



Prime Minister

HARMONISATION OF RATING: THE CONTRACTORS BASIS

At 11:10 PM 10
In my minute of 28 June, I said I would be putting specific proposals to colleagues on two issues, one of which was the rating of those specialist properties where, in the absence of rental evidence, the "contractors basis" of valuation is used.

The "contractors basis" is particularly used for the steel and ship building industries, the oil and petrol chemical industries, much of local government and many Crown occupations. It seeks to estimate a rental value for a property by establishing its effective capital value and taking a percentage of that - the "decapitalisation rate" - as the amount a tenant would be prepared to pay in rent. At present, the decision whether to use the contractors basis, and the way it is applied, together with the decapitalisation rate, are all matters which are left entirely to the discretion of valuers. Practices, especially over the decapitalisation rate have differed as between England and Wales and Scotland. The rate in England and Wales is presently 5% - based on 1973 interest rates - while in Scotland the rate was originally set at 8% in 1985 but has been reduced to 7% on appeal. These differences of approach mean that the levels of assessment for equivalent installations are widely different in the different countries.

In 1990, however, England, Wales and Scotland will have valuations by reference to the same valuation date and there will be no grounds for different decapitalisation rates to apply in the different parts of Great Britain. Malcolm Rifkind and I, therefore, have taken powers in the Local Government Finance Act which permit us to prescribe the same decapitalisation rates. We must now decide whether to exercise these powers and, if so, at what level to set the percentage.



I am advised that the Chief Valuer's office believe that a rate of 7% will be appropriate and that this view is likely to be shared by the Scottish assessors. In principle, therefore, harmonisation at that level is possible without our intervention. However, a decapitalisation rate at that level would be fiercely resisted by the industries concerned. The nature of the method is such that an increase in decapitalisation rate from 5% to 7% on its own would increase rate bills by 40% and the industries have made detailed recommendations to us that 5% remains the appropriate percentage figure. The attached table, which is derived from a desk exercise carried out by the Valuation Office shows the factor by which rateable values might be expected to increase for particular types of property at different rates. I am confident that without prescription increases of the magnitude implied by a 7% rate would lead to the most strenuous series of appeal hearings with the risk that different decisions would be taken north and south of the border so undermining the harmonisation process.

In my view the advantages of prescribing the rate in terms of stability and certainty as well as increased harmonisation outweigh the disadvantages, the main one of which is that the Government would take responsibility for this decision rather than leaving the matter to be resolved in the appeal system. We would therefore become the focus for complaints by businesses.

There is not, however, a single decapitalisation rate. At present separate and lower rates are set for local authority occupations at 3.75% in England and for educational charitable occupations at 2½%. In theory these different rates reflect differences in the rate of interest payable by those classes of occupier. In practice I can see little justification for rating a property less highly simply because it is occupied by a local authority. And, as we begin to blur the boundary between the public and private sector continuing a differential will be anomalous in many cases and undermine competition.



I therefore propose that we should have a single decapitalisation rate which will apply to all businesses, valued in this way, and to the generality of local authority properties (but excluding schools see below). There is no hard and fast method for determining the appropriate percentage. My view is that the rate increases implied by a 7% rate, particularly in steel and shipbuilding look implausibly high. The inclusion of some public sector property in the overall judgement too would suggest a lower average rate. On balance I favour a 6% rate though even that may lead to strong representations from industry.

There is slightly more justification for a lower rate for educational charities to the extent that they are not entirely dependent on borrowing when providing new buildings. This category includes the Universities and the public schools but presently excludes local authority schools and the Polytechnics. Our proposals for the future management of the Polytechnics, and the development of Grant Maintained Schools mean that we need to reconsider the arrangements here. I think we must maintain a lower band, which I believe should be set at 4% and to apply it to all educational institutions. This will ensure a uniform treatment for public schools, Grant Maintained Schools and local authority schools and for Universities and Polytechnics.

The net effect of these decisions would be to increase the rate bills payable by local authorities by about £70m which is equivalent to less than a £2 addition to the community charge. There would also be an increase in the rateable values of public schools. Some of that increase is an inevitable part of the revaluation. It should anyway be more than offset by the increase to 80% in the derating for all charities which we were forced to agree to in the House of Lords. And, to the extent that there are any increases to be dealt with they will of course benefit from the transitional arrangements which will apply to all business ratepayers.



If colleagues agree to these proposals there may be implications for the contributions in aid of rates payable on Crown Properties though any prescribed rate will not apply directly. Officials will need to discuss the implications for the level of the business rate poundage and revenue support grant in due course.

I am copying this minute to the other members of E(LF) and to Sir Robin Butler.

A handwritten signature, appearing to be 'NR', written in dark ink.

N R

5 October 1988

ILLUSTRATIVE UPLIFT FOR 1990 IN RATEABLE VALUES OF PROPERTIES VALUED ON THE CONTRACTORS BASIS, AT DIFFERENT DECAPITALISATION RATES

	<u>Current Rate</u>			
	3.75%/2½%	5%	6%	7%
Specialist Industrial		6.9	8.4	9.8
Oil & Chemical		6.4	7.7	9.0
Heavy Industry		7.5	9.0	10.5
Airports/Conference Centres etc		10.1	12.1	14.1
Local authority: general	8.2	10.6	12.7	14.9
Local authority: schools	7.2	9.6	11.6	13.5
Crown Property	8.7	11.6	14.0	16.3
Educational (Public schools & Universities) (2½%)	8.4	11.3	13.5	15.8

Notes

The average uplift in all non-domestic rateable values arrived at by all methods for all types of property is estimated to be around 7 fold.



LOCAL GOVT

RATES

PT II