The Special Interest Group of Municipal Authorities (Outside London)

SIGOMA response to the Business Rates Reform consultation

1. About SIGOMA

1.1. SIGOMA represent metropolitan and unitary authorities outside London, from the Southern Ports, the East Midlands, West Midlands, North West, North East and Yorkshire & Humberside. The 47 SIGOMA Councils are home to 13.8 million people, 24.9% of the English population.

1.2. Our authorities typically represent areas that have suffered most during post-industrial decline and many have struggled to rebuild local centres of trade to replace the heavy industry on which the country was built. Some members feel that central government has no plans or aspirations for local government beyond the currently thriving parts of the country.

1.3. Business rates retention is a prime example of this approach. The Minister refers to increased rates retention as offering a powerful incentive to grow and invest their local economies. But the same levels of growth do not offer the same incentive for all parts of the country due to their historic rates bases.

1.4. Consider the following table which shows the impact of a 1.5% business rates growth against the funding needs of different authority types.

Varying impact of Business Rate Growth

	Value of a 1.5% increase £million	Value of increase as % of needs
Metroplitan districts	28.77	1.0%
Shire districts	44.82	8.4%
Counties	10.57	0.4%
Unitary authorities	33.48	1.4%
London authorities	35.91	1.7%
GLA	23.94	2.4%

1.5. The concerns of our members for the trend in increased rate retention focus around the disparities between the needs of the communities we serve and the relative levels of taxation that can be raised and grown locally.

1.6. Whilst all authorities would aspire to be self-reliant in terms of local fund raising to finance needs, for many this is not possible. This is the case for the great majority of our members.

1.7. Given the current state of local authority finance as a whole, where the LGA estimate a funding gap of £3 billion, there seems to be little scope for rewarding growth in local taxation for one group of authorities, without cutting below needs-based allocations to others.

1.8. Although the 47 SIGOMA Councils represent 25% of the country's population

- They earned only 19% of England's net business rates in 2017-18[1]
- They earned only 20% of England's Council Tax in the same year

yet at the same time

- 34% of all family households claiming benefits are from SIGOMA authorities
- The morbidity rate in old age is higher for SIGOMA authorities than the rest of the country. 43 out of 46 SIGOMA authority populations had a shorter healthy life expectancy at age 65 than the national average.
- Child protection enquiries are increasing 11% faster in SIGOMA areas than the English Average (2012-2017).
- Using MHCLG's own preferred measure of core spending power (CSP) it is clear that the poorer authorities we represent have borne the greatest burden of cuts to funding.

1.9. Government must understand the potential risk that business rate growth retention presents to some of our members, that they will be given less funds than are essential to preserve services whilst other authorities will earn more. The "risk" that government discuss placing with authorities is actually a risk for their residents, the risk that in some parts of the country services will fail whilst in other areas they will not only survive, but thrive.

1.10. Government must consider how to make growth in business rates an equal opportunity for all and must ensure a Fair Funding formula that provides adequate needs funding for all authorities, as the primary aim.

Q1: Do you prefer a partial re-set a phased re-set or a combination of the two?
Q2: Please comment on why you think a partial/ phased re set is more desirable?
Q3 What is the optimal time for your preferred re set type?

2. Re set.

2.1. Despite our being only 12 months away from the introduction of 75% retention, government have not indicated the levels of partial re-set they would consider appropriate nor (other than in illustration) the number of years of phased re-sets

[1] From MHCLG rates drop down 2018, ignores levy and safety net includes s31

2.2. It is also unclear under phased re-sets what length of time there would be between recalculating needs formula.

2.3. The existing 50% retention scheme has already created large disparities in funding due to rate retention growth, which are not identified in core spending power tables.

2.4. Over the 5 years to 2018-19 we calculate that the <u>average annual</u> percentage added to Core Spending Power by rate retention growth is:

Authority type	Additional CSP %
London authorities	1.7%
The GLA	1.8%
Combined London authorities	1.8%
Shire Districts	7.1%
Shire Counties	0.6%
Combined shire authorities	1.6%
Unitary authorities	1.5%
Metropolitan Districts	1.1%
SIGOMA Mets & Unitary Authorities	1.3%

2.5. These percentages may appear close but a 0.5% difference for metropolitan authorities equates to £237 million over the 5 year period; it will be remembered that this is after charging levy to the highest gainers. In addition many of those in receipt of growth funds have received transition relief, rural services top up and refunds of “negative RSG”. The system is not “joined up” to other funding decisions.

