Appendix 1

Department for Communities and Local Government

HM Treasury

Business Rates Avoidance

Summary of Responses

July 2015
Department for Communities and Local Government
HM Treasury

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July 2015

ISBN: 978-1-4098-4635-2

Summary of responses

Methods and scale of avoidance

Q1. Which methods of avoidance are you familiar with and how commonly have you seen them used?

This question attracted a very high level of comment. The majority of local authorities were aware of or came across more than one type of avoidance in their areas. A number of respondents also mentioned a specific method of avoidance in relation to pubs/ bars. The most common methods they were familiar with were those highlighted in the December 2014 discussion paper:

a. avoidance of empty property rates through repeated periods of artificial/contrived occupation

b. avoidance of empty property rates through artificial/ contrived occupation of properties by charities

c. avoidance of empty property rates through artificial/ contrived arrangements where charities own a property and it appears that when next in use it will be mostly for charitable purposes

d. avoidance of empty property rates through the use of insolvency exemptions.

Authorities suggested that use of the first avoidance method list above had increased since the ruling in the Makro Properties Limited v Nuneaton & Bedworth Borough Council case in 2012.

Business respondents suggested they were familiar with many of the avoidance methods. Many businesses suggested that there was a distinction between different methods of avoidance in that some methods were considered to be a flexible way to allow ratepayers to manage their liability for business rates, whereas others were aggressive avoidance scenarios. The distinction appeared to centre around the extent to which arrangements were contrived and whether third parties were involved.

Q2. What do you consider to be the defining features of specific methods of avoidance?

This question was mainly answered by local authorities and attracted both general and specific comments. The respondents who answered this question directly were focused on

the defining features of the most popular avoidance methods. It was suggested that the defining features of the avoidance of empty property rates through repeated periods of artificial/contrived occupation were: that the occupier sought to occupy the property as minimally as possible; and that the landlord and occupier entered into a tenancy agreement that required a very short notice period while the property is actively marketed. Another feature is that ratepayers notify the council retrospectively of occupation periods.

In cases where avoidance of empty property rates through artificial/ contrived occupation of properties by charities takes place, it was suggested that unsuitable premises (i.e. those that were overly large or located inconveniently) for the charity's purposes were often taken on. Also, it was suggested that charities are often unable to substantiate their claims of future use – on which the eligibility of a future relief depends - and occupation is minimal or infrequent. Some responses identified the use of insolvency exemptions to avoid rates, as highlighted by the discussion paper. One of the more general comments was that agents are often involved in advising occupiers on artificial or contrived arrangements for the purposes of avoidance.

Q3. What is your view on the scale of avoidance?

The majority of local authorities felt that the scale of avoidance is growing. A number of local authorities expressed the view that it is difficult to assess accurately the level of avoidance although some of them provided estimates for their areas. The Local Government Association's initial estimates suggest around £230m per annum is lost to avoidance.

The majority of other types of respondents did not comment on this question. Nevertheless some representative bodies suggested that some local authorities may overestimate the involvement of certain organisation types in rates avoidance or that there isn't sufficient evidence on the scale of business rate avoidance. A few rating agents suggested that the scale of avoidance is either low or declining.

Tackling avoidance

Q4. What are your views on giving local authorities general or more specific anti-avoidance powers, wherby authorities can withhold reliefs and exemptions where they reasonably conclude that the main puropose or one of the main purposes of the ratepayer's occupation or arrangements is to receive the relief or exemption and/or that the arrangements or occupation is contrived or artificial?

This question attracted a high number of comments. Some local authorities were in favour of the government providing them with greater powers (either through specific or general anti-avoidance rules) although a mix of local authorities and rating agents were opposed.

Those opposed claimed that sufficient, clear and well established powers, statutory mechanisms and rules already exist. It was suggested that granting specific anti-avoidance powers could lead to differences in interpretation of the legislation by local authorities, causing more cases to be taken to the courts, which in turn would cause resource and funding problems to local authorities. Local authorities who were in favour of these powers felt that legislation would need to be developed so that they clearly define the responsibilities of the parties involved and set out potential consequences for the ratepayer.

Q5. What changes could be made to legislation that sets out which types of ratepayers or properties are eligible for exemptions or reliefs, to make it easier for authorities to distinguish between ratepayers legitimately entitled to reliefs or exemptions and those seeking to abuse them?

