

# ***‘Non-Domestic Rates: 2005 Revaluation Transitional Arrangements - A Consultation Paper***

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## **Introduction**

1. Under existing legislation, the Scottish Assessors are required to re-value all non-domestic subjects in Scotland every five years. This ensures that rate bills reflect an up to date assessment of market rental values and that the distribution of the rates burden between ratepayers remains equitable. The next revaluation is due to take place on 1 April 2005.

2. The total amount of tax paid by non-domestic ratepayers will not change in real terms following the 2005 Revaluation but for non domestic ratepayers whose rateable values increase by more than the Scottish average this will result in these ratepayers facing real increases in their rates bills. The aim of transitional arrangements is to protect such ratepayers from sudden sharp increases in their bills in the period immediately following the revaluation. This allows ratepayers time to plan to accommodate the true bill over a longer period.

3. This paper seeks comments on: whether transitional arrangements need to be put in place following the 2005 Revaluation; some options for potential transitional schemes; the form a transitional scheme could take. This consultation paper applies to Scotland only. Responsibility for rating matters in England and Wales rests with the Office of the Deputy Prime Minister and the Welsh Assembly Government respectively.

## **Sending us your views:**

4. We invite responses by **Wednesday 22 September** 2004. E-mail responses should be sent to: [TA2005.consultation@scotland.gsi.gov.uk](mailto:TA2005.consultation@scotland.gsi.gov.uk) and paper responses to: Stuart Blackie, Transitional Arrangements Consultation, Local Government Constitution and Funding Division, Area 3J (North), Victoria Quay, Edinburgh, EH6 6QQ.

5. If you would like to access this consultation paper online, then please go to <http://www.scotland.gov.uk/view/views.asp>. Further copies of this paper can be obtained by post from Stuart Blackie, Transitional Arrangements Consultation, Local Government Constitution and Funding Division Area 3J (North), Victoria Quay, Edinburgh, EH6 6QQ or by e-mail from [TA2005.consultation@scotland.gsi.gov.uk](mailto:TA2005.consultation@scotland.gsi.gov.uk) .

6. We would be grateful if you can clearly indicate in your response which questions or parts of the consultation paper you are responding to as this will aid our analysis of responses received. We will make all responses available to the public in the Scottish Executive Library at Saughton House, Edinburgh, EH11 3XD, (telephone 0131 244 4552) by **Wednesday 13 October 2004** unless confidentiality is requested. All responses not marked confidential will be checked for any potentially defamatory material before being logged in the library. Confidential responses will nevertheless be included in any statistical summary of the number of responses received and views expressed.

## Background

7. Transitional arrangements, in some form or other, have been a feature of the rating system in Scotland for some time. At the 1985 Revaluation – when dwelling houses were subject to rates – provision was made<sup>1</sup> to limit large increases in rateable values by setting limits on the increases in rateable values in the first years of the revaluation, thus delaying by stages the introduction of the full effect of the increased valuations. The Abolition of Domestic Rates Etc. (Scotland) Act 1987 provided that with effect from 1 April 1989, all the existing entries in the valuation roll for domestic subjects were to be deleted and thereafter domestic subjects were not to be entered in the valuation roll.

8. By the time of the 1990 Revaluation, control of non domestic rates had returned to central government. Transitional arrangements were put in place for the 1990<sup>2</sup> and 1995<sup>3</sup> Revaluations. For the 1990 and 1995 revaluations provisions were introduced which phased in increases and decreases in rateable values. Under the 1990 and 1995 transitional arrangements, some ratepayers were still not paying their true rates bill for the subjects they occupied by 31 March 1995 and 31 March 2000 respectively - even although they might have been able to afford to do so.

9. By the time of the 2000 Revaluation, responsibility for business rates policy in Scotland had been devolved to the Scottish Parliament. On 8 December 1999, the then Finance Minister said during a statement to the Scottish Parliament that there would be a Scottish transitional relief scheme. The 2000<sup>4</sup> transitional scheme was specifically designed so that all ratepayers would be paying their true rates bill within the quinquennium.

