CFG policy briefing: Charities and business rate relief

At present charities occupying commercial property are entitled to relief on business rates, provided it is used wholly or mainly for charitable purposes. Charities are eligible for 80% mandatory relief, which local (billing) authorities can choose to top up by an additional 20%.

Business rate relief is hugely valuable to the sector: the mandatory element alone was worth £1.5bn in 2013/14 in the UK, a figure which has grown considerably over the past decade[1]. In the same year, charities received £1.04bn in Gift Aid tax repayments.

Despite the scale and value to the sector, historically this relief has received little attention. However, in the past few years this tax relief has come under the spot light. A range of factors including the recession, funding pressure for charities and reform of the business rate system have drawn attention to charitable business rate relief.

This briefing is intended to strengthen understanding of the business rates landscape by providing an overview of recent developments, analysing the issues surrounding business rate relief and assessing what the implications may be.

The debate around business rates is unlikely to go away. It is important, therefore, that charities understand the issues so that the sector is able to fully participate in future discussions around business rate relief.

1. The current business rates system and charity relief

Business rates is a tax on non-domestic properties, billed and collected by local, or 'billing' authorities to help pay for local services. Billing authorities can be district, unitary, metropolitan borough or London borough councils, and are also responsible for applying any reliefs or discounts[2]. The level of business rates paid is calculated by multiplying the rateable value of a property (the rental value, as set by the Valuation Office Agency, or VOA, an executive agency of HMRC) by the business rates multiplier, which is set by the Department for Communities and Local Government and usually changes every year in line with inflation.

The current system of business rates was introduced in 1990 and established by the Local Government Finance Act 1988. However, a similar system has been in place since the early 20th century, and a form of property taxation has existed in England since the 16th century.

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[1] HMRC (2014): 'UK Charity Tax Relief Statistics 1990-91 to 2014-15

[2] House of Commons Library (2014): Business rates standard note.

Business rates throughout the UK

The business rates regimes in England, Scotland and Wales are similar in operation but are devolved matters.

- In **Scotland**, the rateable value of property is calculated by the Scottish Assessors (rather than the VOA) and business rates are set, pooled and redistributed by the Scottish Executive[3].
- In **Wales,** the government announced in Autumn Statement 2014 that business rates would be fully devolved to the Welsh Executive in April 2015. With the new devolved arrangement, the Welsh Executive will be more dependent on business rates as it will receive a reduced Block Grant from Westminster.[4]
- In **Northern Ireland** there is a fully devolved system of property taxation.

A number of reliefs are available on business rates, including reliefs for small businesses, businesses in rural areas, organisations in enterprise zones, and charities. Historically many charities have been eligible for relief, either through various exemptions (e.g. the Scientific Societies Act 1843) or as a result of sympathetic authorities. In 1865 case law provided greater clarity by indicating that charities should be exempt from rates[5].

Under the Local Government Finance Act 1988, charities (or the trustees of a charity) are entitled to 80% mandatory relief, provided the property is used wholly or mainly for charitable purposes. The Act also grants local authorities the power to supplement this by providing additional discretionary relief, up to 100%. Prior to the introduction of the business rates retention scheme in April 2013 the mandatory 80% was fully funded by central government, and the funding of the discretionary element was split: 25% from central government and 75% by the billing authority.

What constitutes ‘wholly or mainly for charitable purposes’ has historically been a grey area, although a number of recent cases have shed some light. The Kenya Aid Programme case, where the charity was taken to court by Sheffield City Council who believed they were ineligible for the mandatory relief that had been claimed, hinged on whether to meet the condition the charity simply had to physically occupy more than 50% of the property, or whether the context (including the extent and efficiency of use) should be considered.[6] The High Court favoured the former interpretation and photos and other evidence suggested less than half the floor space had been used. As a result the Kenya Aid Programme was ordered to pay £3.27m in unpaid business rates.

[3] House of Commons Library (2015): Business rates standard note.
[4] The Devolution of Business Rates to Wales (2015), Report to the Minister for Economy, Science and Transport from the Business Rates Panel
[5] Minister of Housing and Local Government (1959): Report of the Committee on the Rating of Charities and Kindred Bodies.
[6] Greenhalgh Kerr (2013): Charitable Relief Update – Kenya Aid Programme v Sheffield City Council [2013].