This question attracted a wide variety of comments and the majority of them suggested that legislation should be tighter, clearer and more prescriptive. Some respondents suggested defining the occupation of a property as a percentage of the utilised floor space; or extending the length of time an occupier is required to occupy a property in order to qualify for a relief; or placing a cap on the number of times that an exemption for an empty property can be claimed. Others suggested removing/reducing some reliefs or exempting properties below a certain rateable value threshold could reduce abuse of reliefs. It was also suggested that the Insolvency Service and the Charity Commission should use their powers more effectively or be given more powers. A few respondents suggested that there is no need for any change in the legislation.

Q6. Do you have any views on what changes could be made to the administration of reliefs and exemptions that would help prevent or tackle business rates avoidance?

This question attracted a range of comments, the majority from local authorities. The respondents mentioned that limiting backdating for retrospective claims and a more formal application process would make the granting of reliefs a more transparent process. In addition to this, better training could be given to those tasked with considering applications for exemptions and reliefs from ratepayers. Another suggestion was that local authorities should have the right to inspect the interior of empty properties before any relief is granted and that ratepayers should be obliged to notify local authorities of any changes in terms of occupancy. It was also suggested that reliefs should be discretionary so local authorities could set their own criteria.

It was suggested by a high number of respondents that ratepayers should be able to dispute their business rates liability at a Valuation Tribunal rather than a Magistrates'

Court. This would ensure rates continued to be paid whilst ratepayers disputed their liability.

Q7. What are your experiences in taking action against those avoiding business rates?

The majority of responses came from local authorities who mentioned that they have experience of taking avoidance cases to court. The main comment was that doing so places a considerable burden and cost on the local authority in terms of the work involved, such as carrying out property inspections and gathering evidence, which was seen as a significant barrier to taking legal action. In contrast, it was suggested that those involved in avoidance schemes were incentivised to take legal action and legal advice because the gains to be made from successfully avoiding business rates were sufficiently high.

Q8. Do you have any views on what steps could be taken to help authorities come together to tackle attempted business rates avoidance?

The majority of the respondents suggested that a centralised information sharing portal where local authorities could share experiences and solutions would be helpful and provide more consistency to the way they tackle avoidance. Others requested further financial support from the government such as a funding scheme that would help local authorities take joint action in order to cover legal costs.

Some identified the need for two-way data and information sharing between local authorities, the VOA and other public bodies to help strengthen attempts to tackle avoidance. While others called for guidance for local authorities on gathering evidence of avoidance, on what is expected of the council's inspectors, on the legal issues involved in tackling avoidance, and on best practices. It was suggested that local authorities could act proactively by withholding reliefs and exemptions.

Q9. Do you have any alternative suggestions as to how to tackle business rates avoidance?

This question attracted a range of views, the majority of them from local authorities. It was suggested that increasing awareness of avoidance schemes and improvement of understanding of the rules around business rate reliefs are the best methods available to the government to reduce tax avoidance by charitable vehicles. Closer co-operation with HMRC could enable ratepayers to report any new avoidance schemes more easily. Another suggestion was that the responsibility of paying business rates could be placed on the freeholder so that the local authority would be able to recover the charges against the

property. In general the need for improved communication channels between local authorities, the Charity Commission and Companies House was highlighted.

Appendix 2

Charity Retail Association
The voice of charity retail

Institute of Fundraising

CFG INSPIRING FINANCIAL LEADERSHIP

NCVO

Business Rates Avoidance: Discussion Paper

March 2015

Joint response from Charity Finance Group, Institute of Fundraising, Charity Retail Association and NCVO

Founded in 1987, Charity Finance Group is the charity that works to improve the financial leadership of charities, promote best practice, inspire change and help organisations so that they can deliver the biggest possible impact for beneficiaries. CFG has over 2300 members and they manage nearly £20 billion in charitable income.

The Institute of Fundraising is the professional membership body for UK fundraising. It has over 5,000 members and its mission is to support fundraisers, through leadership, representation, standards-setting and education. The Institute champions and promotes fundraising as a career choice.

The Charity Retail Association represents charity retailers and has nearly 400 members, covering over 8,000 shops. The CRA promotes a successful charity retail sector through promoting the benefits of charity retailing, providing expertise and guidance and sharing good practice.

Founded in 1919, NCVO is the largest representative body for charities and voluntary organisations in England. NCVO has over 11,000 members ranging from large 'household name' charities to small community organisations. NCVO's strategic aims are to champion and strengthen civil society and volunteering, and to strengthen voluntary organisations.

For more information on this response contact: policy@cfg.org.uk or Andrew O'Brien, Head of Policy and Public Affairs on 020 7871 5477.

