

# The impact of business rates on flexible workspaces and proposal for a relief

Submitted by Enterprise Nation in collaboration with a flexible workspaces expert group.

## Summary

- Our experience as a small business support and membership organisation tells us that alongside the impact of Brexit, business rates is a top concern for small business owners. For this reason, Enterprise Nation facilitated a discussion among a group of experts in business rates and flexible workspaces, which resulted in this paper.
- It has been found that open workspaces fuel small business growth and productivity; however, small businesses that use open workspace are at a disadvantage compared with those businesses that use traditional buildings or serviced offices as they are currently not eligible for small business rates relief. This results in a barrier for shared workspace operators to create more open workspaces which small businesses are looking for. Shared workspaces in London were disproportionately impacted by the recent rates re-evaluation, and this paper mostly discusses issues faced in London.

## Current policy context

1. Small businesses that use open workspace (like co-working spaces) are at a disadvantage compared with those that use traditional buildings or serviced offices so far as eligibility for small business rates relief (SBRR) is concerned.
2. Businesses which occupy only one rateable property in England assessed at less than £12,000 rateable value (RV) are entitled to 100% relief. Relief on a sliding scale is available if the assessment is between RV £12,000 and £15,000.<sup>1</sup>
3. A property will have a separate rating assessment if it is leased or licenced to an occupier which has exclusive or paramount control of a defined area of floorspace. Thus most serviced office buildings have multiple rating assessments and individual occupiers are able to claim SBRR should they meet the eligibility criteria. The shared space within serviced buildings, such as canteen facilities, will have its own rates assessment, liability for which will fall to the serviced office company.
4. Shared flexible workspace buildings provide similar facilities to serviced operators but as none of its occupiers have exclusive or paramount control of any part, the entire property will be the subject of a single rating assessment and occupiers do not benefit from SBRR, placing them at a competitive disadvantage.

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<sup>1</sup>SBRR is also available to occupiers who have one main property and other additional properties that each have a RV below £2,900 with an aggregate RV for all its properties below £20,000 (below RV £28,000 in London).

5. The current business rate system penalises small businesses that share space flexibly. The system incentivises office space operators to divide space into individual offices rather than open spaces, which are not practical or affordable for small businesses. The current system inhibits development of more open work spaces and increases their cost to users. For example, the 2017 business rates revaluation has almost doubled the amount paid by London's open workspaces. This has a knock-on effect on affordability, diversity and inclusion.<sup>2</sup>

## Market context

### The kinds of businesses that make up the shared workspace market

#### Shared workspace users

6. 80% of business activities in shared workspace can be classified by: digital; advertising; marketing and communications; designer-makers and product design; production, TV, music and photography; or with a social enterprise and charity focus.<sup>3</sup> An increasing number of open workspaces are catering for biotech businesses and scientists.
7. Incubators, accelerators, co-working spaces, makerspaces and artists' studios all make up the shared workspace market and play an important role in the continued success of London's economy. The main users of these spaces are small and micro-businesses; almost a third of SMEs founded between 2009 and 2011 used an incubator, accelerator, or co-working space.<sup>4</sup> The industry of business residents often depends on the demographic of the space – for example community-focused workspaces with outreach programmes are likely to have a more diverse set of users than incubators targeting high-growth start-ups.
8. The shared workspace market is especially popular in the creative economy: one in four of all London's small and medium-sized enterprises in the digital and creative sectors have used a shared workspace, such as an incubator, accelerator or co-working space.<sup>4</sup>
9. A survey conducted by The Clubhouse revealed the following breakdown of members by sector, showing that there is demand for flexible working spaces across the business sectors:

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<sup>2</sup> <https://lep.london/sites/default/files/documents/publication/The%20affordability%20crisis%20-%20business%20rates%20aren%27t%20working%20for%20london%27s%20open%20workspaces.pdf>

