



10 DOWNING STREET

file K6

cc Olive Letwin

From the Principal Private Secretary

9 May 1985

Dear Tony,

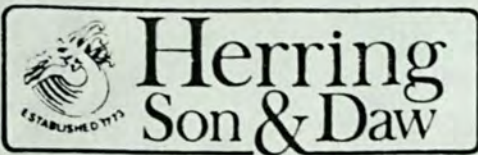
The attached document, which is self-explanatory, has been sent to me by a personal friend who is the Senior Director of Herring Son & Daw. I am passing it on to you in case it may be of interest. I have also given a copy to Oliver Letwin in our Policy Unit here.

Please let me know if you feel that the Herring Son & Daw calculations of the effects on a property tax based on rental value of non-domestic property, with a single centrally set rate in the pound, would be of sufficient interest to ask them to set their computer to work to produce the figures.

Yours ever,

Robin Butler

R. A. J. Mayer, Esq.,
Local Government Finance Policy,
Department of the Environment.



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cc Oliver Letwin

8th May, 1985.

Dear Robin,

I asked you after our recent Harrow GPC Meeting about the continuing interest of the Prime Minister's Office in the problems of non-domestic rates. I understood from you then that you felt that there would be considerable interest in the results of research that we have done, in order to attempt to analyse the results on rates payable for commercial properties if there were to be a revaluation for rating purposes. I am, therefore, sending you a copy of the Report, drawn up by Christopher Hedley who heads our research capability, written on the assumption that a revaluation had just been announced.

I have added to this a brief summary of my own covering in note form the main effects of such a revaluation and some alternatives recently mooted in the press.

You did suggest that it would also be of interest for a copy of this to go to William Waldegrave at the Department of the Environment. Although he speaks for Grey Gowrie on arts matters in the Commons, I have not come across him wearing my ABSA hat, and I wonder if you would be kind enough to pass on the extra copy that I attach, either to him or to whoever you feel is the right person in that department.

You will see that I have mentioned in my notes the possibility of a property tax based on rental value of non-domestic property, but with a single centrally set rate in the pound. If you feel that it would be useful to you to re-do the calculations for that assumption, then I think we could do that given reasonable notice, and assuming that the computer model can in effect be made to work in reverse.

Yours sincerely,

N.A.S. OWEN

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NON-DOMESTIC RATES

There are two distinct defects with the operation of the non-domestic rating system at the moment:-

- A. The proportion of rental value paid in rates varies excessively between types of property.
- B. Rates do not provide a sufficiently large tax base, without supporting grant, to fund high spending authorities without penalising business.

Herring Son and Daw's report of April 1985 seeks to show how a revaluation would alleviate the unfairness between types of property. We summarise the results below and comment on various suggested changes.

1. The Relationship between Rates and Value

- Rates paid now vary between 15% of rental value for some prime shops and over 100% of rental value for some office and many older factories.
- Rates now act as a harsh tax on factories, older properties and the less prosperous regions and a relative concession to town centre shops.
- Rates on non-domestic property will raise almost £9 billion pounds in 1985/6.
- Rates, after some time lag, act as a tax on landlords, discouraging investment and development of factories and in the regions.

2. The effects of a Revaluation

- The disparity in rates paid between regions would be reduced.
- Rates paid on factories would be reduced.
- Development of factories, and even offices, by the private sector would accelerate in the regions, reducing the need for public subsidy.
- The combined rent and rates bill of many multiple shops (and some offices in the South-East) would increase by about 10%. This would gradually work through to fall on landlords and ultimately reduce central area land values.
- The rate poundage charged by different authorities would cover a narrower band than at present.
- There would be no change in the total tax raised.

3. A Standard Rate in the Pound

- A national rate poundage would only be equitable if combined with regular revaluation.
- It would exaggerate most of the changes shown for a standard revaluation, assuming the total tax to be raised remained at £9 billion.
- It would require a tax rate of under 50p. in each pound of rental value, to raise £9 billion, or less than one third of the annual value in rent and rates combined.
- It could be set at a lower rate if it was politically prudent to do so.
- It could be adjusted annually according to an accepted index or as a result of budget policy.
- It would be a tax on the annual value of property and thus ultimately paid by landlords.
- Rate support grant will still be needed.

4. Rates as a Tax Base

- The tax base for non-domestic rates varies between different taxing authorities by reason of the quantity and value of such property within the relevant area.
- It bears little relationship to the resident population of the area or the cost of local services.
- Non-domestic rates are a tax that fulfils the criteria of being visible and easy to collect, but vary unpredictably from year to year and carry no real vote, either in a corporate sense or because the employee necessarily lives in the voting area of the place of business.
- The tax base is large and important as a national source of income.
- Rates will never be a truly local tax because rate support grant or other adjustment will always be needed.

Other Business Taxes

In order to replace non-domestic rates with a non property-based business tax, it would be necessary to increase one of the existing taxes as follows or by some combination of these and other taxes:-

National Insurance	- 37%
VAT	- 49%
Corporation Tax	- 89%

Any of these taxes would be either difficult to determine locally and liable to create local distortions in competition. They would also run counter to recent changes in Government taxation policy.

In no case would the local tax base match accurately the revenue needs of the local authority.

A redistribution formula would still be needed.

Conclusions

Without a satisfactory re-distribution formula there can be no satisfactory local business tax.

Non-domestic property provides a large tax base which is difficult to replace.

Subject to a satisfactory re-distribution formula rates are a fair and sensible tax which might be improved with a standard rate poundage.

If property is to continue to be a tax base regular revaluation must be included in the reforms.

Nicholas Owen
Herring Son & Daw

May, 1985.