EXECUTIVE SUMMARY

- We do not believe that there is sufficient data on the scale of business rate relief avoidance through charitable vehicles. The government should take steps to find out more information on this problem so that proportionate steps can be taken.

- Rules around business rate relief, particularly regarding what counts as use 'wholly or mainly for charitable purposes', are vague and this can lead to confusion for charities. This is compounded by the fact that these rules are often subject to change due to case law.

- **We do not believe that local authorities should be given general or specific anti-avoidance powers in relation to business rate relief for charities.**

- We do not believe that local authorities are in a position to judge whether a property is being occupied by a charity for the purposes of business rate relief. This is an issue which should be handled independently through the legal system - particularly given recent changes (The Business Rate Retention Scheme), which gives local authorities an incentive to reduce the amount claimed through business rates.

- Most charities do not have the resources to challenge decisions if local authorities decide that a charity has failed to meet an anti-avoidance test. This could lead to charities carrying out legitimate activities being deprived of their rate relief without the means to challenge decisions by local authorities.

- We recommend that the government takes a positive approach through better communication with charities about the rules of business rate relief working with the Charity Commission and membership bodies.

- We also recommend that HMRC works with the Charity Commission to set up a confidential line for charities to report individuals they suspect of seeking to use charitable vehicles to avoid tax.

General comments

Business rate relief is a crucial tax relief for charities. The relief dates back to the mid-19th Century and the principle that property being occupied for a public purpose should not be subject to tax.

Premises used by charities which receive business rate relief are used for a wide range of purposes including, but not limited to, service delivery, office functions, charity shops, storage.

Business rate relief is particularly important for charities using properties to deliver a service, where otherwise it might be too costly. The relief also ensures that more funding is devoted towards delivering services and support to those in need.

We believe that it is important that no steps are taken which could undermine the effective operation of this relief for charities and which ensures that thousands of organisations are able to carry out their work in a tax effective way.

While we appreciate that the government is seeking to reduce the amount of tax lost through fraud and error, any steps taken must be proportionate.

It is also important that any future changes to the business rate relief system are based on thorough research both into the scale of the problem and the impact that any changes could have on charities.

Charities have an interest in a robust system of business rate reliefs which are not susceptible to tax avoidance. We urge the government to work with charities to tackle avoidance where it exists rather than through legislation or introducing regulatory changes that could have unforeseen consequences.

Methods and scale of avoidance

We are unaware of any statistics that have been collected into the scale of avoidance of business rate relief through the claiming of charity specific reliefs. We believe it is important that robust data on this issue is collected before policy decisions are made. Without a clear understanding of the scale of the issue, the government is not in a position to examine which steps are proportionate in dealing with this problem.

Individuals seeking to abuse charitable rate reliefs do not inform other charities or membership bodies about the methods that they use to undertake tax avoidance schemes. It is, therefore, extremely difficult for us to provide a list of methods that could be used by individuals seeking to avoid business rate relief through charitable vehicles.

We do not, therefore, have any further methods to add to that list already provided in the discussion paper.

There have been recent cases where charities have been found not to be using buildings 'wholly or mainly for charitable purposes' and this has led to business rate relief being claimed in error (e.g., The Public Safety Charitable Trust).

This is linked to the significant confusion around what constitutes 'wholly or mainly for charitable purposes' and this can make it difficult for charities to navigate business rate relief. For the most part, decisions on this are open to significant interpretation.

We do not favour further legislative changes in this area. Regularly updated and simple to understand guidance from HMRC and the Charity Commission on claiming business rates, taking into account recent cases, would have a positive impact. It would also help to protect charities from individuals who may wish to use charities in order to avoid business rate relief.

Tackling avoidance

We are not in favour of giving local authorities a general or more specific anti-avoidance power whereby local authorities can withhold reliefs and exemptions where they reasonably conclude that the main purpose or one of the main purposes of the ratepayers' occupation or arrangements is to receive the relief or exemption, and/or that the arrangements or occupation is contrived or artificial.

We do not believe that local authorities are in a position to judge whether a property is being occupied by a charity mainly for the purposes of business rate relief. We believe that this is an issue which should be handled independently through the legal system. This is particularly important given recent changes to business rate relief through the business rate retention scheme, which gives local authorities an incentive to reduce the amount claimed through business rates.

Moreover, most charities do not have the resources to be able to challenge decisions if local authorities decide that a charity has failed to meet the 'reasonably conclude' test. This could lead to charities carrying out legitimate activities being deprived of their rate relief and without the means to challenge decisions by local authorities.

