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100% Retention of Business Rates and the Fair Funding Review

Dear Stuart, Sarah and Chris,

This is a joint letter from the Society of County Treasurers (SCT) and the Society of District Council Treasurers (SDCT). Together, these authorities represent 46% of the population of England and provide services across 87% of its land area.

Both the societies will be responding individually to the consultation on 100% business rates retention but given the commonality of our geography and demography we felt there might be some benefit from an early letter outlining what we see as the broad issues. The two societies already have good links with both the LGA and DCLG and we hope this letter might help shape further discussions over the consultation period. We recognise the huge shift in funding that the move to 100% rates retention represents and want to ensure that shire areas are well placed to take full advantage of the potential benefits.

Both societies are represented on the Steering Group as well as at the working groups. The links between the groups is evident to see; hence many of our answers will be predicated on decisions elsewhere. For example, considerations about what appropriate protection could be provided by the safety net will be affected by the levels of risk in the system – either in terms of sufficiency of funding, demographic growth, revaluations, reset periods or the national economy.

Given the interplay between the work streams, the SCT and SDCT members have agreed a set of principles that we feel should govern the way this work is approached:

- Unfunded pressures must be the first call on the quantum; this is particularly important given the pressure on social care budgets and the impact on the NHS. Similarly new burdens must also be properly funded.
- Local government must facilitate healthy local economies and drive business growth in order to reap the benefits of business rates retention
- The new funding system must be focussed on the needs of our residents; starting with a relevant per capita basis and taking all funding streams into account
- The local government sector must fully engage with the consultation and review process in order to create a system which can be tailored to local needs and opportunities.
- There must be transitional arrangements in place to enable a smooth shift to the new system and to assist planning.

Irrespective of the final distribution of Business Rates there is clearly a link between the ability of an area to generate future business rate growth and the existing strategic infrastructure and capital investment streams. Shire areas have frequently been disadvantaged in this area; with Government investment historically favouring large cities.

Both the districts and the counties in shire areas invest for economic growth. This needs to be accompanied by further investment in our infrastructure from Government for areas to achieve their full potential.

Complexity
The current 50% scheme is complex, and is made more so by concessions made to businesses since its introduction (capped multipliers, temporary and then permanent doubling of small business rate relief). On top of these complexities and their accompanying compensation grants, there are other features such as Enterprise Zones, renewable energy projects and safety nets which have made the system unwieldy in a very short period.

In addition to this complexity at a national level; the current system of tariffs and top-ups creates an environment where there is a huge spectrum of risks & rewards between individual authorities. Those authorities with large top-ups will see little benefit of economic growth in their budgets whilst conversely not seeing the impact of a declining tax base. At the other end of the spectrum, made even starker by the removal of levies, there are small authorities with a huge financial incentive to grow but also a massive penalty for decline. With decisions still to be made about the level and operation of the safety net, these small authorities must be feeling very vulnerable and exposed.

At the time that the current system was being initiated ministers took the decision to protect social care-providing authorities. Hence, all upper-tier and some single tier social care providing authorities are insulated from decline in their area; but not all social care authorities receive the same degree of protection. The same is true for planning authorities who are said to control the “levers of growth” – the incentives (and consequential risks) vary between authorities.

It is against this background that the new system is being introduced, and already it is clear that it will be even more complex; we are witnessing a number of devolution deals being agreed with what we refer to as “asymmetrical devolution” – meaning different services being devolved in different areas. In addition, the Department is agreeing a number of pilots of the new 100% retention system. The SCT and SDCT consider it vital to increase the transparency of these pilots, including any impact on the quantum. The two societies believe it is important that we capture learning from these pilots, but also seek assurance that these pilots will not impact on the total quantum to be distributed alongside additional responsibilities. It would be inequitable for funds to be allocated to areas that are given pilot status, with the result that there is a reduced amount of remaining funds for all other authorities.

Alongside these two consultations the department is also considering whether to introduce more frequent revaluations. Given that local authorities, under the current business rates system, have never yet experienced a revaluation it is difficult to quantify the turbulence and shifts that might occur at such a time. If the result of this consultation is that revaluations do become more frequent this is likely to become an even greater issue.

Whilst the aims of the system appear relatively simple; to fund local services whilst creating an incentive for local economic growth, all of these issues mean that the mechanics of the future system will certainly be complex. The SCT and SDCT ask that civil servants and ministers recognise this but also aim not to add to this complexity.

The Quantum
Current forecasts of the "quantum", the additional amount available for redistribution, range from an additional £11-15bn. The current economic environment is very uncertain and this, together with increasing levels of risk in service delivery is in danger of being "locked" into the business rates retention scheme.

