

# Lowering the threshold

*With the threshold for business rate relief to be significantly reduced as of April this year, Sue Boyall assesses the options for mitigating liability*



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It was nearly three years ago that the government introduced full business rates on empty non-domestic properties. This was a highly unpopular move at the time, particularly in view of the prevailing economic climate.

Currently, the rateable value threshold at which an empty property becomes subject to business rates stands at £18,000. This threshold is due to be significantly reduced as from 1 April 2011, thus bringing many more properties within the scope of empty rates liability.

In light of this change, it is important to be aware of the various methods by which liability for empty rates may be mitigated.

## Relevant legislation

The Local Government Finance Act 1988 provides that rates are to be payable in respect of empty properties as set out in Regulations.

Prior to 1 April 2008, most empty commercial properties received 100% relief for the first three months followed by 50% thereafter. Industrial/warehouse properties received 100% relief for as long as they remained empty.

This changed with the coming into force of The Rating (Empty Properties) Act 2007, which restricted the business rates relief available for unoccupied properties. The aim was to encourage owners to bring their properties back into use rather than leaving them vacant.

The Non-Domestic Rating (Unoccupied Property) (England) Regulations 2008 define the properties that are rateable under the provisions of the 1988 Act, and those that are exempt. (Equivalent Regulations apply in Wales). Under the 2008 Regulations, empty commercial properties now

receive 100% relief for the first three months (six months in the case of industrial/warehouse properties), with full rates being paid thereafter (Regulations 4 (a) and 4 (b)).

Initially, the rateable value threshold at which an empty property became liable for business rates was £2,200 (Regulation 4 (g) of the 2008 Regulations).

Following intense lobbying from the property industry, the threshold was increased from £2,200 to £15,000 with effect from 1 April 2009. The government said that this would take approximately 70% of empty commercial properties outside the scope of empty rates. Although this helped to some degree, many felt that it did not go far enough (particularly in London).

For the year 2010 to 2011 the threshold was increased to £18,000.

For the year 2011 to 2012, however, the threshold will be taken back down to £2,600 in England and £2,200 in Wales.

This latest change will bring many more properties within the scope of empty rates, and consequently more property owners (both landlords and tenants) will need to consider the possible ways of mitigating this liability.

## How are business rates calculated?

Business rates are calculated by multiplying the rateable value of the property by the relevant multiplier.

Rateable values are revised every five years by the Valuation Office Agency (the VOA). Current rateable values came into effect on 1 April 2010. Rateable values of individual properties can be checked on the VOA website.

The rateable value is based on the amount of the yearly rent reasonably obtainable for the property in question, assuming that the property has been put into repair where it is economically

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reasonable to do so. If it would not be economically reasonable to do so, the valuation will be based on the yearly rent reasonably obtainable for the property in its actual (unrepaired) state.

The multipliers are revised each year. The standard multiplier in England for 2010/11 is 41.4 pence.

Various reliefs may be available (eg small business rate relief, charitable rate relief and, of course, empty property rate relief).

### Who is liable for payment of business rates on empty properties?

The 'property owner' (ie the person entitled to possession of the property) is liable to pay the business rates. This will include a tenant, so where the tenant is liable for rates under the terms of its lease, which is the norm, then the tenant will remain liable, even if they are no longer in occupation.

### Ways to mitigate empty rates

There are a variety of options open to property owners seeking to mitigate or avoid liability for empty rates. Some of

these depend on the characteristics of the property, and some on the identity of the ratepayer. Others are of general application.

### General considerations

**Keeping existing tenants on the hook**  
Landlords should think carefully before forfeiting or accepting early termination of existing leases, since while a lease is in place the tenant will usually remain responsible for the rates. A landlord may wish to wait until it has found a new tenant before proceeding.

### Finding a new occupier

An obvious suggestion, but clearly not always possible in a difficult market. Property owners may need to consider offering additional incentives to entice prospective occupiers, eg lowering rents, additional rent-free periods, capital contributions, or reverse premiums. Temporary occupations may also be a good option (see below).

### Lease terms

Where a property is let, the lease will state whether the landlord or the tenant

is to pay the business rates. Usually, the tenant will be liable.