Charities carrying out a diverse range of work and often strive to find innovative ways to use property in order to meet the needs of their beneficiaries. A sweeping anti-avoidance rule would likely lead to local authorities taking a risk adverse attitude which could reduce innovation in the sector, having a negative impact on communities.

We recommend that the government takes a positive approach through better communication with charities about the rules of business rate relief working with the Charity Commission and membership bodies. As mentioned above, the business rate relief rules can be confusing for charities and honest charities can potentially be drawn into tax avoidance schemes unless they have the proper guidance and advice.

The Charity Commission has recently published guidance on charity tax reliefs which refers to business rate reliefs and we believe that the government should work with the Commission to further build on this information.

As we have no firm data on the scale of the problem, we believe that this would be a proportionate approach to take until we have a clearer sense of the scale of tax avoidance of business rates through charitable vehicles. It would also be prudent to see whether better information and guidance has the effect of significantly reducing business rate relief tax avoidance through charitable vehicles.

Increasing complexity for the claiming of business rate reliefs through regulatory or legislative change could impact on the ability of charities to move premises, set up new projects or trade through charity shops. This could have negative consequences for communities. For example, research on the impact of charity shops has indicated that they provide a number of benefits and added complexity to the business rate relief system could impact on the setting up of future charity shops.[1]

We also recommend that the HMRC sets up a confidential line for charities to report individuals they suspect of seeking to use charitable vehicles to avoid tax, working with the Charity Commission and membership bodies to promote it.

We believe that the vast majority of charities are made up of honest and law abiding people (mostly volunteers) who will report wrongdoing, provided that they know the means to do so.

Increasing awareness of potential scams and improving understand of the rules around business rate relief are the best methods available to government to reduce tax avoidance through charitable vehicles.

[1] "Giving something back", Demos, 2013
http://www.demos.co.uk/files/DEMOS_givingsomethingbackREPORT.pdf?1385343669

Appendix 3

Makro Properties Ltd v Nuneaton and Bedworth BC

Background

Makro Properties Limited (MPL) owned warehouse premises in Coventry. Up until 1 June 2009 the property was occupied by Makro Self-Service Wholesalers Limited (MSSWL) a subsidiary company and part of the Makro Group. The property was empty between 1 June 2009 and 25 November 2009, when 16 pallets of MSSWL paperwork was moved into the premises and stored there. The storage lasted until 12 January 2010 (a period of just over six weeks) and accounted for usage of 0.2% of the total of 13,000sqf of space in the property. The property was then empty again between 12 January 2010 and 23 July 2010 when further pallets of documents were moved in. It was MSSWL's position that the nature of the documents were such that they were bound by law to retain them. It was MPL's intention to sell the property within the six month empty period and failing that to reoccupy for a further period of six weeks.

Magistrates' Court decision

The district judge took the view that partial occupation still attracts liability for business rates. From case law it would be wrong to conclude that the de minimis principle does not apply. There must come a point when the local authority can say usage is so miniscule so as not amount to rateable occupation. When determining which side of the line this case fell on, it was determined that at 0.2% of floor space usage the council was justified in deciding that the occupation was de minimis. The district judge also held that the occupation was not beneficial just because it was mandatory for the papers concerned to be stored by MSSWL. The only benefit in this scenario was the avoidance of business rates for MPL and applying the rationale in *Furniss v Dawson* there was no commercial purpose to the occupation and it ought to be disregarded. The council were therefore entitled to a liability order for the period in question, as MPL were not entitled to a further six month rate free period following the occupation in November 2009.

Appeal Decision

Following a review of the statutory provisions relating to rates payable on occupied and unoccupied premises, Jarman HJ conducted his assessment of the essential factors of occupation set out in *Laing v Kingswood Assessment Area Assessment Committee* [1949].

- Actual occupation

It was accepted that "slight usage" can be sufficient to attract rating liability. The intention of the parties was considered, in the light of *R v Melladew* [1907] in which the court formed the view that the intention of the alleged occupier in respect of the hereditament was a governing factor in determining the question of whether rateable occupation had been established. Although it was argued by the council that the intention in this case was to avoid liability of rates for a longer period, this was rejected by the court which found that there was an intention to occupy and not just to give a *semblance* of occupation.