2.6. Over the six years to 2018-19 over £3.8 billion has be allocated, not according to needs, but to those with the highest rate base and the highest growth.

2.7. Most of our members view this proposal in the context of an inadequate overall funding total with no assurance that this will improve and therefore consider any proposal that reduces or defers a needs based distribution as an obstacle to essential service delivery. Many ask what other Government services are delivered according to the prosperity of their local area? If the future quantum were higher (or even known) our answer might differ.

2.8. Therefore the requirement for a regular review of needs should be one of the main factors in the decision on the length of re-sets and we do not consider a triennial re-evaluation unreasonable, in line with revaluation if that was administratively advantageous.

2.9. It is worth noting that, in discussing this issue within working groups, authorities that support greater retention percentages under partial re-set, argue that a lower percentage would not make it “worth their while”. They, and we believe MHCLG, do not appreciate that this is the position that many of our top up authorities find themselves in <u>already</u>. Rate growth does not contribute significantly to their needs and the small proportion they gain from rates growth is lost on a share of the national growth on a needs basis. Extending growth retention works against them.

2.10. To address this disparity MHCLG should use this consultation as an opportunity to consider enhanced growth shares for authorities with a low rates gearing.

2.11. Asking authorities to choose between the options offered without details of percentages and length of time is unreasonable

2.12. Under partial re set the illustrated time to a full re-set of 15 years is too long. We would recommend no more than 10 with a partial retention of no more than 10% at three yearly intervals.

2.13. Under phased re-sets we would support a rolling retention period of no more than 3 years, given that it appears there would never be a full re set.

Q4: Do you have any comment on the proposed approach to safety net?

3. Safety net

3.1. The consultation combines this section with a comment on Levy.

3.2. The combined proposal on levy and safety net is one of the more objectionable proposals in the consultation from the stand point of top-up authorities.

3.3. Levy and safety net are both measured in relation to their impact of rate change on funding baseline.

3.4. The message to most of our members is that highly geared authorities will be allowed to retain growth without (or almost without) limit but that if they experience decline our members will be asked to support their funding needs.

3.5. Put simply, highly gear authorities would get most of the reward and limited risk, finance by those with little prospect of significant growth in baseline funding.

3.6. The current mechanism has at least the merit that those most likely to need safety net are also most likely to pay levy

3.7. Our members therefore support a levy and safety net mechanism that is self-financing and do not support raising the safety net to 95% or more, unless this is matched by an appropriate policy on levy.

3.8. Regarding the proposed top slice of rates, for the avoidance of doubt, we would only support a top slice that is borne in proportion to rate base (i.e. not one that is topsliced from rates total before the calculation of funding baselines).

3.9. It should be noted that the consultation also includes a proposal for pooling of appeals. Under those proposals it is less likely that an authority would find itself requiring safety net support, in effect supporting the governments' proposal.

Q5: Do you agree with the approach to Levy?
Q6: If so what do you consider to be an appropriate level at which to classify growth as extraordinary?

4. The Levy

4.1. In addition to the following please see our comments on Levy within the response on safety net.

4.2. The consultation on this section begins with a discussion of growth in terms of extraordinary behaviours by the authority, for example manipulating accounting provisions to generate a desired rate retention figure,

4.3. We agree that what has been called "gaming" of the system presents a challenge that MHCLG needs to address, independently of the levy calculation.

4.4. The paper seems to then move on and discuss general limits for the application of levy i.e.

- The level at which levy should apply
- The rate of levy that should apply

4.5. Levy was a key mechanism of fairness to limit the disparity in income between high tax base authorities and low tax base ones.

4.6. Relaxing levy will have the effect of increasing the funding gap between high and low tax base authorities, whilst infrastructure investment is heavily focussed in high rate income areas.

4.7. At the same time government intend to use the funds of all authorities as a safety net if high tax base authorities experience decline in their rate base.

4.8. SIGOMA supports the continuation of levy both as a funding source for safety net and as a means of equalising the benefit of national growth on a more even basis, relative to needs.

