Response to ‘Administration of business rates in England: discussion paper’

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Our expertise is in the economics of tax policy design; we claim no particular expertise in the administrative costs of different policy options or in firms’ day-to-day experience of business rates. We therefore confine our responses to those questions in the discussion paper where we feel we can make a contribution.

Q2. What are your views on a less individualised approach to arriving at a rateable value, such as banding, a system of ‘zones’, indices, or rolling revaluations, as described above?

Banding and zones:

1. In principle the ideal is to tax each property based on an accurate assessment of its rateable value. Either banding or zoning applies an approximation to this across a group of properties, with the group defined either by a range of rateable values (banding) or a geographical area (zoning). That makes each property’s tax bill less accurate, which is undesirable. Properties with different ‘true’ rateable values would be taxed as if they were the same; and otherwise-identical properties that lay on slightly different sides of an arbitrary banding threshold or geographical boundary could attract very different tax liabilities – clearly inequitable, and conceivably distortionary if a sufficiently large difference in tax liabilities led property developers, for example, to change the location or characteristics of new developments. The distortions to behaviour that have been seen around stamp duty land tax thresholds give an indication of the kind of problems that can be caused, though it seems unlikely the problems would be as severe in this case.

2. The extent of these inequities (and of potential distortions) would depend in large part on the level at which the aggregation was set: the higher the level of aggregation (e.g. the larger the bands), the more heterogeneity there will be in within a class of bills and the more inaccuracy would be introduced (along with bigger ‘cliff edges’ at band thresholds). In the case of zoning it is not the geographical size of the zone per se that matters but the degree of heterogeneity in ‘true’ rateable value (per square metre) within the zone. If banding or zoning were to be used, the disadvantages would be less if it were based on lots of narrow bands or small, relatively homogeneous zones. The banding used for council tax in England, where Band A covers a quarter of all properties and Band H lumps together all properties worth more than £320,000 in 1991, is not a model to follow.

3. The only advantage we can see of a less individualised approach would be reduced operational cost. It may be easier (and therefore cheaper) to assign rateable values if bands or zones are used. There might also be fewer costly appeals (though not necessarily: in the case of banding, only those near thresholds might think they have been mis-valued but the tax saving at stake in such cases, and therefore the incentive to appeal, might be larger than at present). These cost
advantages would presumably be greater, the larger the bands/zones adopted. There is therefore a trade-off between the economic advantages of individualisation and potential operational advantages of moving away from individualisation. Since we do not know the size of the operational savings that could be made by banding or zoning, we are not in a position to judge this trade-off. But our starting point is that there would need to be strong evidence of substantial savings to justify moving to a less individualised approach, and we find it hard to believe that a very coarse disaggregation (such as that seen for council tax) could ever be justified. If methodological and technological advances enable greater use of automation in the valuation process and thus reduce the cost of producing accurate valuations, the case for moving to a less individualised approach becomes even weaker.

Indices:

4. If revaluations are conducted less than once a year, rateable values should be uprated in between valuations to keep them as close as possible to properties’ true market rental values. This could be done, for example, using a local rental price index for properties of a certain type. Insofar as such indices already exist (or could be compiled easily) there should be relatively little cost to using them.

5. Indexing rateable values in this way between revaluations (as opposed to instead of revaluations) is a move towards, not away from, an individualised approach. It would help to keep each property’s share of aggregate tax liabilities in line with that property’s share of aggregate rental value. The more finely disaggregated the indices used (geographically or by property type), the more accurately it will do this.

6. Having a tax base that more closely reflected economic reality would help to make business rates more transparent – for example, countering the widespread misapprehension that revaluations are associated with a general increase in business rate bills not seen in other years.

7. Such a change would also mean changing how the multiplier evolved from year to year. If average bills were to continue to track the RPI then having rateable values that increased in line with true market rents would mean adjusting the multiplier each year to reflect changes in (national) average rents as well as the RPI. This would make more explicit that the implication of current policy is for business rates to levy an ever-changing fraction of property values. Whether this is appropriate should be thought of as part of broader business rates policy. The RPI is a poor measure of household inflation (and has recently been declassified as a National Statistic for that reason), and in any case it is not clear why business rate bills should keep pace with any measure of consumer prices. The government could choose to increase bills in line with a different measure, such as national income. Alternatively, if rateable values increased each year in line with true market rents, then simply keeping the multiplier fixed would mean that business rate bills also increased in line with that tax base, like most other taxes do. One attraction of this (aside from its simplicity) is that bills would then respond (at least partially) to conditions in the rental market. For example, the falls in rents following the 2008 financial crisis would have been reflected in lower bills under this type of system. However, note that the question of how average tax bills should evolve is separate from the question of how rateable values (and therefore relative tax bills) should evolve. Whether or not average bills continue to keep pace with RPI inflation, rateable values should be indexed in between revaluations.
Q6 Some ratepayers have suggested establishing annual, 2-yearly, or 3-yearly revaluations instead of the normal 5 yearly cycle. How frequently do you think the rateable value of a property should be re-assessed at a revaluation, bearing in mind possible impacts on the predictability and volatility of bills? Why?