For charity shops to be eligible for relief they have to be 'mainly or wholly' used for the sale of donated stock. Here there is slightly more clarity, with guidance[7] suggesting that floor space, value of donated vs new goods or the number of items can all be used as factors to determine whether the shop meets the eligibility test. Charity shops are also eligible for retail rate relief worth up to £1,000 for all occupied retail properties with a rateable value of £50,000 or less between 2014-15 and 2015-16. However, trading subsidiaries of charities (and any shops run by them) are not eligible for mandatory relief.

Decisions on the awarding of discretionary relief is a matter for local authorities. However, government guidance[8] states that it is important they have '*readily understood guidelines for deciding whether or not to grant relief and for determining the amount of any relief given'*, and that blanket policies to refuse relief across the board should be avoided. To receive discretionary relief local authorities often check applications against set criteria, for example whether the charity supports the council's strategic priorities, or whether the charity's work benefits the local community. Local authorities may also check charity accounts to determine financial need.

To receive both mandatory and discretionary relief, charities need to apply to their local authority. Once relief is granted, local authorities need to provide one year's notice[9] if they plan to revoke or decrease the amount of discretionary relief awarded.

2. Why are charities eligible for relief?

Business rate relief is a form of charity tax relief. One of main reasons government has granted charities tax relief is to ensure that as much money as possible serves good causes. Business rate relief should be seen therefore, like other charitable tax reliefs, as recognition of the contribution that charities make to society.

As outlined above, charities have historically had access to exemptions from business rates, either as, for example, scientific societies, Sunday and ragged schools, or educational bodies. An 1858 Select Committee report stated that for ratings to apply, the occupier should receive some private benefit from the property, and '*so it follows that where lands or buildings are occupied for a public purpose, they are exempt from rate…'*[10] There is, therefore, a long tradition of charities being exempt from property taxation in carrying out their charitable objectives.

Under the Localism Act, local authorities are able to grant discretionary business rate discounts in any circumstances, provided regard is given to the interests of council tax payers[11].   Therefore while mandatory rate relief exists in recognition of charities' role in delivering public benefit, discretionary rate relief is currently linked to how local authorities

[7] Office of the Deputy Prime Minister (2002): Non-domestic rates: Guidance on rate reliefs for charities and other non-profit making organisations.
[8] Office of the Deputy Prime Minister (2002): Non-domestic rates: Guidance on rate reliefs for charities and other non-profit making organisations.
[9] Legislation.gov.uk (1989): The Non-Domestic Rating (Discretionary Relief) Regulations 1989
[10] Minister of Housing and Local Government (1959): Report of the Committee on the Rating of Charities and Kindred Bodies.
[11] House of Commons Library (2012): Business Rates: Discretionary discounts standard note.

interpret the value of charities in their local area and how this interacts with other competing priorities.

3. The cost of charity business rate reliefs

In terms of value to the sector as a whole, business rates relief is the largest tax relief available to charities. The mandatory element alone was worth approximately £1.5bn in 2013/14 according to HMRC; Gift Aid – the second biggest relief – was worth £1.04bn[12].

The latest data submitted to the Department for Communities and Local Government[13] by the 326 billing authorities in England shows that:

- **Local authorities received £20.5bn in business rates income** in 2013/14, after payable reliefs, cost of collection and other arrangements – a slight fall from the previous year.
- All mandatory and discretionary reliefs **cost £2.5bn** in 2013/14 (excluding small business rate relief), a £120m increase from the year before.
- **Charities received £1.4bn** in mandatory rate relief in 2013/14, a 7% increase from 2012/13.
- Local authorities granted £106m in discretionary rate reliefs in 2013-14**. Charities were granted £43m in discretionary rate relief.**

4. What has impacted on business rate policy?

In recent years a number of external factors have led to an increased awareness of the business rate relief available to charities, and have influenced attitudes towards it.

a. Local authority funding pressures

One of the biggest factors influencing local authority decision making and their approach to business rate revenue has been budgetary pressures. Local government was subject to some of the largest cuts, as a proportion of the total budget, in both of the Coalition Government's Spending Reviews. According to the National Audit Office, local authorities have seen a real terms cut of around 37% between 2010/11 and 2015/16.[14]

Modelling by the Local Government Association (LGA) suggests that the funding shortfall between available and required income will grow by approximately £2.1bn per year across England due to cuts and pressure on services (for example, through population changes)[15]. Cash-strapped councils have inevitably been looking to make cost savings where they can, and this has put added pressure on discretionary rate relief for charities.