*What additional provisions might a landlord wish to include in its leases?*

- A landlord may seek to provide that if the tenant vacates the premises prior to the end of the term, and takes the benefit of any rating relief, then the tenant should compensate the landlord for any loss of relief after the end of the lease term. A tenant would be likely to resist such a provision since, if it were to close the premises before the end of the term (in all likelihood due to trading difficulties), it would wish to avoid the additional expense of reimbursing the landlord for any loss of rating relief.
- Business properties are re-valued every five years for rating purposes. Since the occupier may make a proposal to alter the rateable value, a landlord may wish to restrict or prohibit the tenant from doing so in order to retain control of the situation.

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What additional provisions might a tenant wish to include in its leases?

- Tenants should remember that until such time as their lease is terminated (eg by way of expiry, surrender, exercise of a break clause or forfeiture), or until they have found an acceptable assignee or under-tenant, they may remain liable for empty rates under their lease.
- Tenants should make sure that they have the flexibility to assign or underlet without unreasonable restrictions in the event that they no longer require the property for their own occupation.
- Inclusion of a tenant's break clause would also introduce flexibility.

### Maximisation of void rate relief by way of temporary occupation

#### *Occupation by third parties*

Once again, this is only an option where demand exists, but in light of the reduced threshold this could become an increasingly attractive option for landlords.

Imaginative new initiatives have emerged in recent years, eg the growth of the 'pop-up shop', which has been used to great effect by established retailers as well as by charities and small businesses. There have been pop-up bars, cafes and restaurants as well as pop-up retail outlets.

As stated above, where a property is vacant, full business rates will become payable after six months or three months, depending on whether it is a warehouse/industrial (six months) or not (three months).

However, if a property is let or occupied for six weeks or more then,

when the property becomes vacant again, a new exempt rates period can be claimed (Regulation 5 of the 2008 Regulations). Such arrangements must, of course, be genuine.

Landlords wanting to enter into such arrangements will need to make sure that they are able to regain possession so as to fit in with their future plans. Care needs to be taken in the negotiation and preparation of any documentation.

The benefits for the landlord are that the new occupier will be responsible for rates, and the landlord will receive an income by way of rent (and contributions towards insurance and maintenance of common items where applicable). There may also be other advantages in having the premises occupied (eg repairs/decoration by the ingoing occupier, and an improvement in appearance and security). In addition, of course, when the occupation comes to an end, so long as it has lasted for a period of at least six weeks, the landlord will be entitled to a fresh void period of a further three or six months if it is still unable to let the premises to another occupier.

This sort of arrangement may be particularly attractive to charities and/or small businesses looking for temporary and/or additional accommodation. Charities, in particular, will be entitled to charitable rate relief and may be only too pleased to enter into short-term lease arrangements, particularly if a very favourable rent (or even no rent) is agreed. The downside is that the landlord may want the premises back at short notice if they find a permanent tenant and that, depending on the nature of the property and the intended use, expenditure may be required in order to make the premises fit for the tenant's intended use.

#### *Occupation by the owner*

An owner can trigger a new empty rate period by temporarily occupying the property itself for at least six weeks (eg for storage purposes). Owners who wish to do this should keep the local authority informed of the relevant dates of occupation and make sure their temporary use is not in breach of planning.

### Characteristics of the property

Certain additional possibilities may be available depending on the nature of the property.

## Key changes

### Current position (up to 31 March 2011)

#### Empty non-industrial/warehouse property (eg shop or office)

- No empty rates payable for properties with a rateable value below £18,000.
- For properties with a rateable value of £18,000 or above:
  - 100% business rates relief for the first three months; and
  - full rates payable after three months.

#### Empty industrial/ warehouse property

- No empty rates payable for properties with a rateable value below £18,000.
- For properties with a rateable value of £18,000 or above:
  - 100% business rates relief for the first six months; and
  - full rates payable after six months.

### Position after 1 April 2011

#### Empty non-industrial/warehouse property (eg shop or office)

- No empty rates payable for properties with a rateable value below the new threshold of £2,600 in England and £2,200 in Wales.
- For properties above the relevant threshold:
  - 100% business rates relief for the first three months; and
  - full rates payable after three months.

