FUTURE-PROOFING RETAIL

A SUBMISSION TO THE CHANCELLOR FROM THE RETAIL INDUSTRY

AUTUMN 2018

BUDGET2018

RETAIL IN NUMBERS

SALES GROWTH

YEAR-ON-YEAR GROWTH OVER THE PAST 12 MONTHS (SEP 17 TO AUG 18) WAS

- 1.5% — TOTAL UK
- 3.7% — TOTAL FOOD
- -0.5% — TOTAL NON-FOOD
- 7.1% — TOTAL NON-FOOD ONLINE
- -2.7% — TOTAL NON-FOOD IN-STORE

PRODUCTIVITY

AVERAGE PROFIT MARGINS

3-5%

1% GROWTH RETAIL 2017

VS

0.7% GROWTH UK OVERALL

4.4% PAY GROWTH

(YEAR ON YEAR)

JOBS

3.1M RETAIL JOBS

9% OF UK EMPLOYMENT

BUSINESS RATES

A QUARTER OF OVERALL CONTRIBUTIONS

OR **£7BN** ANNUALLY

INVESTMENT IN TECHNOLOGY

£2.6BN (2017

INVESTMENT INCREASED **5%** IN 2017 FROM 2016

APPRENTICESHIP LEVY

£140-160M IN CONTRIBUTIONS PER ANNUM

ACCOUNTS FOR **20%** OF ALL APPRENTICESHIP STARTS OVER PAST DECADE

RETAIL STARTS HAVE FALLEN BY **34%** IN THE FIRST THREE QUARTERS OF 2017/18

GENDER PAY GAP

MEDIAN PAY GAP OF **9.3%** HALF THE UK AVERAGE

DROPS TO **0.8%** FOR PART-TIME COLLEAGUES

STANDS AT **7.1%** FOR FULL-TIME COLLEAGUES

RECOMMENDATIONS AT A GLANCE

1 FREEZING BUSINESS RATES, REFORMING BUSINESS TAXATION

- Freeze the business rates multiplier for two years up until the 2021 revaluation after which three-yearly revaluations will be undertaken.
- Work with industry to set out principles for future business taxation, outline a long-term vision, align policies to international efforts, publish a holistic road map with immediate steps to reduce the burden of commercial property taxation.

2 POST-BREXIT IMPORT VAT

- Seek to stay part of a common VAT system with the EU underpinned by common rules.
- Introduce a VAT deferment scheme before March 29th 2019.
- Negotiate to maintain eligibility for UK businesses for the MOSS system.

3 IMPROVING APPRENTICESHIP LEVY FLEXIBILITY

- Allow retailers to use levy funds to cover the cost of backfilling time spent off-the-job.
- Extend the lifetime of levy funds for a further 12 months while standards are approved.
- Deliver consistency in approach across the devolved nations.

4 REGULATING THE PAYMENTS LANDSCAPE AND IMPROVING COMPETITION

- Tackle increases in charges by: extending the scope of the IFR beyond interchange fees; restricting the range of fees; and requiring an investigation into major card schemes for abuse of their dominant market position.
- Support improvements to customer journeys in Payment Initiation Services (PIS), including a single, simple, user-friendly bank authentication method, to enhance competition.
- Address uneven advantages for low-value contactless transactions whereby card transactions below £30 require no authentication, yet all PIS transactions do.

5 PLASTICS TAX & CUMULATIVE BURDEN

- Work with the retail industry to ensure there are no unintended consequences for businesses or consumers from new measures on plastic waste and products.
- Link measures relating to tax, DRS, Producer responsibility, the 25 Year Environment Plan, and the forthcoming Resources and Waste Strategy to ensure there is a comprehensive cross-Government strategy and a consistent approach.
- Establish a clear end goal for the Treasury-led parts of the Government's strategy, including channelling funds from any new revenue to waste infrastructure or marine environment improvements.

DEAR CHANCELLOR,

Retail is undergoing a prolonged and radical transformation, driven by ongoing changes in consumer behaviour and technology, fierce competition, rising costs, and squeezed family finances.

The UK's retail industry has always been dynamic and innovative, but the pace and scope of change is creating new challenges. Our industry is rising to these new challenges with significant investment and innovation, but the future will see a reshaped retail industry with different jobs and roles for our employees, less physical space, with a shift by consumers towards online shopping, a greater range of services for shoppers and a more diverse digital experience.