4.9. For example levy on high earning authorities could be used to add to the growth retention shares of low rate base authorities, offering them a real incentive to grow

4.10. We consider the current Levy mechanism which applies the proportion of growth in rates to the proportion of growth in funding to be fair.

4.11. The level above which levy is calculated should continue to be calculated by reference to funding baseline and should be between 50% and 75% of funding baseline.

4.12. We agree a capping rate of 100% above the level. If a higher capping rate is selected we suggest a taper rate from a 0 to the 100% rate.

Q7: What fall-back position should there be for the national tier split between counties and districts, should these authorities be unable to reach an agreement
Q8 Should a two tier area be able to set their tier splits locally.

5. Tier splits

5.1. Whilst we have no view on what the splits should be we feel bound to draw attention to the arbitrary nature of the rate retention mechanism and the mismatch between needs and income from business rates this has caused between two tier authorities.

5.2. Instead of being available where it is currently most needed in the most pressured care services, surplus funds have been directed towards lower tier areas who have thus not faced the cuts that lower tier services in single tier authorities have undergone.

5.3. What is true between the tiers of two tier areas is also true about rate retention as whole across the country**.**

What fiscally neutral measures could be used to incentivise pooling within the reformed system?

6. Pooling incentives

6.1. Within working groups there has been a mixed response to this issue and the fact that this consultation is presented with no proposals suggests that despite discussions in the group there is no clear idea of how pooling can be encouraged without financial incentives.

6.2. Authorities who are minded to act cooperatively will do so but many smaller councils are resistant to actions that may reduce their local autonomy and limit their capacity to absorb cuts at authority level.

6.3. Authorities might also feel more inclined to pool if they felt their regions were getting a good offer out of the rate retention mechanism but many feel they do not and that pooling limits their access to national growth.

Q10: Hereditaments to be added to the central list?
Q11: Hereditaments to be added to the local list?

7. Central List

7.1. Members have the general view that the central list items should be kept to a minimum on the principle that the treatment of central list income is not disclosed and we have been unable to obtain a clear statement from MHCLG on this issue.

7.2. An impression has been obtained possibly unfairly that MHCLG rely on assurances from HM Treasury that central list funds are used for local government purposes.

7.3. Therefore any item that can be transferred to the local lists will at least clearly form part of local authority funding and form part of the total at re-set.

7.4. Our colleagues in other authorities have suggested that railway stations and adjacent related hereditaments should be transferred to the local list and we support them in this suggestion.

Q 12 Do you agree that the use of a proxy provides an appropriate mechanism to calculate the compensation due to local authorities to losses resulting from valuation change?

8. Appeal losses

8.1. Nothing exemplifies the extreme complications of business rate retention more than the problems surrounding revaluation, appeals, appeals provisions and adjustments to rate retention.

8.2. We have worked with colleagues in the rates groups to address this issue and, like many others, have been disappointed at the lack of capacity in the Valuation Office Agency to accommodate the changes necessary to provide Councils, who pay for their services, with the information necessary to calculate this adjustment from data rather than an estimate.

8.3. From our member’s comments, the VOA appear inflexible in adapting their systems so as to provide information in a way that is useful to us. Many of our members have been incredulous when the reasons for the proxy are explained.

8.4. As well as the accounting issues outlined in 3.3.6 of the consultation the pooling proposal faces a number of other obstacles. For example:

- How would the topslice, which would underpin the pool, be calculated and on what property values?
- How would the proxy (and the compensation amount) deal with hereditaments which came into being between lists and had an appeal against their starting valuation.
- How to equitably deal with a starting position on appeal provisions

8.5. To describe the proxy as appropriate therefore is to overstate members enthusiasm for the measure.

8.6. Members are firmly of the view that VOA should be required to adapt their systems to the requirements of MHCLG and councils.

8.7. However, all members of the working group seem resigned to using this measure in the absence of any practical alternative, on the basis that some measure is necessary unless, as indicated by MHCLG, the reforms referred to in question 13 are implemented.

Q13: Do you believe that Government should implement the proposed reform to the administration of the business rates system?

8.8. Members are broadly supportive of the principles behind the reforms which have been recommended by the sector as a partial solution to the complications that have arisen from the business rate retention system.

