Time to rethink commercial rates **Dr. Gerard Turley** **May 2020**

Commercial rates are a vital source of income for local authorities to fund local public services. With many businesses temporarily closed or significantly curtailed due to the Covid-19 pandemic and the subsequent lockdown, revenue from commercial rates for Ireland's 31 local councils will be significantly lower this year that the €1.6bn projected in the 2020 budgets. In March 2020, the national government announced that commercial ratepayers impacted by the shutdown could apply to their local authority for a three-month rates deferral. In all likelihood this would have resulted in some businesses ceasing their rates payments. By May, this temporary deferral of rates transitioned into a rates waiver for ratepayers that were forced to close due to public health requirements, with impacted businesses no longer liable for rates for the three months to end June. At an estimated cost of €260m to be borne by the central exchequer, this may have to be considered again, depending on the timing of the economy's re-opening and the response of businesses and customers. In England, non-domestic business rates (similar to commercial rates as a tax on property used for business purposes but different in that the rate or multiplier is set centrally and revenues are not all retained locally) were waived for small businesses for the entire 2020/21 financial year. It is appropriate to compare to our neighbours in Britain as that is where our rating system originated, as rates predate the foundation of the State.

According to government sources, the legislation governing the levying and collection of commercial rates is spread across numerous enactments, many of which date from the 19th century. The primary legislation relating to rates is the Poor Relief (Ireland) Act 1838. With the exception of the Local Government (Financial Provisions) Act 1978 which removed domestic dwellings from rates liability, and the Supreme Court decision in 1984 which exempted agricultural land from rates, only minor adjustments have been made since 1838 to the operation of the rating system. In current times, local authorities are under a statutory obligation to levy rates on any property used for commercial purposes, in accordance with the details entered in the valuation lists prepared by the independent Commissioner of Valuation under the Valuation Act 2001.

Rates are a recurrent (annual) tax on business properties. Similar to the residential property tax, rates are a local tax, where the tax is assigned to local as opposed to central government, and with rate-setting powers i.e. the rate called the Annual Rate on Valuation (ARV) is determined by the local authority (as a reserved function, by the elected councillors). Currently, commercial rates (and the LPT) are one of three traditional sources of local government income; charges/user fees and central government grants are the other two revenue streams. Commercial rates account for about 30 per cent of annual local authority income. However, that is not the full story. There is a large variation across local authorities with respect to commercial rates. Here we report on four differences.

For one, the rates share of revenue income (Figure 1). There is considerable cross-council variation in the rates share of revenue, with urban city councils that have a large commercial base heavily dependent on rates income as against smaller rural councils that are more reliant on central government grants. In the three Dublin county local authorities, approximately half of their revenue income comes from commercial rates. In small rural councils such as Leitrim, Laois, Longford and Roscommon County Councils, less than one fifth of their revenue income is derived from rates. So although the shutdown will negatively affect all local authorities, the impact will not be uniform.