The shift from consumers to online shopping is creating rapid structural change in the industry, challenging traditional business models. Online retail now accounts for 16.8% of sales and this is growing by about 10% per year. By 2030 we expect that online shopping will account for half of non-food sales and up to 40% of food sales by 2030. Many retailers have already adapted to this new environment, offering customers new and easier ways to shop across digital platforms, some including click and collect and others providing direct delivery. However, the industry is undertaking these radical changes against a backdrop of rising costs, many of which have been driven by policy changes from Government.

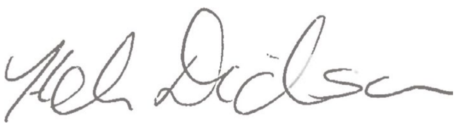
We recognise and understand why some of these policies have been implemented, and indeed work with Government across a range of policy areas, but there must be recognition that retailers are operating at historically low margins and the industry is no longer able to absorb ever-increasing costs such as business rates.

The retail industry pays a disproportionate amount of tax. We represent 5% of the economy but pays 10% of business tax and almost 25% of business rates. A tax system skewed towards high taxes on people and property is contributing to store closures and job losses and is stalling the successful reinvention of the high street. Though it may be tempting to shift the burden of business rates towards some form of online sales taxation, this would simply form a double jeopardy for many of our members who are investing in digital retailing. They would still be paying high levels of business rates on their physical stores whilst facing equally high taxation for their new online sales. This is alarming when eight out of ten of the top online retailers by sales are also on the high street.

Retailers should not be disproportionately penalised for investing in our high streets; nor should they be disincentivised from investing in new technology which will make them fit for the future. A more fundamental analysis needs to be done which looks at a long-term solution to business rates, and business taxation more broadly, as opposed to a short-term fix. During that period of review, the Government should halt the escalating costs incurred by retailers by freezing business rates.

Within the constraints of the current system, retailers continue to modernise and reinvent themselves for a transformed marketplace, making the most of the opportunities that technology present in extending choice, quality and price for consumers. The challenges are wide and many, but the possibilities are equally plentiful, and it has been good to work with Government on many of the issues, for example through the new Retail Sector Council and the Future High Streets Forum. That is why we look towards your forthcoming Budget to reduce the cost of doing business, incentivise innovation and support the industry in creating quality jobs, providing quality products at competitive prices, and future-proofing retail to ensure the best is made of the opportunities and challenges thrown up by transformation.

Yours sincerely,



Helen Dickinson OBE
Chief Executive
BRC

1 FREEZING BUSINESS RATES, REFORMING BUSINESS TAXATION

Retail is transforming. Historically, there has been a clear link between the success of a retailer and its physical shop where transactions only took place in person. However, due to changing technology and consumer behaviour, retail and the wider economy operate very differently now. It is critical that the business taxation system is updated for the 21st Century.

A key component of the business tax system that needs addressing is business rates. Retailers alone are responsible for £7 billion in business rates annually or a quarter of the overall total. The central problem with the rates system is that the national multiplier has grown out of proportion since its introduction in 1990, irrespective of the strength of the economy or success of businesses. An over-dependence on input taxes harms retailers, which are people and property intensive businesses, and such taxes have grown disproportionately compared to other taxes such as corporation tax. For every £1 retailers pay in the latter, they pay £2.30 in business rates.

Consumer behaviour has led to change in modern retail, but business rates are distorting the successful reinvention of places and efforts to future-proof the retail industry. Retail is found across all communities, but consumers now require fewer shops, and consequently staff, and the effect is being exacerbated by the growing cost of doing business. Simultaneously, there are communities facing serious challenges including high levels of deprivation and unemployment. As retail continues to undergo change, these communities are at risk, increasing the need for Government action.

DESIGNING A SYSTEM FIT FOR THE 21ST CENTURY

Retailers cannot afford or absorb another property tax hike; a freeze in the business rates multiplier would maintain the current rate of 49.3% for the next two years (which has risen relentlessly from a base of 34.8% in 1990) and avoid going over the 50% threshold which would have a detrimental impact on communities and retailers' ability to respond to the rapid pace of transformation.