It had been accepted in the original case that there was occupation, albeit miniscule, and Jarman LJ identified the real question as being whether the judge in that case was right to go on and find that the de minimis principle applied, such that occupation could not amount to actual occupation. The proper approach was to consider both use and intention. "If there is clear evidence or inference of an intention to occupy, such an intention taken together with the use, albeit slight, may be sufficient to amount to occupation as determined in Melladew. Slight use without such evidence of intention

may not be sufficient". Jarman LJ found that the storage of 16 pallets of documents, required by law, could not be said to be trifling.

– Beneficial occupation

Jarman LJ found that the possibility that the landlord might reduce its rates bill was not the only benefit but also the fact that the documentation was of value as MSSWL was bound by law to retain it. The court found therefore that the occupation was beneficial to the occupier.

– Exclusive occupation

The court looked at the degree of control exercised by the landlord, it being accepted by the parties that this is an important factor when considering occupation (as per *Westminster City Council and Kent Valuation Committee v Southern Railway Company* [1936]). In this respect, the judge preferred the view that even if MSSWL were occupying at MPL's pleasure then so long as that occupation continued the occupation was that of MSSWL and not of MPL. Although it was acknowledged that if the property was not sold within the six month period, there was a plan to reoccupy for a further period of six weeks, this event did not amount to a present intention as to occupation and was no more than an intention to occupy on the happening of a future uncertain event.

Finally Jarman LJ, when faced with the submission that the outcome of the case meant that a scheme to avoid paying rates for six months had succeeded, commented that rate payers can do and organise their affairs so as to avoid paying rates and stated that the court is not a court of morals but of law. If that outcome was seen as unacceptable then it was for Parliament to determine whether further reform was needed. In other words, it must have been anticipated by Parliament that the scenario which arose in this case must have been foreseen when the reforms were made in 2008.

Comment

The case will be viewed as a setback for local authorities. It has been estimated that a landlord stuck with an empty property can now use this method to reduce the annual rates bill by up to 80%. This could of course have a much bigger impact on authorities from April 2013 when those uncollected rates will come directly off their annual budget.

The case raises interesting questions, considered by local authorities up and down the country, about the difference between rates avoidance (legal) and rates evasion (illegal).

As was clearly demonstrated in the Makro Properties case, when faced with an assertion by a local authority that a particular scenario has been set up with the specific purpose of avoiding rates, the court will go "back to basics" with a literal interpretation of the statutes together with consideration of the four factors in *Laing v Kingswood*.

There is of course nothing in the regulations that prevents a rate payer from repeatedly occupying for six week periods, as long as it can be shown that that occupation is actual, beneficial, exclusive and not too transient.

Councils are now likely to be faced with similar schemes being used by landlords who may wrongly assume that the case gives them carte blanche to put some boxes in a large building and claim occupation. In the Makro case, the judge gave weight to the fact that the documents were legally required to be kept. Other benefits may be factors such as reducing storage costs or freeing up space which can otherwise be used constructively by the company.

The fact that rent may not be charged may not be determinative, given that there are plenty of scenarios in which a tenant can obtain a rent free period in respect of any building or nominal rent of £1. In the recent case of *Re Coll (Valuation Officer) [2012] UKUT5 (LC)* HHJ Mole QC held that "The hypothetical negotiation is between a landlord who has a property he wishes to let and a hypothetical tenant who wishes to occupy it. The personal motives of real landlords and tenants have nothing at all to do with the valuation of the hereditament. It makes no difference that the occupier will not make money out of occupying it."

Similarly it will not matter that the occupation is pursuant to the terms of a lease, licence or tenancy at will. As long as the parties can demonstrate that it was genuinely undertaken for the purpose of creating an interest in land, the court will be reluctant to go behind the document.

It will be important to insist that authorities are notified on each period of occupation to enable inspection. Without this type of evidence, it will be very difficult to make a judgment call on the nature of the occupation.

It is also useful to bear in mind the exception under Section 65(5) under LGFA 1988 in that plant, machinery and equipment that was used or is intended for use should be ignored for the purposes of occupation. This will include shop fittings, counters and shelves, and may include desks and chairs.

Councils will also be familiar with schemes by which occupation is by way of a small electronic device, which purports to broadcast messages via Bluetooth. Again the council must consider whether there is beneficial use of the occupation. If the landlord is paying for the messages that are broadcast, then this may be a relevant factor. It is not necessarily the size of the equipment that determines whether a benefit is being obtained. If the only benefit is seen as the landlord avoiding empty rates, then that ought not to be viewed as beneficial. Similarly where the device is simply used to broadcast "to let" advertisements this should not be viewed as beneficial.