8.9. Members perceive this as a reform that should add stability to the settlement system, allowing authorities to forecast in advance shares from business rates without the pressure that forecasting business rates in January will determine the following years' net revenue

8.10. Members also believe the reforms offer Government a chance to:

- Place needs at the centre of the business rate retention mechanism, ensuring that every authority begins with the funds necessary to deliver services
- Finesse the growth retention mechanism so as to present equivalent incentive to top-up and tariff authorities alike.
- Consider alternatives to rates growth incentives that would synergise with authority wider economic aims around employment and growth that are not focussed purely on traditional high street and out of town retail developments.
- Remove the ability of authorities to game the retention mechanism through provisions

8.11. Hence the reform has support, but members believe that there is a huge amount of work necessary to implement the reform in the short time available and urge MHCLG to begin the necessary further detailed work at once, explaining through the working groups the detailed proposals.

Q14: What are your views on the approach to resetting Business Rates Baselines?

9. Re setting baselines

9.1. The outcomes of this process will have an equal impact on the net revenues of authorities to the setting of the formula shares in Fair Funding.

9.2. We agree that estimates for non-collection and appeals will present a challenge and will have a number of potential alternative approaches rather than a single "right" one.

9.3. We suggest that setting the baseline would still be important under the alternative system, as this would be used to calculate “growth” in the reward element of the system

9.4. For a non-collection estimate we would recommend an average going back to the 2017 revaluation. Members also point out that collection rates tend to vary between relatively deprived areas and others. So for example the collection rate for metropolitan districts has been a consistent 1% below the national average over 2012-13 to 2016-17

9.5. Appeals are a more complex issue.

9.6. The aim is to measure actual income each year against the set baseline, to measure growth.

9.7. If the proposal in this section to create a pooling mechanism for appeals is successful, authorities will avoid the direct cost of the huge majority of appeals from 2020-21, which result from a re-assessment by the VOA.

9.8. Instead all authorities will pay a top slice based on their annual rate value against which they will claim if an appeal is successful

9.9. We suggest that the top-slice percentage should also be applied to baseline rates for each authority.

9.10. When measuring actual income in succeeding years rate retention calculations, authorities would then ignore or remove appeal provisions in their returns and in time would claim against the pool for successful appeals, or re-introduce unsuccessful appeals as income. In either event the authority does not suffer the impact of the appeal on a backdated 2020 list item as a revenue impact, only the value of their pool contribution.

9.11. There would be some accounting issues connected with this that would need resolving to ensure the authority could take the correct amount of income into revenue reserves but difficulties could be overcome by adjustments between top up and tariffs and the pool contribution fund.

9.12. All the above is true for VOA errors only. A small adjustment would be required for appeals which are not a fault of the VOA.

9.13. If the alternative reformed system is implemented the methodology will be different.

9.14. Under this method measurement of growth is separated from top up and tariff. Due to the lag in the system it will be possible to adjust baseline for the retrospective impact of appeals and measure true growth (or decline)

9.15. The system effectively results in a pooling of appeal estimates with the authority bearing the impact of an over/under provision. Some members are of the view that with a system annually balanced to needs and with growth being retrospectively calculated it may be simpler to exclude appeals from the baseline entirely and allow authorities to measure growth against a baseline adjusted to take into account new appeals, this would need financing out of an appeals pool and thus require a pool of finance, as suggested in section 3.3.

9.16. There remains the more difficult issue of arrears of appeals relating to 2019-20 and earlier and of potential appeals against rate charges of 2019-20 and prior which have not yet materialised.

9.17. Due to the disparity of provisions within local government, sometimes dictated by auditors, Government should seek a way to put authorities on an equal footing at the start of the re set period.

9.18. We will continue to work with colleagues in the working groups on this issue.

Q: 15 Do you have any comments on the potential impact of the proposals outlined in this consultation on persons who share a protected characteristic?

10. Protected persons

10.1. It will come as no surprise that we view the business rate retention proposal as one that, under the current level of funding, removes much needed funded from people who reside in poor areas and with high needs and tends to place those funds where they are less urgently required.

10.2. Under different circumstances and a less narrow measure, our members would support the retention of greater portions of locally raised income.

10.3. As it is, they wish us to remind Government that Business Rates are a tax, not a charge for services, and as such need to be placed where they are most urgently needed in this 10th year of austerity.