SCOTTISH BUDGET 2024-25

POST-BUDGET SUBMISSION FROM THE SCOTTISH RETAIL CONSORTIUM

A RETAIL INDUSTRY IN TRANSITION

1. A thriving and successful retail industry is a great route to better paid jobs, more private sector investment, and additional tax revenues for the public sector. It also keeps down prices for households, supports communities[1] and helps everyone saving into a private sector pension. The industry is crucial to supporting indigenous Scottish firms as a route to market, with billions of pounds of Scottish products exported by retailers every year to the rest of the UK and beyond. Just as importantly the industry provides a key market for many other indigenous suppliers, from logistics companies moving products to builders, electricians and plasterers resolving issues in physical stores. The multiplier effect of retail on Scotland's economy is measured in billions.

2. The industry is one of the most dynamic and innovative. This can be seen through significant new investment in in-store technology and order points, home delivery and logistics capabilities, click and collect services, digital customer loyalty and payment arrangements, and new and refreshed own-brand products. The industry is in the midst of a customer led revolution, and all of its investment - from new ways of working to sharpening prices – is because customers are demanding it.

3. However, these are testing times. Retail sales growth has consistently been at a low ebb, falling 0.3% in real terms in 2023[2]. Retailers are working ever harder to maintain let alone grow sales at a time of profound structural, economic, and regulatory change for the industry. Retail is currently Scotland's largest private sector employer. However recent data highlighted a drop in the number of posts in the industry as well as a reduction in the number of stores. Meanwhile, profitability has fallen. Embracing these changes and becoming more productive requires retailers to invest in new technology, a higher skilled workforce, revamped stores and warehouses, and transformed logistics capabilities.

OVERALL REFLECTIONS ON BUDGET

[1] Retailers raised £16m for charity and good causes in 2022, SRC Charity Report
[2] SRC-KPMG Scottish Retail Sales Monitor, 9 January 2024

4. With Ministers facing a projected £1bn deficit the SRC advocated[3] for the financial gap to be plugged through cuts to the cost of government and spending restraint, rather than tax increases which could hamper economic recovery. Furthermore, we called for a more competitive tax regime to aid economic growth.

5. What was unveiled was, we understand, a fiscally balanced one-year Budget. However, difficult decisions to make major structural changes to the way the public sector is organised and run, e.g. fewer public bodies or a rescinding of the no compulsory redundancies policy, seem[4] to have been put off or not considered. The Auditor General recently highlighted how the number of civil servants has doubled since devolution, in part due to extra responsibilities for things like social security, yet the Budget implications for headcount remain unclear. All this risks a further fiscal gaps in subsequent years. This, and the consideration being given to a new business rates surtax, leaves a strong feeling that Ministers will be back for more in taxes at the next Scottish Budget and perhaps subsequent ones.

6. There were positives. The freeze to the basic property business rate, which SRC was in the vanguard of championing, will benefit modestly-sized stores. More money for the police might help bear down on spiralling levels of shoplifting. The council tax freeze should support consumer spending, albeit the decisions on income tax - including on thresholds – will impact the money available to spend in shops.

7. However, retail trading conditions remain challenging[5], the cost of doing business is elevated, and the near-term economic outlook is weak. This means retailers have a heightened interest in fiscal measures which either increase or reduce costs. The decision not to blunt any increase to the business rate for medium-sized and larger stores was very disappointing. Frustratingly, thousands of shops continue to pay a higher business rate than applies down south. The proposed new rates surtax was a shock and at odds with promises to "use rates to boost business". It reaffirms the perception that Ministers view business rates as a revenue generator instead of a means of encouraging commercial investment into retail destinations.

8. Measures to mitigate rising costs were insufficient, further cost pressures were added to businesses, and some firms face brand new burdens. Scotland's economy isn't in great shape and the Budget seems set to make things more challenging. Ultimately the solution to the yawning fiscal deficit is through growing Scotland's economy. That requires a vibrant and dynamic private sector. A clear signal is required that economic growth is the priority. A good place to start would be committing to a timetable for lowering the poundage for all to a permanently lower level, faster restoration of the level playing field with England on the higher property rate, and nixing the notion of a new retail-only business rates surtax.