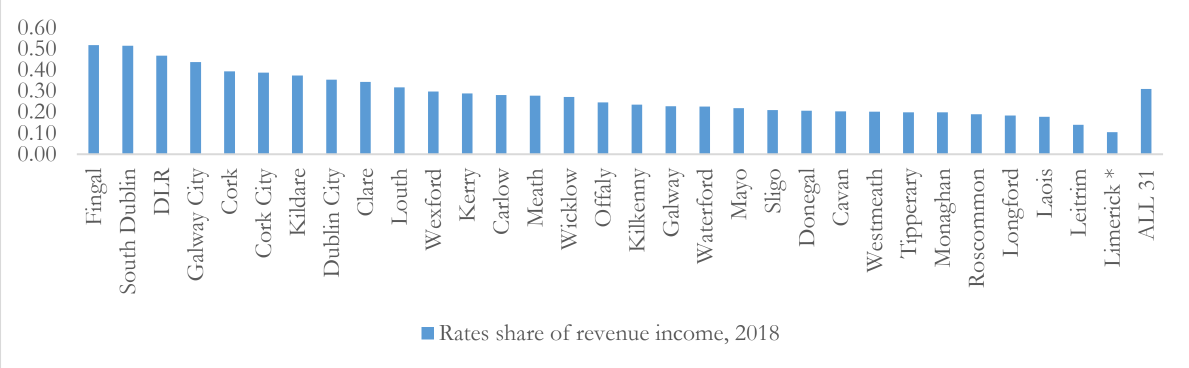


Figure 1: Rates share of revenue income, 2018

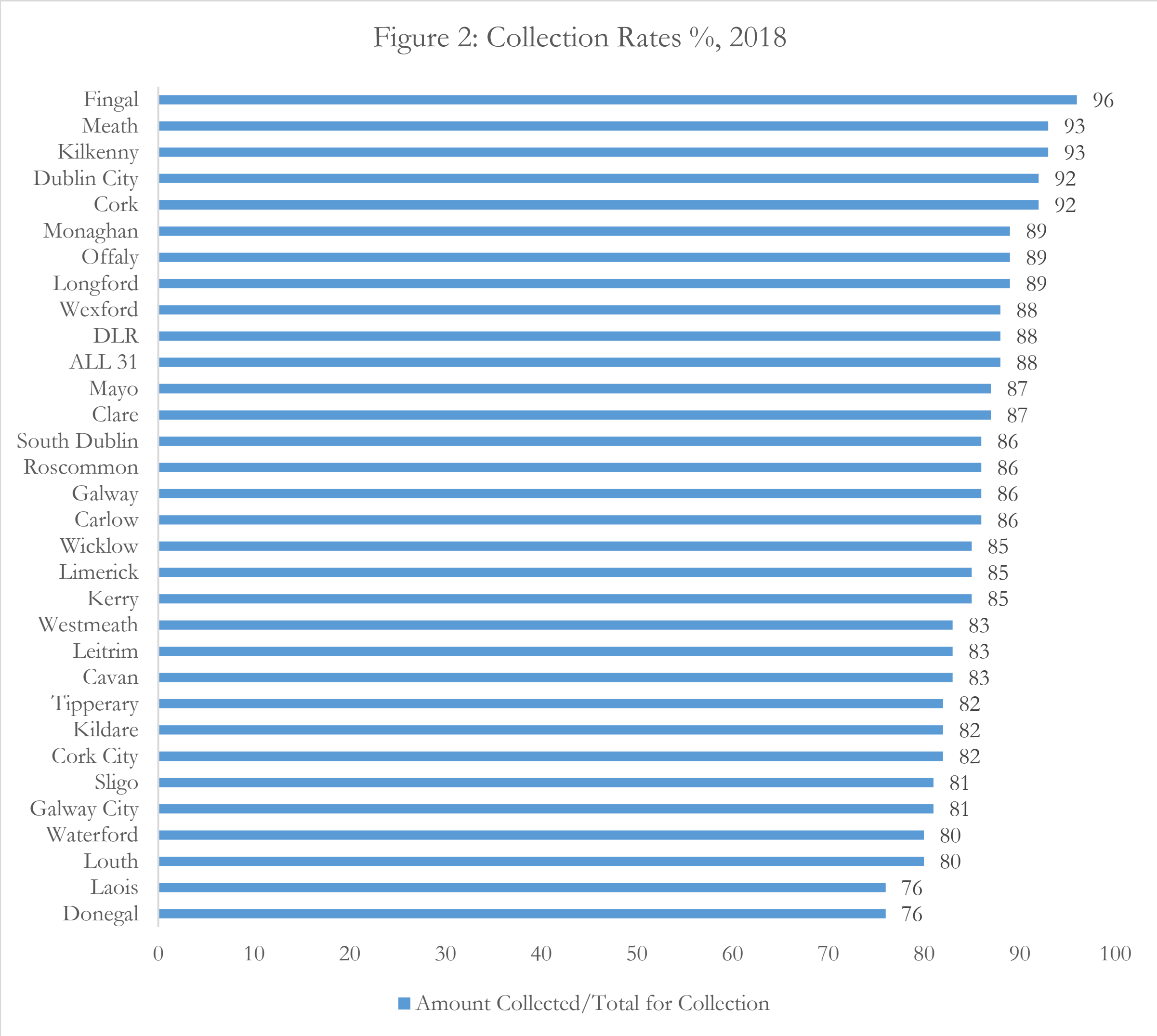
Two, the variation in the ARV (Table 1). Although it is difficult to compare the ARV across the local government sector due to revaluations undertaken in some but not all councils, the difference is striking. For those councils that have undergone a rates revaluation, the ARV varies from a high of 0.2760 and 0.2680 in South Dublin County Council and Dublin City Council respectively to a low of 0.1796 and 0.1732 in Fingal and DLR County Councils respectively, with 19 other councils levying rates between 0.2677 and 0.1919. Of the eight councils yet to undertake a revaluation, Kerry County Council 'strikes' the highest rate at 79.25 whereas the lowest rate, at 66.59, is levied by Galway County Council. Of course, one of the explanations for these large cross-council differences in ARV is the variation in expenditure per capita, ranging from a high of over €1,500 to a low of less than €600 in local council spending per person. As local governments are required to balance their adopted revenue budgets, all current expenditures have to be financed from revenue income (i.e. no planned borrowing permitted to pay for day-to-day spending, unlike at central government level), with the ARV and commercial rates used as a balancing item.