10. The 2000 transitional scheme aimed to combine simplicity with tight initial protection for those faced with significant real increases in bills. In the year immediately following the 2000 Revaluation (2000-01) increases in rates bills were limited to 5 per cent in real terms for small subjects (i.e. those with a rateable value of £10,000 or less) and 7.5 per cent in real terms for all other subjects. To fund the transitional protection decreases in rates bills were limited to 5 per cent in real terms for all subjects.

11. If a ratepayer occupied a subject whose real increase/decrease in true bill was less than these limits then these ratepayers paid their true bill from 2000-01. If a ratepayer would otherwise have received an increase or decrease in their rates bill in excess of the limits referred to above then the ratepayer would have seen an “adjustment” being made to their rates bill in 2000-01<sup>5</sup>. These “adjustments” were phased out in equal steps between 2001-02 to 2003-04<sup>6</sup> so that by 2004-05 all non domestic ratepayers in Scotland were paying their true rates bill.

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<sup>1</sup> Rating (Revaluation Rebates) (Scotland) Act 1985 (c.33).

<sup>2</sup> The Non-Domestic Rates (Levying) (Scotland) Regulations 1990/788 followed by SI 1991/645, SI 1992/642, SI 1993/234

<sup>3</sup> The Non-Domestic Rates (Levying) (Scotland) Regulations 1995/548 followed by SI 1996/103, SI 1997/452, SI 1998/519 & SI 1999/276

<sup>4</sup> The Non Domestic Rates (Levying) (Scotland) Regulations 2000/92, SSI 2001/71, SSI 2002/91 & SSI 2003/160.

<sup>5</sup> Non Domestic Rates Revaluation 2000 Transitional Arrangements <http://www.scotland.gov.uk/library2/doc14/lgl3-00.asp>

<sup>6</sup> NDR Transitional Arrangements 2001-02, 2002-03 & 2003-04 <http://www.scotland.gov.uk/library3/enterprise/ndrta-00.asp> <http://www.scotland.gov.uk/library3/government/ndrl-00.asp> <http://www.scotland.gov.uk/library5/finance/ndrl-00.asp>

## **Effect of the 2005 Revaluation**

12. The Scottish Executive has set the key aims of the 2005 Revaluation as stability, certainty for non domestic ratepayers and continued harmonisation of valuation treatment and practice north and south of the border. Under the terms of the current Partnership Agreement, the Scottish Ministers have said that rate increases will be limited to no more than the rate of inflation for 2005-06.

13. The Revaluation will have different effects on different regions of the country, and different types of property, reflecting regional and sectoral trends in property costs. Revaluations work by transferring rates liabilities to those subjects where rateable values have risen by more than the average change in rental value for the country as a whole. Therefore if the value of a particular property rises by more than the average, the rates liability will rise; otherwise the liability will fall. A property can therefore show an increase in rateable value and still have a reduction in rates liability following a revaluation.

## **Transitional arrangements and the 2005 Revaluation**

14. It has been argued that after a revaluation it can be difficult for ratepayers, especially small businesses, to accommodate immediately what might be a significant increase in operating costs. Implementing transitional arrangements which phase in significant increases in rates bills over a period of time would benefit ratepayers in all parts of Scotland whose rates bills increase significantly following the revaluation.

15. The currently prescribed industries<sup>7</sup> will be valued on a conventional basis at the next revaluation. It is over 50 years since these industries have been valued in this way and it is not yet clear what impact this may have on rateable values. Representatives from some of the currently prescribed industries have indicated that should rateable values of the subjects they occupy increase significantly at the Revaluation then they would wish transitional arrangements to be put in place to help them adjust to changes in operating costs.