[12] HMRC (2014): UK Charity Tax Relief Statistics 1990-91 to 2014-15
[13] Department for Communities and Local Government (2014): Statistical Release: National non-domestic rates collected by local authorities in England 2013-14.
[14] National Audit Office: Financial sustainability of local authorities 2014 (2014)
[15] Local Government Association (2013): Future funding outlook for councils from 2010/11 to 2019/20.

b. Pressures on the High Street and the growth of charity trading

UK high street trading has suffered significantly over the past decade due to a range of factors including the growth of out of town shopping centres and online trading. The recession also saw household incomes further squeezed, and since the financial crisis many well-known high street chains have closed down.

The significant pressure on the charity sector's finances, driven by a considerable cut government spending with the sector has forced charities to diversify their income. Many have turned to trading as a means to generate a sustainable stream of income. The number of charity shops has doubled in the past 20 years and the CRA estimate there are now over 10,000 in the UK, generating over £220m for charities[16].

A consequence of this growth in charity shops, running in parallel to pressure to private shops on the high street, is that increasingly charity shops have been criticised for distorting the market due to the tax benefits they receive. However, research carried out by Demos[17] found that there was no evidence that charity retailers have a negative impact on the local economy. In contrast, charity shops are exerting a stabilising influence on ailing high streets - maintaining footfall, catering to specific local needs, and filling shops that would otherwise be empty.

The Portas and Grimsey reviews

In 2011 the Government commissioned Mary Portas to conduct an independent review and make recommendations on how to revive the UK's high streets. During the course of the review Mary Portas suggested it could be helpful to use the tax system to limit the number of charity shops, but stopped short of including the recommendation in her final report. However, the report still levelled some criticism at charity shop rate relief, suggesting that it '*builds a disadvantage into the system… Landlords are choosing the safe option of charity shops and small new retailers aren't getting a look in*[18]'.

In September 2013 Bill Grimsey, former CEO of a number of high street chains, published his 'alternative' high street review, suggesting that the Portas project had lost momentum. The report identifies a number of problems with the current business rate regime and suggests that a 'root and branch review' of the system is required – a view shared by others (see below). While there is no explicit criticism of charity relief in the report, it includes recommendations to reduce mandatory rate relief for charities to 70% (putting the additional 10% revenue into a ring-fenced pot for local authorities to use for projects which benefit the community); and establish greater clarity over the mandatory relief criteria[19].

However, neither of these reports' claims on charity shops have been substantiated with any research to indicate that charity shops distort local markets.

[16] **http://www.charityretail.org.uk/faqs_shop.html**
[17] Demos (2013): Giving Something Back **http://www.demos.co.uk/files/DEMOS_givingsomethingbackREPORT.pdf?1385343669**
[18] Mary Portas (2011): The Portas Review: An independent review into the future of our high streets.
[19] Bill Grimsey (2013): The Grimsey Review: An alternative future for the high street.

Moreover, it is unlikely that any research would demonstrate that charity shops have a distorting effect. This is because charity shops are not directly competing with small businesses in most cases. A charity shop's biggest source of competition is generally other charity shops. Additionally, the requirement that the building must be used 'wholly or mainly for charitable purposes' acts as a check on availability of the relief and ensures that charity shops undertake a unique function, different from other retailers on the high street.

Charity shops have come under the spotlight, but it must be remembered that these are only one part of the sector and the implication for changes to business rates have not properly considered the impact on service delivery charities which make up the vast majority of the sector. There is a danger that policy formulation becomes focused on one type of charitable activity, ignoring the impact on the rest.

c. Localism

Localism, the devolution of decision-making power from central government to individuals, communities and councils, has been a major policy theme of the Coalition Government.

Business rates, and the ability to set reliefs, have been identified as one of the key areas where local authorities would benefit from greater autonomy over decision making. The Localism Act, which came into force in 2011 and sets out a number of changes to the law to devolve power, amended the Local Government Finance Act 1988 to give councils the ability to offer business rate discounts, provided they are paid for from their own resources. Localism was also the driving principle behind the business rates retention scheme, which aims to give councils greater control over the money they earn.