Three, there are sizeable differences in collection rates (Figure 2). Defined as the ratio of commercial rates collected to total rates for collection, the national collection rate in 2018 was 88 per cent. Taking into account the commercial rates accrued, but also arrears, waivers, write-offs and reliefs for vacant properties, collection rates range from a high of 96 per cent (by Fingal County Council) to a low of 76 per cent (by Donegal and Laois County Councils). Many councils with relatively low collection rates established debt collection units to manage and improve collection rates, with varying degrees of success. The increase in unpaid rates bills associated with the economic contraction is likely to result in an increase in debt collection services, used internally or, more controversially, outsourced to third-party private debt collectors.

Table 1: ARV, 2020

Kerry	79.25	
Mayo	78.42	
Cork City	74.75	
Cork	74.75	
Clare	72.99	
Donegal	71.81	
Galway City	67.40	
Galway	66.59	
South Dublin		0.2760
Dublin City		0.2680
Limerick		0.2677
Waterford		0.2648
Carlow		0.2571
Wexford		0.2460
Longford		0.2401
Sligo		0.2300
Monaghan		0.2260
Roscommon		0.2250
Kildare		0.2246
Laois		0.2217
Leitrim		0.2208
Offaly		0.2198
Wicklow		0.2170
Louth		0.2100
Cavan		0.2010
Kilkenny		0.2000
Westmeath		0.1940
Meath		0.1938
Tipperary		0.1919
Fingal		0.1796
DLR		0.1732

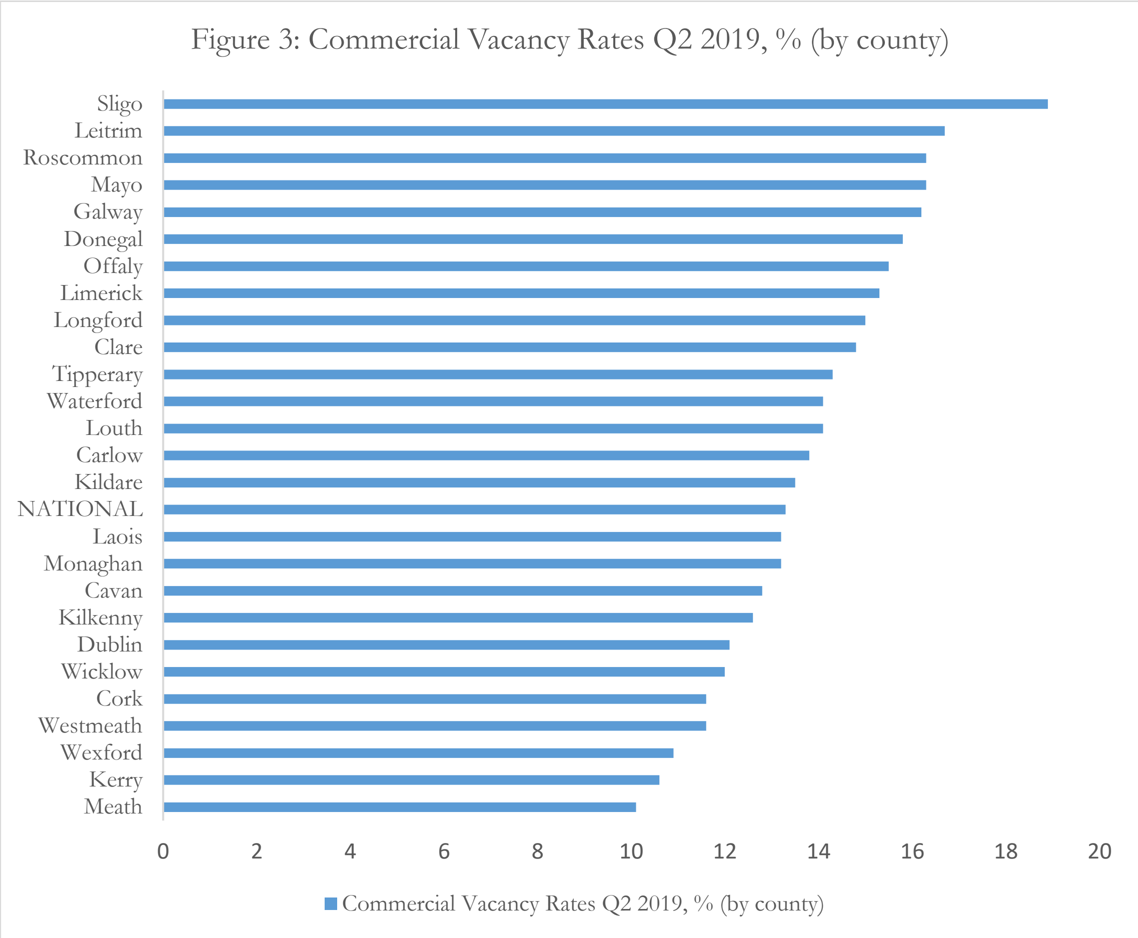
Source: Department of Housing, Planning and Local Government