The Government should also revisit its current approach to business taxation and look across all taxes. Given the fundamental questions we now face in a digital and globalised world we need to go further than the current business tax road map, published in March 2016. Specifically, we need to rebalance input and output taxes, address other underlying problems and attract investment, which would lead to greater productivity and improved living standards.

DIGITAL TAXATION

We agree that the Government must work with the OECD to address problems with current international tax frameworks, but oppose any interim measures that result in additional burdens on the supply of goods to consumers. Taxes apply to all businesses, so the answer to current disparities in the system is not another tax solely on retail, for example on online sales or the delivery of products bought online. With every £5 spent with retailers, £1 is spent online, more than half of which is with retailers that also have shops. Government needs to reduce the business rates burden and create a system fit for the 21st century, which more fairly distributes taxes across the economy. When eight of the top ten online retailers by sales are also on the high street, a new tax burden is unlikely to ease the pressure on high streets.

RECOMMENDATIONS

- Freeze the business rates multiplier for two years to the 2021 revaluation after which three-yearly revaluations will be undertaken.
- Working with industry, set out principles for future business taxation, outline a long-term vision, align policies to international efforts, and publish a holistic road map in addition to taking immediate steps to reduce the burden of commercial property taxation.

2 POST-BREXIT IMPORT VAT

The implications for cashflow and business and UK Government compliance connected with the decision on whether the UK will seek to stay within a common VAT area with the EU are potentially huge. If the UK leaves the EU without any withdrawal treaty and thereby exits the common VAT Area without alternative arrangements, goods transferred from the EU into the UK would attract upfront import VAT liability. The increase in bureaucracy for the businesses involved would completely alter the way many operate and, in some cases, completely undermine current business models.

In that situation, goods moving between the UK and the EU would become liable for payments of import VAT upfront at the border. The reverse-charge mechanism would no longer apply to imports from the EU, which would create significant issues for cashflow. This would be particularly unwelcome for retailers already feeling the pinch of a transforming consumer landscape, an ever-increasing tax burden and the cumulative effect of other public policy and commercial pressures.

The successful negotiation and agreement of the Withdrawal Agreement with the EU will solve this problem for the duration of the transition, but there is still a great deal of uncertainty about what the UK's relationship will be with the Common VAT Area after that. We note concerns about the possible governance of a common VAT area post-Brexit, particularly with regards to the European Court of Justice, but believe that an indirect jurisdiction model could meet our policy goals without breaking the spirit or the letter of the Government's negotiating red lines.

MITIGATING RISK AND AVOIDING CASHFLOW PROBLEMS

It is encouraging that Government, through the no deal technical notices, would implement a VAT deferment scheme on business to business transactions in the event of a no deal, which would mitigate the risks to company cashflow. This offers protection for retailers and consumers and avoids the need to take out indemnity or insurance plans against the risks to cashflow. However, the technical notices do not account for transactions between EU businesses and UK consumers, and vice versa, which would result in a VAT bombshell for consumers making direct purchases from companies based in the EU. Any scheme should be put in place in advance of 29th March next year whether there is a no deal or not, to account for the risk that the final deal between the UK and EU may not necessarily contain provisions on a common VAT area.

Remaining part of or establishing a new common VAT system with the EU post-Brexit, would prevent vast additional cost and red tape in business to business and business to consumer transactions, and movements of goods and services, between the EU and UK and vice versa. Without this, UK-based companies would have to register in the EU member states they do business in, adding significantly to the burdens of doing business. Equally, without a common area, it would be impossible for a UK company to facilitate the movement of a good between two EU member states.

Unless they establish EU entities or register in at least one EU member state, UK companies would also lose access to the Mini-One Stop Shop (MOSS) in terms of making cross-European VAT payments through a single portal.

RECOMMENDATIONS

- Seek to stay part of a common VAT system with the EU underpinned by common rules.
- Introduce a VAT deferment scheme before March 29th 2019.
- Negotiate to maintain eligibility for UK businesses for the MOSS system.

IMPROVING APPRENTICESHIP LEVY FLEXIBILITY

Retailers are committed to investing in the skills of their workforces. Before the introduction of the apprenticeship levy, the industry invested £5.1bn per annum on training and development, the third highest amount invested by any industry. Apprenticeship starts in retail and commercial enterprise account for around 20% of all starts over the past decade. However, apprenticeships are only one part of the solution for retail. We welcome the recent announcement from the Chancellor for £100 million for a National Retraining Scheme and want to work with Government to ensure employers can draw down funds to pay for different types of training suitable for their workforce. The Government's commitment to engage with industry on the future and flexibility of the levy is also welcome and we will work closely with Ministers to ensure that it works better for retailers.