While it is too early to fully understand the impact of the Act, particularly the financial impact, of both of these changes, one of the wider implications is that business rates are increasingly seen as a local matter and there are calls that this local control should extend to include the setting of all reliefs. If this approach was adopted, it could have a significant impact on charitable rate reliefs, effectively creating a 'postcode lottery' for charities.

By favouring localism and local decision making, central government has also indicated that they will not intervene should local authorities change their approach to charity reliefs. During the development of the business rate retention scheme, a number of charity sector bodies, including NAVCA, NCVO and CFG, raised concerns that the funding changes were likely to result in local authorities reviewing charity reliefs as a burden. However the Government's response, while reinstating their commitment to the current levels of mandatory relief, was to stress that setting discretionary reliefs was a local matter.

Greater local autonomy over business rates means that they are increasingly viewed as a flexible tool that can be used to raise revenue and meet local needs. While this is not bad in itself, it does mean that councils are likely to change their business rate relief policies and this will mean that charities will need to be aware of these changes and adapt their financial plans. As one council's policy document states, the purpose of the discounts is to '*provide* *greater opportunity for local authorities to use innovative approaches in delivering a wide range of policy objectives through use of this new power[20]'.*

d. Structural review into the structure of business rates

While not directly related to charity rate reliefs, one notable issue is that there are growing calls amongst influential bodies for a full scale review of the business rates system. The Institute for Fiscal Studies' Mirrlees Review, which brought together experts to identify the characteristics of an effective tax system, and to assess how the UK's matches up, stated simply that '*the business rate is not a good tax*'[21]. It criticises the tax for artificially distorting firms' production choices away from property, and for encouraging land to be used inefficiently, a view it has repeated in subsequent Green Budgets and briefings.

Elsewhere criticism has also been made of the fact that a large – and growing - proportion of trading is no longer based out of single premises but online, making a tax based on property less relevant. Additionally the system has little flexibility: the ratings do not change regardless of external circumstances (e.g. poor trading conditions during the recession), but are simply increased each year in line with inflation.

In Autumn Statement 2014, the Chancellor announced that a 'root and branch review' of business rates. The government has now published a discussion paper[22] which has asked for respondents to alternative systems for business rates. The Chancellor also stated in Budget 2015 that he favoured '*far reaching reform'* of the business rate system. The paper states that the review will not consider charities directly; however it notes that any decisions on the future structure of the relief are likely to have an impact on the sector. It is therefore asking for evidence on the importance of the relief to charities. It is important that charities of all kinds feed into this review.

5. Business rates relief and tax avoidance

The Rating (Empty Properties) Act 2007 changed the law so that rather than receiving 50% rate relief on empty properties, landlords would be liable for the full rates once the property had been unoccupied for over three months.

The legislation meant that landlords with empty commercial properties, looking to avoid paying business rates on top of losing out on rent, increasingly started to lease them out to charities at heavily discounted rates (or even for a donation to the charity), often on a short-term basis (42 days or just over) or with a short notice period.

Arrangements between charities and landlords to make use of empty properties can be mutually beneficial and the previous government has supported organisations, such as

[20] City of York Council (2013): Report of the Cabinet Member for Corporate Services Discretionary & Mandatory Business Rate Relief and Discounts
[21] Mirrlees, James et al (eds) on behalf of the Institute for Fiscal Studies (2010): 'The taxation of land and property' in The Mirrlees Review - Reforming the tax system for the 21st century
[22] HM Treasury (2015): Business Rates Review: terms of reference and discussion paper **https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/413070/business_rates_review_final.pdf**

Meanwhile Space, to broker such arrangements. The Meanwhile Project operated in 2009-10 and worked '*with landlords, agents, potential occupiers and local authorities to enable uses that benefit the community while something else is waiting to happen*[23]'. The charity 3Space also does similar work, making vacant spaces available for pop-up community projects. In many cases charities' use of vacant properties are positive arrangements which limit the number of vacant properties in town centres.