16. It could equally be argued that the existence of transitional arrangements dilutes the overall premise that a fair valuation gives a fair rates charge. The point could also be made that the Scottish Executive's Small Business Rate Relief Scheme – which, since 1 April 2003, has provided between a 5 per cent and 50 per cent discount on the poundage rate for qualifying subjects – goes some way towards ameliorating the rates costs faced by small firms thus reducing the need for transitional arrangements.

17. Subjects change over the lifetime of a valuation roll and entries in the roll need to be amended due to physical and other changes to the subject. As any transitional arrangements would require to interact with these changes (e.g. a subject moves from being occupied to unoccupied) it has been argued that this can make the calculation of the rates liability complex and difficult for ratepayers to understand. In the same vein, transitional relief is only one of a number of rate reliefs/allowances now available to qualifying subjects. It can be difficult for ratepayers to fully comprehend how the various rate reliefs/allowances interact with each other.

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<sup>7</sup> Electricity generation/distribution/transmission, Docks and Harbours (large), Railways, Train Operating Companies, Gas & Scottish Water

18. Although the 2005 Revaluation Factor<sup>8</sup> for Scotland is not yet known, we would nevertheless welcome views on the general issue of the need for transitional arrangements to be implemented for the 2005 Revaluation.

### **Q1. Should transitional arrangements be put in place at the 2005 Revaluation?**

#### **Key Principles**

19. In designing any transitional scheme for the 2005 Revaluation, the Scottish Executive will be guided by 3 key principles:

- **simplicity** – it should be easy for ratepayers to understand, and for local authorities to administer;
- **time limited** – it should come to an end before the next valuation roll takes effect in April 2010, so that we obtain the transparency of every ratepayer paying their “true” rates bill within the quinquennium; and
- **cost** – it should be self financing. This is in line with the aims of the 2000 Revaluation transitional arrangements.

#### **Potential Transitional Schemes**

20. If there is to be a transitional scheme at the 2005 Revaluation, then this paper outlines two potential options and seeks views on a number of issues related to these options. Option 1 proposes that a limit is put on real increases/decreases in rates bills between 2004-05 and 2005-06 and that the “true” rates bills would be phased in, in equal steps, in subsequent years. Option 2 proposes that reductions in rates bills are implemented immediately and that the cost of any transitional protection would be funded by an adjustment to the poundage rate.

21. However, the Scottish Executive is also keen to hear the views of businesses and rating professionals on the form a transition scheme could take whilst taking due cognizance of the key principles set out at paragraph 19 above.

#### ***Option 1***

22. It would be possible to introduce a scheme which provided tight initial protection for those faced with significant real increases in bills by limiting increases in bills in the year following the revaluation to a set percentage. For those subjects whose bills were limited in this way the “true” bill would be phased in, in equal steps so that all subjects would be paying their full rates bill by the end of the quinquennium. The cost of providing this transitional protection would require a limit to be set on the real decrease in bills of those subjects whose true bill will fall following the revaluation. For those subjects whose bills were limited in this way, the true bill would require to be phased in at the same rate as those receiving transitional protection.

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<sup>8</sup> Revaluation Factor is the average amount that rateable values in Scotland will increase as a result of the 2005 Revaluation

23. Within the general framework of the scheme outlined above there are a number of key parameters which might be varied whilst ensuring the scheme remains self financing.

*Level of initial protection to be provided*

24. Two issues to be considered here. A scheme could be introduced which limits the real increases in bills between 2004-05 and 2005-06 of smaller subjects (those with a rateable value of £10,000 or less) at a lower level than that set for all other subjects. For example, the transitional arrangements introduced at the 2000 Revaluation limited the real increases in bills for smaller subjects to 5 per cent and of all other subjects to 7.5 per cent in real terms. However, as discussed above it could be argued that the introduction of a Small Business Rate Relief Scheme obviates the need to set a lower limit for small businesses.