[3] SRC's Scottish Budget recommendations paper, September 2023
[4] SPICe briefing on Budget: "… the Budget contained no details on plans around public service reform, the size of the public sector workforce, or any details on assumptions and policy for public sector pay in 2024-25."
[5] Scottish retail sales fell 2.4% in real terms in December and has fallen in real terms for the past 6 months; shopper footfall fell 2.2% in December and remains a sixth below pre-pandemic levels

DETAILED ANALYSIS

Growth projections

9. Prospects for Scotland's retailers are ultimately determined by the state of the economy and their own ability to adapt and seize on the opportunities that arise. The anaemic predictions from the Scottish Fiscal Commission (SFC) for economic growth over the next few years, down from the previous estimate, are sobering. GDP growth of a smidgen over 1 per cent over the next few years presents a challenge for retailers let alone government revenues and living standards. If we are to see a step change in Scotland's economic fortunes then lifting private sector investment and productivity and supporting consumers becomes even more critical.

Income Tax

10. Real terms retail sales growth has been non-existent of late. Increases in income tax and council tax last Spring took a £250 million bite out of consumer spending. As such we were relieved to see those on modest earnings being protected from increases in income tax rates, which alongside the proposed council tax freeze should support consumer spending. However, the additional 'advanced' band and elevated rates for higher earners adds further complexity to existing income tax rules and makes it potentially more expensive and challenging for employers in Scotland to attract and retain the specialist and senior talent they need. Its important Ministers don't incentivise businesses to locate the highest paid roles and commercial operations outwith Scotland, which will reduce the ability of the private sector to deliver the highly paid jobs and investment we need to grow the economy.

Business Rates

Basic Property Rate

11. SRC was in the vanguard of the campaign to secure a freeze to the Basic Property Rate and we therefore welcome the fact Ministers listened and acted on industry representations[6]. This will protect smaller and modesty-sized shops from rates rises and help keep down costs. It comes as the increase in the National Living Wage is at the top end of what most retailers can swallow, and which itself has added implications for employers' national insurance and pension contributions.

Intermediate & Higher Property Rates

12. Given the nature of some categories of retailing, a high proportion of retailers operate from medium-sized and larger commercial premises. It is deeply disappointing that the rates freeze was not extended to premises liable for the Intermediate Property Rate and Higher Property Rates, where a disproportionally high share of retail employment is concentrated. This will mean 22,120 commercial premises overall (including 4,550 retail stores[7]) will pay considerably more in rates

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[6] SRC co-ordinated a letter from 35 industry bodies calling for a business rates freeze
[7] Ministerial replies to written PQs – S6W-24113 & S6W-24116

from April, a 6.7% rise which is well above current CPI inflation[8] and the biggest yearly rise since 1999. It puts added pressure on those retailers stiving to trade profitably and pushes up the cost of commercial investments which stores up problems for the future.

13. An uplift of this magnitude is at odds with the Scottish Government's pledge[9] to "use business rates to boost business". It could undermine efforts at high street and town centre rejuvenation, more so with some larger town centre and shopping centre stores already at risk due to weak economic growth and changing consumer habits. Once large stores close on a high street it can be challenging to replace them.

14. For these firms their business rate will escalate to a 25-year high, piercing the 50p/50% threshold for the first time since devolution. Indeed, the headline business rate was just 40.7p in the £ at the start of the previous decade, in 2010-11, so a rise to 54.5p and 55.9p respectively in April will be a 34% hike since 2010-11.

15. Over and above this, firms liable for the Higher Property Rate (a slab tax[10]) will continue to pay a higher business rate than competitors or counterparts in England. We are on the cusp of entering the ninth consecutive year of this discrepancy, well past the timeline for restoring parity recommended by the Barclay Review. This higher rate makes it more expensive to operate on our high streets and retail destinations and raises the hurdle for attracting commercial investment. We remain baffled as to why Ministers think firms operating in Scotland are better placed to be stumping up more.