However, in addition to the creation of many legitimate arrangements, the changes to business rate liability also gave rise to instances of charities entering into tenancy agreements which have been identified by local authorities as business rates avoidance by landlords, or as failing to meet the eligibility criteria for mandatory charity relief. The Charity Commission became aware during the course of one case (in 2011) that 700 tenancy agreements had been entered into on the basis that the charity involved in the case (Public Safety Charitable Trust) would occupy empty properties. In the past few years private companies have been created which profit from setting up these often dubious arrangements. One council even reported that they do so by submitting Freedom of Information requests to obtain the details of empty properties[24].

In cases like these, there is a fine line between what is and isn't considered legitimate behaviour by charities. The Charity Commission has reissued guidance on charity tax reliefs which makes clear that trustees must not enter into any arrangements which can damage the reputation of the charity and may bring it into disrepute.[25]

As outlined above, to qualify for mandatory relief (and therefore pass as legitimate use by charities) the building has to be 'wholly or mainly used for charitable purposes', and many of the contentious cases hinge around this condition. The Public Safety Charitable Trust, which occupied over 2000 properties in exchange for a donation from landlords, had to wind up after losing a court case and finding itself liable for a large rates bill. The charity was installing Bluetooth/WiFi transmitters into the empty properties to omit safety messages – which the High Court ruled did not believe constituted 'wholly or mainly' for charitable purposes.

It is also worth noting that while previously local authorities had little incentive to invest in checking that charitable rate relief was granted legitimately (as it would not have any bearing on their funding levels) this has changed as a result of the business rates retention scheme and is likely to lead councils taking a 'hard line' on business rate reliefs.

6. Business Rates Retention Scheme

The business rates retention scheme (BRRS) was introduced as part of the Local Government Finance Act 2012. The reforms, which came into force in April 2013 in England only, represented a major change in the way that local government is funded. Under these arrangements, local authorities are able to keep half of all business rates revenue raised

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[23] See http://www.meanwhile.org.uk/about-us.
[24] Local Government Chronicle (2013): Charity rate 'scam' hitting coffers
[25] **https://www.gov.uk/government/publications/charity-tax-reliefs-guidance-on-charity-commission-policy/charity-tax-reliefs-guidance-on-charity-commission-policy**

locally, and are given greater flexibility to pool revenue with other local authorities and borrow money against future income growth.

a. Previous operation of the business rates regime

Under the previous system the business rates revenue collected by authorities was sent directly to HM Treasury and pooled at the national level. It was then redistributed to local authorities (as their 'formula grant settlement') using a complex formula.

b. The business rates retention scheme – in more detail

Under the BRRS, each local authority is provided with a baseline figure of revenue based on the formula grant. Local authorities can then retain 50% of the rates collected (the local share) with the other 50% is paid to central Government (central share), although revenue will still meet their baseline figure through a top-up and tariff system (more below). Where retention will make a difference is on any growth (i.e. anything collected above the baseline), as local authorities will be able to keep up to half of any additional revenue. However, in line with the principle of the scheme that '*risk and rewards should be shared*[26]' between central and local government, local authorities will also have to fund 50% of any *new* reliefs granted (existing reliefs are already accounted for in the baseline).

The new system does include a number of mechanisms to help ensure that the system is equitable and does not disproportionately benefit the richer local authorities with greater potential for business rate income growth.

- A system of top ups and tariffs will increase or reduce a local authority's business rate income to bring it in line with its baseline agreement.
- For additional business rate income, Government will calculate a levy rate for each local authority which has a disproportionate amount of business rate growth. The minimum a local authority will be able to keep is 25 pence in every pound, and the maximum 50 pence.
- Safety net payments – funding set aside by Government to support authorities whose income has dropped significantly.

c. Rationale for the new system

The Government stated that the rationale for reform of business rate funding was that there were a number of problems with the previous system. It suggested that the system was '*one of the most centralised in the world*[27]', which did not give local authorities enough flexibility or autonomy to do what was best for their area, and that it failed to reward local authorities for generating growth. As a result there was no incentive to support business[28].