<sup>3</sup> [https://www.london.gov.uk/sites/default/files/supporting\\_places\\_of\\_work\\_-\\_jacs.pdf](https://www.london.gov.uk/sites/default/files/supporting_places_of_work_-_jacs.pdf)

<sup>4</sup> [https://www.ippr.org/files/publications/pdf/start-me-up-final-report\\_Dec2016.pdf](https://www.ippr.org/files/publications/pdf/start-me-up-final-report_Dec2016.pdf)

Financial Services/ Wealth Management/ Asset Management	13.30%
Professional Services/ Accountancy	1.20%
Professional Services/ Management Consultancy	20.60%
Professional Services/ Law	3.00%
Professional Services/ Other	7.80%
Transport & Logistics	1.20%
Property Development/ Investment/ Advisory	10.90%
Technology/ Telecoms	12.10%
Mining / Oil & Gas / Energy	2.40%
Executive Search/ Recruitment - Training and Development	6.00%
Marketing/ Media/ PR	6.00%
Venture Capital/ Private Equity	1.80%
Fashion/ Design/ Art	0.00%
Consumer Goods	0.00%
Leisure/ Entertainment	1.80%
Hospitality/ Travel	<1%
Healthcare	1.20%
Retail/ Wholesale	2.40%
<a href="#">Other (View all)</a>	7.20%
	100%

### Shared workspace owners

10. There are now more than 2,800 companies that have flexible office space as part of their portfolio. This represents a 4.9% increase in the number of operators within the UK during 2017.<sup>5</sup>
11. The charity sector is prominent, with 42% of sites in London operated by a charity provider. A further 12% are run by social enterprise/community interest providers, 8% by educational institutions, local authorities and cooperatives, and 37% by the private sector.<sup>6</sup>
12. The three largest providers of serviced office space in London in 2017 only made up 17% of the total market with a huge number of niche providers. These smaller operators cater for unique but growing segments of the market. The number of smaller operators, who run only one or two centres, has continued to proliferate and represent a large proportion of supply to the market.<sup>5</sup>

### Evidence of an unmet demand for shared workspace

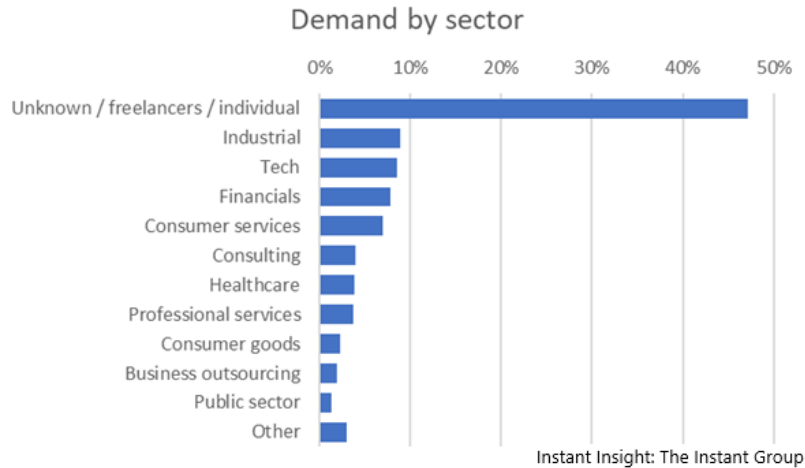
13. The rapid increase in demand for shared workspace has been a recent phenomenon. As such, there is limited research around unmet demand although as early as 2014, the GLA noted that 3,500 artists are on waiting lists for workspace.<sup>7</sup>
14. The gaps identified in shared workspace provision in London are predominantly by geography and sector. The majority are operated in central London, and tend to be dominated by the digital tech, communications and media sector.
15. Demand is increasing in the secondary and tertiary markets across the UK. Traditionally these markets have had limited high quality space as seen in the major cities; however, this is changing as new providers move into these markets with increasing amounts of high quality “hybrid” space (hybrid space is one space that has both coworking and private offices included).