25. The second issue to be considered is at what level should the limits in real increases in bills between 2004-05 and 2005-06 be set e.g. 5 per cent, 10 per cent etc. The wider the initial limits are set (with correspondingly wider limits to the real reductions in bills necessary to finance the scheme) then the fewer subjects would be affected by the transitional arrangements. However, wider limits would provide businesses with less protection against the initial impact of the revaluation.

**Q2. Should the limit on real increases in bills between 2004-05 and 2005-06 be set at a different level for smaller subjects (those with a rateable value of £10,000 or less)?**

**Q3. If you consider that there should be two limits set for real increases in bills between 2004-05 and 2005-06 then what do you consider appropriate limits to be?**

**Q4. If you consider there should only be one limit set for real increases in bills between 2004-05 and 2005-06 for all subjects what do you consider an appropriate limit to be?**

*The speed of phasing in the true bill*

26. Any transitional arrangements which may be introduced as a result of the 2005 Revaluation will require to unwind before the end of the quinquennium. As with the 2000 transitional arrangements the true rates bill could be phased in over a four year period so that all subjects are paying their true rates bill by 2009-10. It could be argued that there would be some merit in phasing out transitional protection over a shorter timeframe as those in receipt of transitional protection have had sufficient time to adjust to their new bill, and it is “unfair” to those ratepayers funding the scheme to delay the phasing in of their true rates bills longer than is strictly necessary.

**Q5. Views are sought on the period over which transitional protection should be phased out and the true bill phased in.**

***Option 2***

27. It has been argued that funding transitional protection by limiting the real decrease in bills of those ratepayers whose true bill will fall, following the revaluation and then phasing the true bill in at the same rate as those receiving transitional protection is unfair. The point is

made that these are occupiers whose rates liabilities have fallen as a result of lower demand for the property, due in many cases, to a reduced ability to pay higher rents.

28. It would be possible to design a self funding scheme which allows reductions in rates bills to be implemented immediately. The cost of any transitional protection – such as that discussed under Option 1 above - could be funded by an adjustment to the poundage rate. The adjustment to the poundage rate could work in a number of ways. The same adjustment could be made to the poundage rate in each year of the scheme, or a year to year adjustment could be made which would change in accordance with the cost of transition in that year. This would spread the cost of providing transitional protection across a wider group of ratepayers.

**Q6. Would you be in favour of an adjustment being made to the poundage rate to cover the cost of providing transitional protection?**

**Q7. Do you have a preference between the schemes outlined at Option 1 and Option 2?**

### **Next Steps**

29. A broad outline of next steps is given below:

- An analysis of responses received will be published on the Scottish Executive website by **Friday 5 November 2004**.
- Over the summer months once data are to hand on the revaluation some modelling of the options for transitional schemes can be undertaken. This information will be fed into the decision making process.
- In reaching a decision on (a) whether transitional arrangements will be put in place for the 2005 Revaluation and (b) what form these arrangements will take, Ministers will carefully consider the responses received to this paper along with information fed in from the modelling exercise.
- Ministers will announce their decision in November 2004.

### **Summary of questions on which views are sought**

**Q1. Do you consider transitional arrangements should be put in place at the 2005 Revaluation? (paragraphs 14-18)**

**Q2. Should the limit on real increases in bills between 2004-05 and 2005-06 be set at a different level for smaller subjects (those with a rateable value of £10,000 or less)? (paragraphs 20-25)**

**Q3. If you consider that there should be two limits set for real increases in bills between 2004-05 and 2005-06 then what do you consider appropriate limits to be? (paragraphs 20-25)**

- Q4. If you consider there should only be one limit set for real increases in bills between 2004-05 and 2005-06 for all subjects what do you consider an appropriate limit to be? (paragraphs 20-25)**
- Q5. Views are sought on the period over which transitional protection should be phased out and the true bill phased in. (paragraph 26)**
- Q6. Would you be in favour of an adjustment being made to the poundage rate to cover the cost of providing transitional protection? (paragraphs 27-28)**
- Q7. Do you have a preference between the schemes outlined at Option 1 and Option 2? (paragraphs 20-28)**

## The Scottish Executive Consultation Process

Consultation is an essential and important aspect of Scottish Executive working methods. Given the wide-ranging areas of work of the Scottish Executive, there are many varied types of consultation. However, in general Scottish Executive consultation exercises aim to provide opportunities for all those who wish to express their opinions on a proposed area of work to do so in ways which will inform and enhance that work.