[26] Department for Communities and Local Government (2012): Business rates retention: policy statement
[27] See https://www.gov.uk/a-plain-english-guide-to-business-rates-retention
[28] Department for Communities and Local Government (2012): Plain English Guide to: Business Rates Retention and the 2013-14 Local Government Finance Settlement

The previous business rates regime had also long sustained criticism from local authorities and support bodies too. The Local Government Association, in their report *Balance Transfer – from Whitehall to Town Hall* said: '*Even though many councils raise more in council tax, business rates and other local revenue than they spend, all are having to make deep spending cuts… [Determined by] an untransparent funding formula that everyone can find some fault with. Local democratic accountability is undermined by the current arrangements*.'[29]

Government stated that it hoped that the BRRS, by restoring the link between the rates collected and revenue received, would incentivise local authorities to encourage growth and job creation in their area.

d. Charity rate reliefs under the new scheme

The Government has consistently stressed that there will be no changes to the architecture of business rates as a result of the scheme, and that the level of relief available to charities will remain the same (80% mandatory 20% discretionary). The only difference will be in the way in which this is funded.

For any additional new reliefs, the cost is shared 50-50 between the local authority and central government. In the case of charity rate relief, this means that local authorities will now have to fund more of the mandatory element (half of the 80% relief, previously nothing), but less of any discretionary relief (half of up to 20% relief, previously three-quarters). For all existing reliefs, there will be no cost impact as the level of reliefs (mandatory and discretionary) will be taken into account in the funding settlements. However, the new funding split has had a material impact on any new reliefs granted – the net effect being a greater cost for local authorities.

In addition to the costs associated with any new mandatory reliefs, the issue of rate relief is further complicated with section 69 of the Localism Act 2011 which gives local authorities the new power to grant discretionary rate relief to businesses, provided they are satisfied it is reasonable to do so with '*regard to the interests of [council tax payers*[30]*]*', i.e. it supports growth in the area. In addition to any new charity reliefs coming at a greater cost, this also means that there is more competition for the same 'pot' of discretionary funding.

e. What has the impact of the scheme been?

The BRRS came into force in April 2013, and so it is too early to say fully what the financial implications of the scheme have been. However what is clear, however, is that there is greater volatility in local authority funding levels. The Local Government Association has highlighted the increased risks to councils in forecasting and calculating their income from business rates.[31]

[29] Local Government Association (2013): Balance Transfer – from Whitehall to Town Hall
[30] House of Commons Library (2013): Business rates standard note.
[31] LGA (2013): Rewiring Public Services: The story so far – business rate retention scheme

A study by the Joseph Rowntree Foundation on the impact of spending cuts at a local authority level found that given the volatility of economic performance in local areas, most authorities have not seen growth. Out of 121 single-tier authorities, only 19 showed real growth in their income per capita over the period between 2009 and 2014. Over 100 showed a decline. While a return to stronger levels of economic growth may result in increased business rate income, in the medium term, the scheme is likely to have a negative impact on the finances of local authorities.

The decline in business rate income has also come in those areas where local government spending cuts have had the biggest impact. Manchester, which has recently seen significant devolution, saw business rate income per capita fall by £143 in real terms between 2009 and 2014. Trafford, Bolton, Leicester, Nottingham and Luton also saw significant reductions in per capita income. By contrast, Westminster and Kensington & Chelsea saw significant increases in income per head.

> *'The new business rate retention scheme means that the council carries more of the risk of volatility in the business rate tax yield. This includes the effects of successful rating appeals, business closures and new business start-ups or expansion as well as sharing the cost of mandatory and discretionary reliefs with government'*
>
> **A council business rate consultation, 2013**

The changes also mean that local authorities are likely to prioritise raising business rate revenue in a way that they did not before. Lots of factors affect growth in a local area, however for the most part these are out of control of the local authority. This could mean that local authorities will be more inclined to wield greater control over those aspects that they can, for example, by not granting additional discretionary rate relief to charities. And given the above data on the geographical impact of changes in business rate income, this is likely to take place in those areas where spending cuts are greatest and the operating environment for charities is toughest.

f. What is the impact of the scheme been on charities?