<sup>5</sup> <https://www.theinstantgroup.com/media/1624/uk-market-summary-2018.pdf>

<sup>6</sup> GLA 2016

<sup>7</sup> [https://www.london.gov.uk/sites/default/files/artists\\_workspace\\_study\\_september2014\\_reva\\_web\\_0.pdf](https://www.london.gov.uk/sites/default/files/artists_workspace_study_september2014_reva_web_0.pdf)

16. Based on The Instant Group’s view of the market, the below represents current demand for flexible space in the market:



### Evidence of where rates have been a barrier to growth in the supply of shared workspace

17. A report by IPPR found that affordability was a key concern for many workspace providers they spoke to. London businesses faced large increases in business rates in due to the 2017 revaluation, with some areas on the edge of the Central Activities Zone (CAZ) facing a doubling of notional business rates. These areas have many open workspaces in which small business tenants effectively pay business rates, as providers pay rates on the whole space which they pass on in rent – even though they would receive small business rate relief if they occupied an individual unit that was not shared. Open workspace providers are concerned that ongoing issues around rates will make their spaces unviable.
18. The overall business rates bill for a sample of 340 open workspaces in the GLA open workspace database has almost doubled<sup>2</sup>. This significant increase has compromised the business and impact model for open workspace provision, which has a knock-on impact on affordability, diversity and inclusion for London and Londoners.
19. In central London especially it is hard to run a shared workspace that is financially profitable. Capital Enterprise found that around 30% of shared workspaces have ceased operation in the period since 2016. Case studies and qualitative research indicates that increase in rents and rates are the main contributory factors. No data is available on the number, location or type of open workspaces which have opened in the same period. Anecdotal evidence suggests that smaller, more community and more entrepreneur-focused open workspace providers are being replaced by larger, more commercial operators which often offer more traditional office space alongside co-working space.

## Proposal

20. Availability of affordable and flexible office space supports entrepreneurs in early stages and is therefore crucial for innovation, economic growth and creation of jobs.<sup>8</sup>
21. Business rates should therefore be reduced in respect of open workspace so that rates liability is comparable between buildings whether used for serviced or flexible space.

### New discretionary relief scheme

22. Local authorities already have discretionary powers to reduce rates in deserving cases, but very few councils choose to do exercise this discretion as they have to meet the cost of discounted rates. The proposal therefore is that the Government should announce a new rates relief scheme for shared workspace, whereby councils granting discretionary relief would have the costs reimbursed by central government.
23. This is a route which has been used frequently by government over recent years as a means of delivering targeted rates relief without the need for any new legislative powers, either primary or secondary. Examples of rates reliefs and discounts which have operated through this regime over the last 4 years, with central government reimbursing the costs of discretionary relief granted in accordance with government guidelines, include the Discretionary Revaluation Relief, Temporary discount for shops, pubs and restaurants, the Reoccupation Relief Scheme and others. The new relief for small retailers announced at Budget 2018 is also to be funded in this way. While ways exist to support small businesses in some sectors, one for shared office spaces does not exist.

## Impact

### Costs

24. Business rates are estimated based on square footage, and it is a fair assumption that the UK has 12,600,000 square feet of open coworking space - some 85% of this is estimated to be in England.<sup>9</sup> Gerald Eve LLP, specialist business rates surveyors, advise that these co-working spaces presently pay business rates in the region of £107m per annum. The cost to Government of any new relief would depend on the details of such a scheme, but if the one-third reduction being granted to small retailers for 2 years from April 2019 is replicated, the cost of the proposed coworking relief scheme would be around £36m pa.
25. The plan to devolve business rates in 2020 further complicates discussion of 'cost', as the split between the GLA, Treasury and London Boroughs is subject to unknown change.