While details of particular circumstances described in a response to a consultation exercise may usefully inform the policy process, consultation exercises cannot address individual concerns and comments, which should be directed to the relevant public body. Consultation exercises may involve seeking views in a number of different ways, such as public meetings, focus groups or questionnaire exercises.

Typically, Scottish Executive consultations involve a written paper inviting answers to specific questions or more general views about the material presented. Written papers are distributed to organisations and individuals with an interest in the area of consultation, and they are also placed on the Scottish Executive web site enabling a wider audience to access the paper and submit their responses<sup>9</sup>. Copies of all the responses received to consultation exercises (except those where the individual or organisation requested confidentiality) are placed in the Scottish Executive library at Saughton House, Edinburgh (K Spur, Saughton House, Broomhouse Drive, Edinburgh, EH11 3XD, telephone 0131 244 4552).

The views and suggestions detailed in consultation responses are analysed and used as part of the decision making process. Depending on the nature of the consultation exercise the responses received may:

- indicate the need for policy development or review;
- inform the development of a particular policy;
- help decisions to be made between alternative policy proposals;
- be used to finalise legislation before it is implemented;

If you have any comment about how this consultation exercise has been conducted, please send them to:

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Area 3 J (North)  
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EH6 6QQ

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<sup>9</sup> [www.scotland.gov.uk/view/views.asp](http://www.scotland.gov.uk/view/views.asp)

# **PARTIAL REGULATORY IMPACT ASSESSMENT (2004/11)**

## **Non-Domestic Rates: 2005 Revaluation Transitional Arrangements - A Consultation Paper**

### **1. Purpose and intended effect**

Occupiers of non-domestic subjects (property) in Scotland pay non-domestic rates. Non domestic rates are levied on the basis of a national poundage rate – set annually by the Scottish Ministers - multiplied by the rateable value of each non-domestic subject in the valuation roll. The rateable values for non-domestic subjects are set by the Scottish Assessors. The rateable value is an Assessor's estimate of the annual rent which a subject would command on the open market.

Under existing legislation, the Scottish Assessors are required to re-value all non-domestic subjects in Scotland every five years. This ensures that rate bills reflect an up to date assessment of market rental values and that the distribution of the rates burden between ratepayers remains equitable. The next revaluation is due to take place on 1 April 2005. Since rental evidence needs to be collected around a point in time the official valuation date (called the tone date), is set 2 years before the implementation date for the revaluation. The tone date for the 2005 Revaluation is therefore 1 April 2003.

The total amount of tax paid by non-domestic ratepayers will not change in real terms following the 2005 Revaluation but for non domestic ratepayers whose rateable values increase by more than the Scottish average this will result in these ratepayers facing real increases in their rates bills. The aim of transitional arrangements is to protect such ratepayers from sudden sharp increases in their bills in the period immediately following the revaluation. This allows ratepayers time to plan to accommodate the true bill over a longer period.

### **2. Risk Assessment**

To enable the Scottish Executive to provide ratepayers with earlier notification of likely changes to their rates bills following the 2005 Revaluation, the Scottish Executive requires to consult on transitional arrangements at an earlier stage in the revaluation process than at previous revaluations. It is too early, at this time, to say what the likely movements in rateable values will be at the 2005 Revaluation and therefore what the Revaluation Factor for Scotland will be. The Revaluation Factor is the average amount that rateable values in Scotland will increase as a result of the 2005 Revaluation.