8. If we are to have a tax on property values, it is preferable to base it on current values, or at least on the most up-to-date values possible. This suggests that more frequent revaluations are preferable. More frequent revaluations would also mean that the distribution of the tax across properties was more responsive to the economic cycle. The appropriate frequency of revaluations reflects a trade-off between the advantages of having a tax base that is more aligned with actual value and the administrative cost of more frequent revaluations.

Q7 Would your views change if more frequent revaluations meant:

a) rates bills changed more often i.e. were less stable and less predictable than currently?

9. It is not necessarily the case that more frequent revaluations would mean less stable and predictable business rates bills. Bills would change (other than by RPI inflation) more often, but the changes would be smaller. Long periods between revaluations avoid frequent changes in bills (although there are, of course, still changes as a result of the annual RPI uprating of the tax rate). But this comes at the expense of larger changes when revaluations do take place, since we would ordinarily expect relative values to move ever further from any given starting point, so that the adjustment required to bills increases over time.

10. The stability and predictability of the revaluation process itself also matters. Delaying the planned 2015 revaluation to 2017 has also added uncertainty to a system in which, to date, everyone has known when to expect revaluations: now that the consistent practice of 5-yearly revaluations has been broken, businesses are more likely to doubt whether the 2017 revaluation (and subsequent ones) will take place as scheduled.

11. The current system provides five years of stability and predictability followed by a very large and unpredictable change. If revaluations were more frequent then adjustments in bills to reflect changes in relative property values would be small, gradual and routine. Administrative cost permitting, the latter route seems preferable.

b) it were necessary to use a less individualised approach to valuing property than currently which would mean that ratepayers with different rents, who at the moment pay significantly different bills, might pay the same amount?

12. If the cost of more frequent revaluations could be met by using a less individualised approach to valuation, there is a trade off between the benefits of more individualised valuations and the benefits of more frequent revaluations. Without knowing how great a move away from individualisation (e.g. how large the bands/zones) would be needed to pay for what frequency of revaluations, it is impossible to judge that trade-off. However, note that the use of finely disaggregated local rental price indices to adjust rateable values in between revaluations can help to ease the trade-off, allowing for low-cost frequent adjustments to rateable values at a somewhat disaggregated level.
Q8 Do you think ratepayers would be more, less, or just as likely to appeal the rateable value of their property if revaluations were more frequent?

13. This is unclear. More frequent revaluations clearly means more opportunities for dispute, but on the other hand the change in each case would be smaller.

Q22 The Valuation Office Agency publishes data on its website that shows rateable value and floorspace. What are your views on how the Valuation Office Agency could improve the data it makes available? If you had greater access to Valuation Office Agency data, how would you use it?

14. We use data to undertake research and policy analysis in order to inform public debate and promote the development of effective fiscal policy. One recent example is our use of data on business rates in a chapter of the 2014 IFS Green Budget (cited above). Greater access to VOA data would have been useful for that publication, and in future would allow us to say more about who pays business rates and more about the likely effects of different policies.

15. In writing the Green Budget chapter we encountered the following problems:

   a) We were interested in the distribution of rateable values across industries and across narrow bands of rateable value. The data that are regularly published are limited in this regard. We did find a data series that had been made available as a result of a request in September 2013. This was more disaggregated than the data usually published (though it still did not include certain useful band cut-offs such as those corresponding to thresholds for particular reliefs). It would be useful to have relatively disaggregated series on the number of properties by location, industry and narrow rateable band published on a regular basis rather than on an ad hoc basis in response to requests. Ideally, this data would make it possible to observe how many businesses would be eligible for the different types of reliefs. More generally, routinely providing more summary statistics and breakdowns of all the data that VOA has (such as those provided for some other taxes and tax bases in HMRC Statistics) would be a useful resource.

   b) In the end much of the data we used was drawn from HMRC Statistics (https://www.gov.uk/government/collections/non-domestic-rating-in-england-and-wales--2) rather than from the VOA website, partly because HMRC provided the same data in a more user-friendly form. However, it was sometimes difficult to marry the HMRC data with the VOA data. For example, both the VOA and HMRC have published documents that separate out ‘retail properties’, but they do so using different definitions of ‘retail’ so they cannot be combined to make full use of the statistics; and, more worryingly, neither states on their website what definition of retail they are using – we had to make a special request to find out. Greater co-ordination would be beneficial – starting with each website including a link to the other. It might even be worth considering whether two separate websites for business rates statistics are needed.

   c) Furthermore, there is much data on business rate revenues, collection, reliefs, etc. that is not available on either VOA or HMRC website – some are available (including at the local authority level) from DCLG, which again seems to remain entirely separate, and some which is not publicly available at all, This is not all ‘VOA data’ – local authorities, not the VOA, is responsible for collecting business rates. Meanwhile, HMRC Statistics includes little information about business rates beyond summary statistics of rateable values (e.g. data about business rate payments is lacking, while Ready Reckoners and estimated costs of tax reliefs also exclude business rates), presumably because business rates is not ‘an HMRC
tax’. But again some basic co-ordination across government would seem desirable; it cannot be sensible that statistics on business rates are sparser and harder to find than statistics on other taxes simply because business rates are administered differently.

16. Beyond descriptive patterns, availability of property-level micro-data (as opposed to summary statistics), for example via the HMRC Datalab, might facilitate econometric analysis to shed light on how firm behaviour responds to business rates policy.