Skills development is critical to support retail colleagues as new technology enters the workplace, as well as support those who are at higher risk from the changing nature of work remain active in the labour market. The apprenticeship levy is an opportunity to invest in the right skills for the future of the industry, but one year in it is clear that the levy in its current form is not working. Apprenticeship starts have fallen by 34% in the first three quarters of 2017/18 compared to the previous year. Retail starts over the same period equate to just 45% of the total in 2016/17.

The retail industry's contribution to the apprenticeship levy is around £160m per annum. Retailers worked hard to prepare for the levy ahead of its introduction, with a number giving up time and resource to help the development of the new trailblazer standards. Despite the significant contribution the industry continues to make, the levy is not delivering for retail.

UPDATING THE LEVY FOR THE FUTURE

In order to facilitate quality off-the-job training in customer facing roles, time must be backfilled at additional cost to retailers, on top of the levy. Backfilling wages adds a further 20%-30% to the total cost of an apprenticeship, making it increasingly financially unviable for many in the industry, despite high demand. Allowing levy funds to be drawn down to cover the costs of backfilling would support the industry to engage more effectively with the policy.

Retailers have been paying into the system for over a year and many cannot yet draw down funds to deliver the relevant standards due to the lengthy approval process, effectively making the levy just another tax on hard-pressed retailers. Steps taken to streamline the process are welcome, but it remains out of sync with levy contributions, leaving retailers worse off and unable to deliver relevant training. The industry is waiting for up to six standards to be approved for delivery, which could see an uplift in apprenticeship starts. We have taken the initiative to develop a Level 6 apprenticeship programme as part of our BRC Learning offering; though this is welcomed by industry, there is a way to go before retailers can access all the standards needed in England.

We support the devolution of skills policy, but there are currently significant barriers to employers looking to train colleagues in the devolved nations. Many retailers have taken the decision not to offer apprenticeships in the devolved nations as the training is not consistent across borders. Greater consistency is needed in training across the UK, as well as clarity for employers in how to draw down levy funds outside of England.

RECOMMENDATIONS

- Allow retailers to use levy funds to cover the cost of backfilling time spent off-the-job.
- Extend the lifetime of levy funds for a further 12 months while standards are approved.
- Deliver consistency in approach across the devolved nations.

4 REGULATING THE PAYMENTS LANDSCAPE AND IMPROVING COMPETITION

The way consumers pay for products is one of the many demonstrable areas of changing behaviour. We produce an annual Payments Survey measuring the sales volumes and values of different payment channels. Our most recent survey shows card payments are firmly established as the dominant payment method in retail, accounting for 75% of transactions by value and, for the first time from 2016, accounting for more than half of retail purchases by volume (54%).

E-commerce, which grows every year, is almost entirely reliant on card payments. And even most digital payment methods, such as ApplePay and GooglePay, are card payments of some kind, further cementing the dominance of cards in retail payments. Retailers spend £1.1bn on accepting payments of this kind every year, the vast majority of which goes to the card payments industry.

MORE EFFECTIVE REGULATION AND SUPPORTING COMPETITION

The retail industry has long called for measures to tackle cost and lack of transparency in card fees and charges and have supported EU-level regulatory action on card interchange fees. However, since December 2015, when EU legislation was introduced to regulate interchange fees, card scheme fees have increased by £1bn in the UK and there has been a proliferation in the range of fees themselves that vary depending on the type of card, where it's issued, and where and how it's used. Card scheme fees increased by 31% on average for the retail industry in 2017, and in April 2018 increased by more than 70% for Visa transactions alone. Further increases from Mastercard are now emerging.

The revised Payment Services Directive (PSD2) supports competition in the payments market through guaranteed direct access for Payment Initiation Services (PIS) providers to the payment accounts of consenting customers, providing an alternative payment method to cash and cards. PIS are popular abroad. Giropay in Germany and iDEAL – the most popular method for online payments in the Netherlands – operate in similar ways to the way PIS could operate in the UK, and give a useful barometer of the popularity of these payment methods in markets where the political and regulatory framework supports their development.