While the Government has explicitly stated that there would be no change to mandatory rate relief, a number of concerns have been raised by charities and sector bodies about the possible impacts, including:

(i) Local authorities have less funding to grant discretionary reliefs

Since any new charity setting up or apply for business rate relief in an area will come at a greater cost to the local authority as a result of the scheme, concerns have been raised that this could lead some local authorities to determine that it would not be financially viable to also support the charity sector through discretionary reliefs at the same level they did previously. This may also be exacerbated by the additional powers in the Localism Act to grant discretionary relief to businesses. A local authority may decide that with each new charity claim for discretionary rate relief coming at an additional cost, the 'funding 'pot' could be better spent on supporting and nurturing businesses in the area, rather than charities who already receive the mandatory 80%. Anecdotal evidence has also suggested that local authorities have been increasingly tough on granting relief to charities, with charities losing discretionary rate reliefs in order to help reduce council expenditure.

For the most part, local authorities have been slow to adapt to the change in business rate reliefs system. But now many are looking to reduce their exposure to avoidable costs, including discretionary rate relief as well as starting to search for added or increased rateable values that can be placed into the Rating List to either generate additional income or off-set losses in income due to successful rating appeals which can now have a significant impact on their income.

(ii) The scheme will give local authorities a financial incentive to withdraw discretionary reliefs already granted

The funding for the BRRS was set so that local authorities' baseline figures (the amount they can expect to receive in total, excluding any revenue from business rate growth) have taken into account any mandatory and discretionary reliefs they already grant. While local authorities cannot amend the mandatory reliefs offered, they can withdraw discretionary reliefs, and NAVCA raised concerns that this will then create '*a financial benefit to local authorities that have traditionally given discretionary relief but then decide to discontinue offering it.*'[32]

Moreover, with local authorities facing an even tighter funding settlement over the coming Parliament, it is likely that more councils will be under pressure to find savings through discretionary reliefs.

Related to this, the uncertainty for charities around the future of discretionary rate relief means that charities may choose to remain in their current location, rather than move to a better suited premise where they may not be able to access discretionary rate relief. At a time when many charities are in the process of restructuring, uncertainty in business rate relief is a significant factor.

(iii) With new charities coming at an additional cost, local authorities may be discouraged to support the development of the charity sector in their area

The impact of the BRRS will be felt across the charity sector, but one area that has raised early concerns has been the arts and culture, particularly museums. The issues raised for this part of the sector can be taken as indicative for other charities.

In a statement during the consultation on the BBRS, the Association of Independent Museums (AIM) said that local authority support was vital when museums want to expand their charitable activities into new areas or new sites. They raised concerns that the additional costs in terms of lost relief, particularly in the cases of large historic sites with high rateable value, could act as a significant barrier to local authority support.

[32] NAVCA (2011): Local Government Resource Review: Proposals for Business Rates Retention

AIM also suggested that the system could affect local authority decision making when it comes to community asset transfer – the process of local authorities handing over the ownership of buildings and land to community organisations. AIM's statement said local authorities may be disincentivised from allowing the transfer of heritage and museum functions to independent museum trusts because '*the financial benefit in terms of the rates bill … would only amount to around half of the existing cost, rather than all of it*[33]*',* i.e. central government would no longer meet the full 80% relief. The statement voices concern that the additional costs may be forced on the new museum trust through the funding agreement with the local authority.

Early evidence suggests that in museum sector fewer museums are now receiving discretionary rate relief than before and that many are having their discretionary rate relief phased out as councils seek to retain the funding.

However, as there has been no comprehensive review of the impact of the BRRS on charities, and this means it is impossible to identify any national trends.

(iv) Local authorities will place greater focus on raising business rates revenue, and less on the valuable role that charities play in the local area

A less tangible but nonetheless important potential effect is that rather than taking a holistic view, local authorities may start to focus predominantly on the cost of a new charity, rather than considering the wider social value and economic growth (in terms of employment and income generation) charities can bring. NAVCA raised concerns that the cost of voluntary sector organisations and funding pressures could '*inadvertently lead councils to taking a purely financial view and determining that voluntary sector organisations are a cost rather than an asset*[34]*'*.

It is important that charities are not seen as a 'burden' on a local area, and that the benefits from charities are widely understood.

(v) Challenges for charities that work nationally or internationally

Many local authorities have adapted their business rates policy to prioritise charities that have a local impact or meet a council's strategic priorities. Whilst this is understandable, it does have an impact on organisations that have a national or international brief. Charities that work on a national or international basis make an important contribution but the shift in the cost burden for rate reliefs can lead local authorities to discriminate against organisations that do not have a local footprint. This was not an intention of the BRRS, but the incentives that have been created through it have led to a narrowing of the discretionary rate relief base.

