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Briefing Note

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Business rates warning for multi-let office buildings

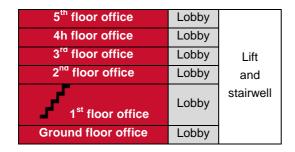
In July 2015, the Supreme Court handed down a decision on a business rates appeal for an office assessment in Tower Hamlets. This seemingly innocuous case (Woolway v Mazars [2015] UKSC 53) turned on whether the second and sixth floors of an office building could be classed as one unit for business rates purposes. It was not surprising that the Supreme Court said no in that instance, but the reasoning for that decision has overturned more than 50 years' practice and will affect a large number of tenants in multi-let office buildings.

What does this mean in practice?

It has been standard practice for the Valuation Office and rating surveyors to amalgamate adjoining floors into one assessment i.e. if a tenant takes floors two, three and four in a 10-storey building, those floors will have a single assessment. Often the Rateable Value will be reduced to reflect the quantum of space occupied. After Mazars, this will change.

The Supreme Court decided that, where a tenant has to pass through common areas to get to the rest of their office, there should be a separate rating assessment for each office; the only exception being offices that are directly connected without the need for passing through common areas.

So, if we consider a six-storey office block as follows:



The first and second floors are linked by an internal staircase. Assuming there are only two tenants in the building, ABC Accountants on ground, first and second floors, and SLS Solicitors on third, fourth and fifth floors.

Currently, there would be two assessments in the Rating List and, if there is a discount for quantum, both firms will benefit from lower values. Following Mazars, there should be five assessments: ground floor; first and second floors; third floor; fourth floors, and; fifth floor.

Putting some flesh on the bones, let us assume each floor is 300m² and the value of the separate floors is £200/m². Taking three floors in a single letting would give a 10% discount with a 5% discount for two floors.

Rates liability for 2016/17 will be $\pounds 0.497/\pounds$ so the current position for the two firms is:

Tenant	Rateable Value	Liability
ABC Accountants (ground – third floor)	£162,000	£80,514
SLS Solicitors (fourth – sixth floor)	£162,000	£80,514

After Mazars, the situation will be:

Tenant	Rateable Value	Liability
ABC Accountants (ground floor)	£60,000	£29,820
ABC Accountants (first – second floor)	£114,000	£56,658
Total	£174,000	£86,478



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Tenant	Rateable Value	Liability
SLS Solicitors (third floor)	£60,000	£29,820
SLS Solicitors (fourth floor)	£60,000	£29,820
SLS Solicitors (fifth floor)	£60,000	£29,820
Total	£180,000	£89,460

So, ABC Accountants will be £5,964 a year worse off and SLS Solicitors will be £9,126 a year worse off. From the view point of equity, two tenants in the same building occupying the same amount of space will no longer have the same costs of occupation.

The split of the rating assessments will have no regard to the leases, even if both firms have a single lease for three floors, the decision of the Supreme Court will take precedence, based on physical facts not legal title.

This scenario will be played out across the country, with increased rates liabilities for larger occupiers in multi-let office blocks.

The example given is a simple model, but the separation could be horizontal as well as vertical. Consider a building let in suites, if the suites are not interconnecting and the tenant has to go through the common areas to get from one office to another, there will be separate assessments. Even parking spaces let with an office will be separately assessed.

Although office occupiers are the most likely to be affected, the same ruling applies equally to all property types and uses.

Next steps

Currently, the Valuation Office does not have the staff or resources to make all of the changes this decision requires in the rating lists. It is looking at it for the 2017 Revaluation and when its staff are freed up later this year (after the revaluation exercise is mostly completed), it will be looking at altering the current rating assessments and may backdate the changes to 1 April 2015, raising backdated demands for additional rates payments.

Tenants will be hardest hit but landlords will also be directly affected for empty offices and indirectly affected when rents are next up for discussion as the increased cost of occupation is factored into negotiations.

If you think you might be affected, please email <u>Rating@lsh.co.uk</u> for further advice and one of our Business Rates experts will be in touch.

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