With all the current uncertainty surrounding the recent decision to leave the EU, as well as the change of leadership at number 10 and the rest of cabinet, it would seem prudent for these forecasts to be revised, reflecting the consensus that we are entering into a period of reduced growth compared to that forecast prior to the 23 June. This revision will also need to take into account the current push to convert more maintained schools into academies, which as charities are exempt from 80% of their rates bill, as well as the threat of legal action from NHS trusts who consider they are eligible for reliefs from business rates.

The consultation paper in question quotes £12.5bn additional quantum, please can the basis for this forecast be shared with local authorities. To aid the work going forward, it is important that there is transparency regarding the calculation of the quantum, including a clear statement of the assumptions regarding growth and inflation.

The Societies note that the quantum has already been top-sliced for Transport for London (TfL); this is a national income stream and top-slicing in this way will see residents in one part of the country immediately at an advantage over their fellow citizens. Funding for TfL should have been secured from elsewhere.

New Responsibilities
The Needs and Responsibilities workstream is looking at what services or grants could be transferred to local government to be netted off against the quantum.

Each society will respond more fully to the consultation questions regarding new responsibilities in our respective responses but both wish to highlight now that many of the suggested "new responsibilities" are, in fact, not new responsibilities at all. They merely represent a change of funding stream from specific grant to business rates.

The recent House of Commons CLG Committee Interim Report on this issue set out some principles on which decisions on new responsibilities should be based including giving local government genuine discretion over how services are provided. The report also suggested that responsibilities should be linked to economic growth such as skills and transport.

The SCT and SDCT agree with this approach and want to see powers devolved to them that really are new and that fit appropriately with funding coming from business rates. For example; growth funds, skills and higher education, infrastructure funding and transport investment. Local government want to be able to control their budgets properly in a way that can make a difference locally; not simply administer a benefit or continue providing a service that used to be funded via a specific grant.

Local Resources
Currently a proportion of a local authority's budget is financed by council tax. This proportion ranges between individual authorities and there can be many reasons for this difference. Over the last decade and a half the Government have continually carried out what is referred to as "resource

equalisation", the result of which has always been to penalise those authorities with large tax bases. The resulting inequalities across the country are stark.

Despite many shire residents working in cities and metropolitan areas, according to the Annual Survey of Hours and Earnings (ASHE), wages for residents in shire areas are generally 11% lower than the national average. Yet the average adult living in a shire area will pay over 5.6% more towards the costs of services through their council tax.

When compared to London, residents living in shire areas earn, on average, 20% less. However, residents in London pay 4% less in council tax than those in the less affluent shires.

Despite wages in shire areas being, on average, 11% higher than metropolitan authorities, the shire residents pay almost 30% more in council tax.

Although less easily quantifiable, it is generally accepted that residents in shire, and often rural, areas will tend to receive less services (either through removal of service or reduced hours) as well as travel further to reach them.

When council tax was introduced it was intended to be related to wealth. It was therefore based on property values because, at the time, it was felt this was a suitable proxy for wealth. However, almost 30 years since the last revaluation, it is indisputable that residents in shire areas are paying more than any other class of authority for their services. This is not because shire areas are less efficient, but because the proportion of central funding is less, and therefore a larger element of funding has to be met locally. This is inequitable in terms of affordability for the 46% of the population who live in shire areas and contribute to the economy.

In the interests of fairness and transparency, we firmly believe that this issue needs to be discussed openly and addressed as part of the BRR work. Council tax makes up a considerable element of local authority budgets and ignoring the current inequality risks undermining the whole process. In our view, the 100% retention of Business Rates cannot be viewed in isolation from funding through council tax and it is not tenable for the Department to state that these will not be considered.

Funding the Current Pressures

Both Societies feel very strongly that before new areas of responsibility are devolved, there must be some accommodation to meet unfunded current pressures which are considerable. These have arisen and will continue to arise from the reductions in central government funding, and the increase in demographic growth. Evidence was provided after the provisional settlement of the impact of these pressures going forward.

There are complex interdependencies between the NHS and local authority services and finances – where one service is underfunded there is the potential for devastating consequences in the NHS; some of which are becoming more visible recently.

At the 2016-17 Settlement the DCLG introduced a new measure called Core Spending Power; this includes:

- The Settlement Funding Assessment,
- Council tax requirement including the Adult Social Care precept and £5 flexibility,
- New Homes Bonus
- Rural Services Delivery grant, and
- Transitional grant (introduced between provisional and final settlement for 2 years)

From 2017-18 the Core Spending Power (CSP) will also include the Improved Better Care fund.

Whilst neither society supports the use of the CSP figure as a transparent way of communicating the pressures to residents we accept that it has become the Government's preferred way of summarising grant settlements. It is for this reason that we have used it to illustrate the funding discrepancies.

In 2016-17 residents of all ages in shire areas received £741.70 per head of CSP funding; this is 6% less than the national average; 5% less than metropolitan districts and 24% less than residents in London. Ministers are also keen on showing figures by dwellings; in which case shire areas receive 7% less than the national average; 6% less than metropolitan districts and 31% less than London.