Case Study

An international development charity which supports children in the developing world had to re-apply for discretionary rate relief. The charity said: *'We were unsuccessful, mainly because our work does not benefit [the local authority] residents, but overseas children. So this year we have to pay over £2,000 in rates. For a medium sized charity…this is a significant amount.'*

a) Local authorities are becoming more stringent when checking and applying charity relief

Prior to the introduction of the BRRS, local authorities had little incentive to police the validity of (particularly mandatory) relief claims as business rate income was static regardless. However, under the new scheme, the level of business rate revenue received will directly affect the local authority's financial position, providing a strong incentive for them to maximise the collection of rates and ensure reliefs are being used correctly.

Charities have reported that local authorities have started to undertake regular checks on charity property to ensure it is being used properly. A representative from one council said that, particularly in the case of charity shops, they were going to '*have to be slightly more proactive and actually check the use of the shop, particularly in relation to the proportion of recycled vs new goods. Although if this does result in taking action against shops, it does raise questions around whether it's better to clamp down or take a more laid back approach and have more shops open.'*

Charities should, therefore, make sure that they thoroughly review their operations to ensure that they are meeting criteria for mandatory and discretionary business rate relief.

7. Conclusions and recommendations

The business rate landscape has changed significantly over the past few years. The business rates retention scheme means local authorities have a different perspective on charities and the business rates they pay. Funding pressures are leading councils to assess all the funds going out and question whether they are a good value for money. With high street under pressure it is perhaps inevitable that the role of tax reliefs in successful charity shops has been questioned.

Business rate relief is a hugely effective and valuable relief. Relief on business rates supports charities to have a hub and physical presence within communities. For many charities, paying full business rates isn't an option – operations would either end up being significantly scaled back, or they may be forced to move to new premises which may not be suitable for their work. Charities play a vital role in local communities, whether by supporting the vulnerable, providing employment or adding to an area's vibrancy.

It is not only charities that benefit from rate relief, but ultimately beneficiaries and society more widely. A growing charity sector helps local communities to thrive, generating positive benefits to an area in terms of growth and employment. Charities are also being asked in some cases to deliver many of the services previously delivered by the council, business rate relief is an important way for charities to deal with the operating costs of these changes.

Charities and sector bodies need to work together demonstrate the value of this form of tax relief and the added value that they enable charities to bring to their local area. Charity Finance Group believes that there are a number of measures that need to be taken to improve the business rate relief system for charities.

Recommendations

- **Improve charities awareness of business rate relief rules.** There have been a number of cases on business rate relief rules that affect charities but the implications of these cases have not been widely communicated to charities. The Charity Commission and HMRC should work together to provide better information of the rules around business rate relief. This will reduce the risks of charities claiming rate relief in error and protect charities against business rate scams.

- **Charities need to better demonstrate their value to the local community when applying for rate relief.** Charities should be explicit about the value their organisation adds and communicate this with local authorities when applying for business rate reliefs (mandatory or discretionary). Charities need to think beyond core activities and also consider the charity's contribution to local growth, e.g. through volunteering or employment opportunities when communicating to councils on rate relief. Initiatives such as the Charity Retail Association's effort to measure the social value generated by charity shops are a welcome part of this process.

- **Create a dedicated hotline for charities to report business rate relief scams.** HMRC and Charity Commission should operate and promote a confidential line for charities to report individuals that approach them to participate in business rate relief scams.

- **There is a need for better data on business rates.** There is sparse quantitative information available about the types of charities that claim business rate relief available and their locations. HMRC should work with DCLG to publish better data on this, so that gaps in claiming are identified.

- **Local authorities need to have a holistic view of the role of charities.** Funding cuts and the changes under the business rates retention scheme have led some local authorities to cut discretionary rate relief for charities. However, councils should take a holistic view: a charity may not bring in as much revenue as other organisations, but they do create social capital needed for sustainable growth.

- **A full review of the business rate retention scheme's impact on charities.** A number of charities have reported the loss of discretionary rate relief, and councils are tightening their discretionary rate relief policies. This was not the intention of the BRRS but it is important that the impact of the scheme is understood and if significant negative impacts are identified, policy action taken.