Business rates surtax on shops/Public Health Supplement

16. It is alarming that Ministers are countenancing the introduction an arbitrary Scotland-only Public Health Supplement surtax in an apparently discriminatory approach towards certain larger retailers (ironically often those who have been in the vanguard of initiatives to improve nutrition[11]). The Budget document explicitly says this would be to plug a gap in government finances.

17. If the plan is to regurgitate the approach from 2012-15 then the title 'Public Health Supplement' is a misnomer as the receipts from the previous incarnation of this surcharge went into the Scottish Government's general pot and wasn't ring-fenced or hypothecated for public health. Ministers should be candid about this and end any pretence that this has anything to do with public health when, as the Budget document clearly states, it is about plugging a shortfall in the devolved finances.

18. We have numerous concerns about this retrograde step to introduce an additional tax.

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[8] Scottish Government describes a 5% uplift in council tax would be "above inflation", SG PR, 22 Dec 2023
[9] SG press release 'A fresh start for Scotland', 18 April 2023
[10] The higher rate applies to the full rateable value of a premises
[11] E.g. through labelling, health eating initiatives, funding DrinkAware etc

19. Firstly, the announcement came without warning. This falls well short of the thrust of the New Deal for Business which includes 'no surprises' and the involvement of business at the inception of policy development. A new levy would be an egregious example of a policy taken for revenue-raising purposes with little consideration for those affected. The move has a whiff of a predetermined outcome about it. SRC has played a leading and positive role in the New Deal for Business Group, yet the handling of this proposed new tax falls short of New Deal promises let alone the close collaboration promised as part of the Scottish Government's Retail Industry Leadership Group.

20. Secondly, the introduction of a surtax would breach the SNP manifesto commitment[12] to "ensure that the largest businesses pay the same combined poundage in Scotland as in England"[13]. A levy on one part of the retail sector would contradict the Scottish Government's own Framework For Tax, in particular its principles on engagement, proportionality and certainty, as well as the matrix for tax decision making which includes "proposals being accompanied by a policy costing". It would contradict the Framework's pledge to maintain "competitive" non-domestic rates.

21. Thirdly, regurgitating a policy from a dozen years ago doesn't take account of changed circumstances. The nature of the retail market has changed significantly in recent years, with competition intensifying and a greater prevalence of online shopping[14] and less shopper footfall. Also, government-mandated costs are higher now. For example, the business rate is decidedly more onerous now – 45p[15] in the £ in 2012-13 but 55.9p in the £ from April 2024 (for shops liable for HPR) - so a tax rate more than a fifth higher. Over and above this the Apprenticeship Levy has been introduced in recent years.

22. Fourthly, shackling stores with a new levy could hinder rather than help retailers' ability to keep down shop prices. At this juncture and without any detail of the proposal it is too early to say for sure what the impact may be on prices at tills, however if grocery shop prices were to rise that would be most keenly felt by lower income households who spend proportionally more on groceries. A levy would add to the cost of operating for those retailers that provide such a significant share of retail employment and investment, and low-cost essentials for customers. Ultimately, the cost of operating a retail business is borne by consumers.

23. A new surtax would come on top of an already onerous rates burden. As mentioned above, for many firms the business rate will rise to a 25-year high this Spring. Many already pay more than comparable premises down south[16]. A new levy would be

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[12] P47 of SNP's 2021 election manifesto
[13] The Framework For tax reaffirms the SNP manifesto to ensure that the largest businesses pay the same combined poundage in Scotland as in England
[14] The proportion of non-food items bought online (penetration rate) was 15% at the start of 2013 and 35% in the final months of 2023, SRC-KPMG Scottish retail sales monitor
[15] Scottish Parliament written answer S6W-21205
[16] 2,410 shops will be liable for the Higher Property Rate in 2024-25, S6W-24113

wholly at odds with the Scottish Government's pledge to 'maintain a competitive non-domestic rates regime' and to 'use business rates to boost business'. Furthermore, a Scotland-only levy would go against the thrust of the Barclay Review which was about minimising complexity and ensuring predictability and competitiveness in the rates system.