If the average amount that rateable values increase as a result of the 2005 Revaluation is a significant figure then some ratepayers will face a sudden and significant increase in their rates bill on 1 April 2005. This could impact on the financial health of some businesses unless they are given time to adjust to higher rates bills.

### **3. Options**

There are essentially two options:

- Option 1: introduce transitional protection which phases in real changes in rates bills brought about by the revaluation.
- Option 2: do not introduce transitional protection.

#### 4. Costs

##### **Option 1: Introduce Transitional Protection**

The consultation paper outlines two proposals for funding the cost of providing transitional protection.

One proposal is that a limit would be set on the real decrease in bills of those subjects whose true bill will fall during the revaluation. In addition to which, the true bill would require to be phased in at the same rate as those receiving transitional protection.

The second proposal would allow reductions in rates bills to be implemented immediately (subject to the poundage adjustment). The cost of any transitional protection would be funded by an adjustment to the poundage rate. This would spread the cost of providing transitional protection across a wider group of ratepayers.

##### **Option 2: Do not introduce transitional protection**

For those non-domestic ratepayers whose rateable values increase by more than the Scottish average this will result in these ratepayers facing real increases in their rates bills. Without any transitional protection in place then these ratepayers will have no time to plan to accommodate their increased rates bill. The worst case scenario for those ratepayers who face a significant increase in operating costs is that it may lead to them having to rationalize their business operations.

#### 5. Benefits

##### **Option 1: Introduce Transitional Protection**

The existence of transitional protection will give ratepayers facing significant increases in their rates bills time to plan to accommodate the increase.

##### **Option 2: Do not introduce transitional protection**

It has been argued that the existence of transitional arrangements dilutes the overall premise that a fair valuation gives a fair rates charge. If no transitional protection was in place then all ratepayers would be paying their true rates bill with effect from 2005-06. Transitional arrangements can make the calculation of the rates liability complex and difficult for ratepayers to understand.

#### 6. Compliance costs

It is not possible to say at this point in time as the costs will depend on (a) if transitional arrangements are put in place at the 2005 Revaluation and (b) what the details of the final

transitional scheme are. However, any scheme would reduce rates bills for businesses facing the largest increases. For those businesses with large bill decreases, the final scheme may involve smaller decreases and so higher bills than if there were no scheme, but bills would still be lower than before the 2005 Revaluation.

## 7. Enforcement and sanctions

Non-domestic rates are collected and enforced by the 32 local authorities in Scotland. There is no evidence to suggest that collection rates have been affected by introducing transitional arrangements at the 1990, 1995 and 2000 Revaluations.

## 8. Impact on Small & Macro Businesses

All business sectors – apart from those occupying agricultural lands and buildings which are currently exempt from rating – will be affected if transitional arrangements are put in place at the 2005 Revaluation.

Generally rates bills represent a higher proportion of the costs of turnover for smaller businesses and in recognition of this fact the Scottish Executive introduced a rate relief scheme for small businesses in April 2003. The 2 transitional schemes outlined in the consultation paper provide options which would allow the schemes to be more favourable to small businesses.

## 9. Consultation

The Scottish Executive is holding a 12-week public consultation seeking views on the need for transitional arrangements to be put in place at the 2005 Revaluation, and on the form the transitional scheme should take. The Scottish Executive will use the responses to the attached consultation document to help inform the decision making process. Should Ministers decide to introduce transitional arrangements at the 2005 Revaluation then the transitional scheme will subsequently be set out in a Statutory Instrument and laid before the Scottish Parliament.

## 10. Monitoring & Evaluation

Feedback both from Local Authority Revenue staff who would be responsible for the day to day administration of any transitional scheme put in place and from individual ratepayers will be taken into account when considering the need for transitional arrangements at the 2010 Revaluation.