As explained above this CSP figure includes the council tax which we have already shown to be unfair for shire residents. If you strip out the element of the CSP for council tax the differences become starker. Individual residents in shire areas receive, on average, 20% less than the national average; 33% less than metropolitan residents and over 46% less than residents in London. When number of dwellings replaces the resident population shire areas receive less than half that of London.

The members of the need and redistribution working groups have agreed on the importance of getting the ASC funding right. For SCT members this makes up the biggest proportion of budgets after education. The proportion of the population aged over 85 in shire areas is forecast to double in the next 20 years – this is the fastest growth in ageing of all authorities. Those aged over 65 is set to grow from 20% of the population in 2016 to well over a quarter of all residents by 2036. Only London is forecast to see a greater rate of growth of over 65s by 2036, however they remain a low proportion of the resident population at just over 15%.

For Shire Districts, the highest proportion of funding goes on Waste collection and recycling, Planning and Building Control and Leisure and Open Spaces. These are services which touch on the lives of every resident. Not only can Planning services contribute to the growth agenda, ensuring both housing and business growth occurs in a sustainable way but these are all services which contribute to the wider health preventative measures and which residents see as essential. Leisure and open spaces whilst a totally discretionary service, plays a significant role in both the physical and mental well-being of the population and reduces pressure on NHS services.

Before any further services are devolved there must be assurance that these pressures will be adequately recognised by the new Fair Funding formula but also fully funded past the baseline year. In many cases there is little or no correlation between demand for services and economic prosperity.

If the issue of unfunded pressures is not addressed soon, the impact on the NHS will grow. Already we are seeing an increase in delayed discharges. The recent NAO report on this issue highlighted that there has been a 31% increase in bed days taken up due to delayed transfers. The amount of people waiting for a package of homecare over the last two years has increased by 100% and the amount waiting for a nursing home placement has increased by 63%. There are still 2 more years of very significant reductions to RSG before the new BRR system is introduced. Without some additional injection of cash to the social care system, the impact on the NHS will worsen considerably and it would seem opportune to allocate some of the quantum against this heading to allow care to be provided in the care sector which is considerably cheaper than that provided by the NHS

Flexibility
Currently local government are able to vary the council tax precept they set locally. This is done openly through each Council by elected members who are subject to re-election every 4 years. The introduction of freeze grants and referendum limits have diluted this in recent years but the link still remains that locally raised taxes can be increased to fund services or decreased to reflect local decision making.

The SCT and SDCT believe that this level of flexibility and accountability with regard to business rates should be introduced; not just in areas with an elected mayor. The current proposal to allow local authorities to reduce the multiplier sees no further devolution of powers than those already laid out in the Localism Act. Even in areas with an elected mayor will only be allowed to increase rates if they have agreement from business and the additional funding is to be spent on infrastructure.

If Business Rates really are replacing Revenue Support Grant (RSG) as one of the primary means of funding local services then local authorities need the power to spend their additional income without restrictions. RSG was used for the totality of the budgets; so business rates, even additional rates as a result of an increased multiplier, should come with the same freedoms.

As the proposals currently stand there will be an inequitable impact on councils without directly elected mayors and on the associated service provision for the residents in these areas. Given this, we believe freedom to increase business rates should apply to all. We request to see the Equalities Impact Statement accompanying this decision to limit flexibility.

Our members also request that the Government removes the mandatory discounts applied to both the council tax (i.e. single person discount) and business rates. Given the pressures that local services are under, current burdens will need to be the first call on the new quantum but it will also be necessary for local authorities to be able to exercise genuine flexibility on their income streams.

In some services the rigid legislation means that local authorities are not able to tailor the services provided to meet the needs of their populations. Being able to vary the eligibility or statutory requirement for services would increase control over budgets too.

Funding Assessment
We support these two consultations being published in conjunction with each other as the issues of need and resourcing are so closely linked. It is critical that both systems are fit for purpose but they must also work alongside each other. In theory it is possible to match need and resources in the baseline year but the result will be varying levels of risks/rewards. As time goes on and we begin to see revaluations and partial resets and then possible further alterations to the system of mandatory reliefs not to mention demographic growth, need and resources are very likely to diverge. The two societies are very keen to ensure that this doesn't happen – that services are always fully funded and turbulence in the system can be minimised.

The current funding baseline is based on a discredited system of thresholds, scaling and ministerial discretion. The underlying need formula only serves to lock in the past patterns of over/underfunding by regressing to past spend and/or activity. The SCT and SDCT want to see all local authorities start from an equal position where need is funded through agreed cost drivers and not past funding.

We hope you have found this letter helpful. We believe it is right that we set out at this stage some of the high level principles that we believe should be adopted going forward. We do appreciate the openness and collaborative nature that the Department and the LGA have adopted in working with all colleagues, and look forward to continuing that way of working going forward.

Yours sincerely

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