### Benefits

26. Recent data has indicated a change in focus for shared workspace providers, with existing operators looking to increase the scale of their locations rather than the number of centres increasing with anecdotal evidence attributing this to increased rent and rates. As previously

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<sup>8</sup> <https://www.ippr.org/publications/start-me-up-the-value-of-open-workspaces>

<sup>9</sup> The Instant Group

stated, 30% have ceased operation in the period since 2016. With the introduction of rates relief, we foresee more shared working spaces to be opened, which would drive competition and in turn drive the cost to small businesses down.

27. A recent study undertaken by the International Workspace Group shows that business leaders acknowledge that flexible working has made their business more productive (85%), and a remarkable 67% think that flexibility can improve productivity by at least a fifth<sup>10</sup>.
28. Availability of affordable flexible working space enables business growth and increase in productivity by:
  - Providing an environment for collaboration, creativity and new business opportunities
  - Providing a community for learning and business support
  - Reducing social isolation, and improving mental health
29. Growing businesses provide increases in corporation tax, VAT, PAY and NI contributions. In addition, open workspaces have a positive impact on regeneration<sup>11</sup>.
30. The UK's Industrial Strategy recognises the value of start-ups and the need to create conditions that allow them to increase productivity and reach their full potential. This proposal is cost-effective, easily implemented and goes some way to create better conditions for small business in the UK.

### Impact outside of London

31. The recent rates re-evaluation disproportionately impacted shared workspace in London due to large property price increases in the capital – eighteen London boroughs saw average increases of over 20 per cent, compared to one in the West Midlands and none in Manchester. Despite this, clarity on shared workspace eligibility for SBRR and discretionary relief would be valued by workspaces across the country.
32. The most notable gap in provision of shared workspace is the current scarcity outside cities, however existing research does not tell us whether or not there is considerable demand there. Successful workspaces depend on the local attractions of the area, with research finding that good public transport links were highly desirable, as well as a location within a known hub or clusters of similar businesses within the same sectors – particularly for creative and digital technology focussed workspaces.<sup>3</sup> The proximity to cultural and leisure facilities and the general vibrancy of the area has also been listed as a key factor.<sup>3</sup>

### Eligibility definition

33. In order to ensure that relief is limited to the targeted properties and not used as an avoidance scheme, it is suggested that the relief scheme applies to a separately rateable hereditament

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<sup>10</sup> [http://assets.regus.com/pdfs/iwg-workplace-survey/iwg-workplace-survey-2019.pdf#\\_ga=2.263786444.1507680416.1553885575-1338964512.1553885575](http://assets.regus.com/pdfs/iwg-workplace-survey/iwg-workplace-survey-2019.pdf#_ga=2.263786444.1507680416.1553885575-1338964512.1553885575)

<sup>11</sup> <https://www.futureoflondon.org.uk/wp-content/uploads/delightful-downloads/2017/11/Workspace-that-Works-report-WEB-270317.pdf>

where, other than those providing management services, the users of the hereditament are not employees or representatives of the same company or group of companies as the rateable occupier.

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**About Enterprise Nation**

Enterprise Nation is a small business network and business support provider. Its aim is to help people turn their good ideas into great businesses – through expert advice, events, acceleration, diagnostics and networking. Enterprise Nation was founded in 2005 by Emma Jones MBE, also co-founder of national enterprise campaign StartUp Britain. She is author of best-selling business books including Spare Room Startup, Working 5 to 9, Go Global, Start a Business for £99 and the StartUp Kit, Going for Growth. In 2016 she was announced as the Government's Trade Ambassador. In 2017 the Institute of Chartered Accountants England and Wales (ICAEW) announced it was to collaborate with Enterprise Nation to start building a world-leading adviser platform. In 2018, Richard Harpin, the entrepreneur behind global home emergency repair firm Homeserve, invested in the company as part of a drive to create a 'more entrepreneurial Britain.'

34. 2<sup>nd</sup> April 2019