 'levelling up' with the rest of the UK;
- Greatly improve the accuracy of valuations, reducing the need for costly and burdensome appeals.

I hope that you will consider these recommendations carefully, and will look to incorporate them, or at least their underlying principles, into the remit of the forthcoming business rates review.

I look forward to your reply.

Yours sincerely

Richard Pennycook, Co-Chair, Retail Sector Council on behalf of retail representatives of the Council

cc. Retail Sector Council members

Appendix

The Retail Sector Council recently undertook research into business costs facing the retail sector. The research found that:

- Profit margins have shrunk over time for retail from 4% in 2013 to 2.5% in 2019;
- Business rates accounted for 44% of total tax costs between 2016-2018, compared to 12.5% for Corporation Tax;
- In 2017/18 the retailers analysed paid more in tax than they made in net operating profit (£4.2bn vs £3.5bn);
- Between 2016-18, the retailers analysed paid 106% of their total net operating profit (ie before Corporation Tax) in tax. Once Corporation Tax is included, this figure is even higher;
- Rises in business rates and other costs (e.g. payroll costs and the Apprenticeship Levy) more than outweighed the value of the reduction in Corporation Tax from 20% to 19% in that time.

Retail representatives on the Council have agreed a number of the recommendations following from its research and would like to see them, or the principles underlying them, incorporated into the business rates review terms of reference, in addition to the core principle of seeking to reduce the overall burden of business rates.

The Council believes that these recommendations are key to ensuring that the review is genuinely fundamental and allows positive changes to result from it that improve the functioning of the business rates system, and the property market more generally, which in turn will support higher economic growth.

Note that, while these recommendations are focused on the rates system in England, the underlying principles would be of value across the UK.

The recommendations are:

1. <u>Remove the fixed income requirement from the business rates system</u> - the terms of reference for forthcoming review should allow it to result in a business rates system that does not have to raise a fixed sum each year (allowing for inflation and appeals). This requirement is unique of all taxes, and, because it requires an element of 'reverse engineering' in the design of rates, is economically inefficient, as the multiplier is designed to raise a particular sum, rather than be set at an optimal rate. This would also mean that any falls in total revenue resulting from a change in the design of the business rates system could be mitigated by other revenue sources, for example any of the other main business taxes. The review should be open to this possibility – without prejudging the outcome - in order to ensure that it is genuinely fundamental.

2. <u>Abolish/centrally fund downwards phasing of transitional relief</u> – partly as a result of 1), the business rates system requires any relief for ratepayers facing sudden increases in rates following revaluations to be funded by ratepayers whose liability should be lower. This results in rates for retailers that can be in excess of 200% of rents in parts of England, particularly the North West and Yorkshire & Humber. Upwards transitional relief should be maintained, but the cost of this should be met through general taxation, as the current retail relief and other reliefs are.

3. <u>Transparency in property costs</u> – part of the problem with the business rates system is the quality of valuations made by the Valuation Office Agency, and the consequent difficulty for

ratepayers in understanding how they have been calculated. In order to ensure more accurate valuations at the outset (which would reduce the need for costly and time-consuming appeals), it is recommended that: data currently held by the HMRC and the Land Registry on commercial property transactions is made available to the Valuation Office; that Government reduces the ability to redact very large portions of commercial leases when they are registered with the Land Registry, and that the prescribed clauses at the start of registrable leases are required to state the rent payable during the first five years of the term. The terms of reference for the forthcoming review should include a commitment to transparency and the smoother functioning of the valuations process, allowing for this recommendation to be considered.