Source: Department of Housing, Planning and Local Government.

Four, the variation in vacancy rates (Figure 3). Using county data, GeoDirectory publishes quarterly estimates of commercial property vacancy rates. In Q2 2019, the national vacancy rate was 13.3 per cent (equivalent to over 28,000 vacant commercial properties), with a high of 18.9 per cent in Sligo and a low of 10.1 per cent in Meath. The highest vacancy rates were all in the west and north west of the country, corresponding with the most rural parts of the economy. Given the economic downturn and the short-term prospects for the business sector, the number of vacant commercial properties is expected to increase, with a knock-on effect for commercial rates and local authority income.

Aside from these (not unexpected) cross-council variations reflecting differences in local preferences, circumstances and choices, what does this brief analysis of commercial rates tell us? Given the current economic circumstances, and the inevitable competing calls on a new government from businesses (and especially SMEs) for assistance and enterprise supports, what is needed is a comprehensive and urgent review of commercial rates. Returning to our British counterparts, when announcing the abolition of business rates in 2020/21 for small businesses the UK Chancellor of the Exchequer Rishi Sunak in his March budget also announced a fundamental review of business rates by HM Treasury. In Scotland a similar review was published in 2017. Some of the 30 recommendations of the Barclay Review of Non-Domestic Rates that might be considered here include a redefinition of the rates base, more regular revaluations and a business growth accelerator that would provide for a one-year holiday on investment in new machinery or business expansion.



Source: GeoDirectory

In the Irish context, similar reviews have taken place in the last 15 years, but arguably in very different conditions compared to present circumstances. To name but three, there was the Indecon Review of Local Government Financing in 2005, in 2009 the Commission on Taxation Report and in 2018 the Local Government Audit Service Overview of Commercial Rates. Interestingly, in the two earlier reports there was a recommendation to widen the rates base to include certain properties, including Government buildings, educational and professional institutions with commercial outlets/activities and certain non-State properties exempt from commercial rates.

Aside from an overall review of local government funding (which may not be the best option as unlikely to recommend anything other than the need for the three sources – local taxes, charges and grants - outlined above), what would be more useful is a root and branch review of one of these sources, namely local taxes. This time-limited review should incorporate a review of the LPT (not just the date of revaluations, but also the method of valuation, the base rate and the local adjustment factor, the 80/20 split and the equalisation fund, and more substantive issues like alternatives to the LPT such as, for example, a site value tax) and a review of commercial rates, with a broad terms of reference to include not only the operation of the rating system and its overall burden on businesses and impact on ratepayers but also other business tax alternatives, of a local nature.

Among others, consideration might be given to, for example, a local business tax with a base other than property, reassignment of motor vehicle taxes (where, in future, the revenue is shared between central and local government) or a congestion tax/charge in our main urban centres. Whatever the recommendations of such a review of local taxes, the present crisis presents a new government with an opportunity to rethink commercial rates, with a view to identifying, based on theory but also international best practice, the most desirable – or least harmful - local taxes, levied by local councils and imposed on local taxpayers.