24. A new levy is a recipe for self-inflicted economic harm. As highlighted previously[17], investment in retailers' research and development expenditure in Scotland fell when the previous incarnation of the Public Health Supplement was in place in 2012-15. A new levy will make it more expensive for retail businesses to operate in Scotland and who often have to compete with other parts of the UK for increasingly mobile capital.

25. The Budget document explicitly says the purpose of a new levy would be to raise extra tax revenue. This would be more persuasive if a greater emphasis had been placed on cutting the cost of running government. The Scottish Government's Spending Review eighteen months ago identified a total of 129 public bodies under its purview.

26. In terms of the wider economy, this arbitrary move sends a message about the predictability or otherwise of devolved policy making on tax. Businesses make long term investment decisions based on the costs of operating and the predictability of tax and regulatory decisions. A shift to a more ad hoc and less predictable approach towards levying taxes aimed at specific sectors rings alarm bells. It could well affect commercial decisions and make economic recovery more arduous. Even when the previous public health supplement eventually ended it was followed shortly afterwards by a doubling of the then large business rates supplement (now higher property rate), and which is set to be higher than the rate applied down south for a ninth consecutive year.

27. A new levy on grocers' smacks of incoherent policy making within government, and not just between Finance/Treasury and Economy departments. Other Ministers are currently looking to grocers for help to implement new regulatory measures including in-store restrictions on alcohol marketing, curbs on selling products high in salt and sugar, and a likely rise in alcohol minimum unit pricing. This move comes mere months after the deposit return scheme farrago left grocers nursing a bill for tens of millions of pounds.

28. A new rates levy conceivably risks unintended consequences, especially if those firms affected sought to put under the microscope existing investment programmes. For example, larger grocery retailers make significant investments through local buying teams and support for organisations like Scotland Food & Drink to find and help new products come to market.

[17] What's Next – The Future of Scottish Retail, SRC, April 2017

29. A surtax could well have consequences for the state of our town centres. Escalating rates bills even further could undermine support at future ballots for business improvement districts (BIDs). Many of the stores affected by a surtax are likely to already be liable for the Higher Property Rate as well as a BID levy. A surtax could incentivise affected retailers to take a sterner line in votes on new or renewed BIDs, which are usually funded by a surcharge on the business rate.

30. Shop staff themselves may not be immune from the impact of any new surtax. Staff bonuses at some retailers are dependent on the 'profit and loss' performance of their own individual store.

31. At this precise moment it is unclear how developed the government's thinking on all this is. We don't know the scope of the proposed levy, who it might apply to, how it might work, how much affected retailers would be expected to stump up, whether it would come on top of the higher property rate, whether it would be a slab tax like the higher property rate, how long it would apply for, nor why retail has been singled out.

32. Indeed, if the state of the devolved public finances turns out to be worse than feared then presumably it opens the door to a widening of the scope of the surtax to capture smaller retailers, and/or even higher tax rates being applied, or other economic sectors out-with retail being similarly targeted.

Retail, Hospitality & Leisure sectors' rates relief (RHL relief)

33. The decision not to follow Wales and England on temporary rates relief for the coming financial year for retail, hospitality, and leisure sectors is a regrettable omission, more so as we understand Barnett Consequentials were forthcoming from a decision to award relief down south. Scottish stores have already missed out on eighteen months of relief which has been available to counterparts in Wales and England. Retailers missing out on RHL relief, together with the 2,410 shops liable for the Higher Property Rate, are paying more in business rates than counterparts down south.

Flexible Workforce Development Fund (FWDF)

34. Our understanding from media reports is that the FWDF has been axed. This presents a blow to beneficiaries including those retailers of scale operating in Scotland who pay the Apprenticeship Levy but will now find they cannot access any of the FWDF. With skills provision being one of the keys to driving productivity growth and consequently economic growth it would be disappointing to see this cut and spend on skills development supressed at a time when retailers' taxes are increasing.

Scottish Retail Consortium
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