Several challenges are yet to be resolved in the UK for PIS to compete effectively, and on a level-playing field. Consumers expect seamless experiences and interfaces, but PIS currently involves a customer journey that renders it ineffective.

RECOMMENDATIONS

- Tackle increases in charges by: extending the scope of the IFR beyond interchange fees; restricting the range of fees; and requiring an investigation into major card schemes for abuse of their dominant market position.
- Support improvements to customer journeys in Payment Initiation Services (PIS), including a single, simple, user-friendly bank authentication method, to enhance competition.
- Address uneven advantages for low-value contactless transactions whereby card transactions below £30 require no authentication, yet all PIS transactions do.

5 PLASTICS TAX & CUMULATIVE BURDEN

Retailers take their responsibility on environmental issues seriously and have done a great deal already to tackle waste, but they are under pressure from measures to tackle plastic waste and marine pollution. The Government has floated a number of policy options on plastics but has no single comprehensive strategy. Such a strategy should be outlined in the Resources and Waste Strategy later this year, including measures to make local government take a consistent approach to recycling and for sufficient waste and recycling infrastructure to improve efficiency. Measures proposed, such as producer responsibility regime reform and bans on some single use plastics can't deliver serious reductions in waste on their own. The current approach carries the risk that these multiple measures will have unintended implications for businesses and consumers.

Government has confirmed its intention to introduce a Deposit Return Scheme. We have developed proposals for a scheme that avoids disruption and cost to retailers and consumers. Based on the cost of DRS in Denmark, estimates suggest a UK-wide DRS would cost £1.1bn per annum, discluding installation costs. With retailers' margins tight, part of that cost would inevitably fall on consumers at the point of sale. However, retailers will engage constructively to ensure success in reducing plastic waste and to avoid any unintended consequences. Industry needs a system that is consistent across the UK, cost-effective and in line with the rest of the Government's environment strategy.

A HOLISTIC APPROACH AND CLEAR PRINCIPLES

Retailers strive to do the right thing and know they need to contribute more directly towards the costs of recycling and recovering packaging, alongside working with suppliers to reduce packaging and remove plastics. A reformed producer responsibility system should incentivise best practice and reward those who use easily recyclable packaging, whilst penalising those that don't move away from less recyclable packaging.

Using taxation to control the use of plastics could change producer and consumer behaviour, but if revenues raised are not put back into reducing waste and increasing re-use and recycling, it will be only a partial solution. Any fiscal measures should follow these principles:

- Proportionality: Government should seek to avoid unintended consequences that make the industry's ability to be agile and responsive on environmental and waste issues harder.
- Holistic approach: Measures should be implemented in a way that doesn't undermine reductions in other forms of waste, like food waste. Additional taxes need to take into account other costs and their impact on other reforms and policies. A combination of unconnected measures will impact margins and costs of goods, so there must be a coherent approach to ensure clarity around the impact on the cost of operations.
- Clarity of purpose: The desired environmental outcomes must be clear.
- No duplication: For packaging, reformed PRN would be the best way to deliver better outcomes.
- Transparency: Clarity about where and how a measure is being used to combat environmental issues is needed.

RECOMMENDATIONS

- Work with the retail industry to ensure there are no unintended consequences for businesses or consumers from new measures on plastic waste and products.
- Link measures relating to tax, DRS, Producer responsibility, the 25 Year Environment Plan, and the forthcoming Resources and Waste Strategy to ensure there is a comprehensive cross-Government strategy and a consistent approach.
- Establish a clear end goal for the Treasury-led parts of the Government's strategy, including channelling funds from any new revenue to waste infrastructure or marine environment improvements.

THE BRITISH RETAIL CONSORTIUM

Retail is an exciting, diverse and dynamic industry undergoing transformational change. The BRC is at the forefront – enhancing, assisting, informing, and shaping. Our broad range of stakeholders demonstrates how retailing touches almost every aspect of our culture.

The BRC leads the industry and works with our members to tell the story of retail, shape debates and influence issues and opportunities which will help make that positive difference.
We care about the careers of people who work in our industry, the communities retail touches and competitiveness as a fundamental principle of the industry's success – our 3 Cs.

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