#### Empty industrial/warehouse property

- No empty rates payable for properties with a rateable value below the new threshold of £2,600 in England and £2,200 in Wales.
- For properties above the relevant threshold:
  - 100% business rates relief for the first six months; and
  - full rates payable after six months

**Listed Buildings**

If the property is a Listed Building it will be exempt under Regulation 4(e) of the 2008 Regulations.

**New properties: delay in completion**

As new properties will only become liable for rates as from the date of completion, a developer might wish to delay completion until such time as they have agreements in place with prospective tenants or purchasers. The local council may serve a completion notice in certain circumstances.

**Demolition**

Under the terms of the 2008 Regulations, empty rates are payable in respect of a building (or part of a building), together with the land used for the purposes of the building (or part of it). Empty rates are not payable in respect of open land.

Properties subject to demolition will be removed from the rating list from the date of commencement of demolition. If a property is due for demolition, an owner may bring its programme forward in order to avoid paying rates. There must be a genuine demolition plan.

For older vacant buildings (particularly those that are reaching the end of their useful life), this might be a possible course of action, although the

advantages would need to be weighed against the disadvantages (eg expense of demolition).

**Properties subject to a prohibition against occupation**

If there is a legal prohibition of occupation (Regulation 4 (c) of the

2008 Regulations), or if a property cannot be occupied due to the action of a public authority (Regulation 4(d)), a vacant property will be exempt from rates liability (eg under fire regulations or health and safety legislation). This may be worth exploring in certain cases.

**Properties incapable of beneficial occupation**

If a property is incapable of beneficial occupation it will be removed from the rating list and no rates will be payable. If part of the property is incapable of beneficial occupation, the rateable value for the period during which the relevant part cannot be used will be reduced.

A property may be incapable of beneficial occupation for a number of reasons, eg:

- By reason of an external event such as fire flood or storm damage. The effect would need to be severe.

*An owner can trigger a new empty rate period by temporarily occupying the property itself for at least six weeks.*

- Alteration, renovation or modernisation. If works are being carried out that will produce a different property from that existing prior to the works commencing, then the property (or part) may be removed from the rating list on commencement of works and added back following completion. There must be a genuine scheme of works.
- Constructive vandalism. This occurs when the owner removes items and/or services from a property without any intention of carrying out a modernisation programme, or demolition, in order to argue that rates should not be payable either because the property is beyond economic repair or that occupation will be prohibited under health and safety legislation. It is not clear exactly what services would need to be missing from a property in order for it to be removed from the rating list, and so care should be taken if considering this as an option.

**Properties for which there is no demand**

If there is no demand for a property, then the property would command no annual rent and might be removed from the rating list. The owner would need to show that it had carried out active and comprehensive marketing.

**Conclusion**

The lowering of the empty rates threshold will mean that many more properties will fall within the scope of empty rates liability. Advisers should be aware of the various options open to ratepayers to mitigate or avoid potential liability, and should take into account both the nature of the property and the individual ratepayer when considering the options in each case. ■

**Other possible exemptions and reliefs**

There are various additional exemptions and/or reliefs available in certain circumstances.

**Characteristics of the owner  
Exemptions under the 2008 Regulations**

The property will be exempt if:

- the owner is entitled to possession only as personal representative (Regulation 4(h));
- the owner is subject to a bankruptcy order (Regulation 4(i));
- the owner is a company subject to a winding-up order (Regulation 4(k));
- the owner is a company in administration or subject to an administration order (Regulation 4(l)); or
- the owner is a liquidator (Regulation 4(m)).

**Charities/Community Amateur Sports Clubs (CASCs)**

If the owner is a charity or a CASC, and it appears that when the property is reoccupied it will, wholly or mainly, be used either for charitable purposes or for the purposes of the CASC, then the property will be zero-rated.

**Other available reliefs**

Depending on any other reliefs available to the ratepayer (eg a small business entitled to small business rate relief), it might be worth continuing to occupy the property in order to obtain the benefit of those reliefs.