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Business Rates Retention Consultation
Local Government Finance
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Self-sufficient local government: 100% Business Rates Retention Consultation – Response from Solent Local Enterprise Partnership (LEP)

The Solent LEP is a partnership organisation between the business community, the Higher Education sector, three unitary authorities, eight district councils and one county council, all of whom are actively working together to secure a more prosperous and sustainable future for the Solent area. LEPs have assumed a strategic role as the lead bodies for economic development in their areas. Accordingly, the Solent LEP is the key interface and lead for economic development in the Solent, and has set out its evidence-based strategy to deliver transformational economic growth within the area in its Strategic Economic Plan (SEP), published in 2014.

With a population of more than 1.3 million (2011) and more than 50,000 businesses, the Solent Local Enterprise Partnership (LEP) area is an internationally-recognised economic hub anchored around the Isle of Wight, the two cities of Portsmouth and Southampton, the M27 corridor and the Solent waterway. Solent also has immense natural advantages supported by strengths in key economic sectors, world-class universities, a strong base of high quality Further Education (FE) colleges, renowned heritage, countryside and coastline, and excellent global transport links by air and sea. The Solent is bordered by two national parks and its natural geography comprises three islands and two peninsulas. The mainland Solent LEP area is also the most urbanised area in the South of England, outside of London. It therefore has a complex geography, which, whilst giving the area its unique character, provides both opportunities and challenges with regard to local economic growth.

Our responses to the individual consultation questions follow, but Solent LEP would first like to raise a few key issues as follows.

A. The Business Rates System – The need for reform

There are well documented concerns from business ratepayers that business rates are in need of major reform to make them fit for purpose for the modern economy. The consultation sets out that the business rates system should provide stable and sustainable revenues to fund public services going forward and it should also under pin a system of self-sufficient local government. There is an on going debate about whether the tax itself is sustainable, fairly targeted and sufficiently responsive to both the changing patterns of property usage and the conditions in the wider economy. Key issues include:

- The burden of business rates on certain sectors, particularly SME's (where business rates far outstrip rents in some areas) and the retail sector; and
- A call for improvements in the administration of the system including clearer billing, better levels of information sharing and a more efficient appeals system; and
- Business rates are essentially a property tax based on property rental values. They do not take into account other considerations (for example such as building size, turnover, number of employees) beyond the rental value of the property it occupies; and
- Changes to the use of property. During the period that the business rates system has operated, major changes have taken place to the way that people in the UK work, live and shop. This, in turn, has contributed to changing patterns in the occupation of non-domestic property, on which business rates are payable. This includes flexible working practices, the increasing importance of Wi-Fi Internet, smartphones and cloud technology, all of which have affected the amount of space required by businesses, particularly office space. People have also changed the way they shop. Internet shopping has increased in popularity, with 82% of internet users making an online purchase in the period 2014 – 2015 which is the highest in Europe. Recent years have seen a decrease in demand for high street shopping and an increase in demand for online retail services which combine both 'bricks-and-mortar' and online services. The banking sector has also adapted to a move towards increased mobile and internet banking and over 60% of their customers use internet banking regularly. These patterns of property usage show that the business rates tax base is changing.
- The proposal for self sufficient local government is based on the system being fiscally neutral and there is an assumption that a move to 100% business rate retention will result in an additional £12 billion being transferred to local government. This is based on an estimate only. Further work needs to be undertaken to establish whether this is indeed the case as there are already funding pressures in the system. Transferring new responsibilities on the basis that it is estimated that there is additional funding coming forward could undermine the sustainability of local government finance at a very early stage in the new system.

B. Business rates and Local Growth

The consultation sets out that the Government are committed to ensuring that local authorities have the right incentives to grow their business rates base and that there is a balance to be struck between providing a strong incentive for growth in local areas and considering the distribution of funding between local authorities. The private sector in the Solent area want to highlight that some further points as follows;

- From a development perspective there needs to be a coherent and consistent approach to the planning process which inspires business confidence; and

- The need for certainty is paramount. Therefore the track record of local authorities and their appetite for change influences investment; and
- To what extent can additional growth in business rates be hypothecated to inform future infrastructure capital investment as it is recognised that it takes time to plan and activate such projects. To assist this it would be helpful if Local Authorities could indicate areas for development intensification; and
- There is a need to bring together funding regimes such as the Business Rates retention proposals, TIF and CIL; and
- There is a recognition in the business community that there will be strings attached to 100% business rates retention given devolution and this will mean that there is not unconditional flexibility on how to spend the funds. For example there is a growing pressure on the increasing demand for services in LA areas and the private sector are concerned that the extent of this demand may mean that additional proceeds derived from growth in business rates income may go fully or in the main to support public services as opposed to investing in infrastructure to support growth.

The submission below is a response to the consultation documents by Solent Local Enterprise Partnership.

A consultation exercise has recently been undertaken in the Solent area about establishing a Mayoral Combined Authority comprised initially of three unitary local authorities, Southampton City Council, Portsmouth City Council and the Isle of Wight Council together with Solent LEP. Solent LEP therefore has a direct interest in questions that relate to the flexibilities and resources likely to be available under devolution deals. The Board of Solent LEP has also engaged with the businesses in the Solent area in relation to this consultation and responses reflect the business view. It is recognised that there are questions that are specific to local authorities and hence we have not commented on all questions in the consultation documents.

1: Which of these identified grants/responsibilities do you think are the best candidates to be funded from retained business rates?
2: Are there other grants/responsibilities that you consider should be devolved instead of or alongside those identified above?
3: Do you have any views on the range of associated budgets that could be pooled at the Combined Authority level?
4: Do you have views on whether some or all of the commitments in existing and future deals could be funded through retained business rates?

The Office for Budgetary Responsibility estimates that the additional business rate retained by local authorities in 2019/20 will be £12.5bn and the consultation therefore proposes a change in functions so that the effect is fiscally neutral. It proposes the abolition of a number of specialised grants (eg Public Health, Early Years, Youth Justice) and invites views about which other functions could become self-financing, especially in the context of devolution

Current forecasts of the quantum, show the additional amount available for redistribution, ranging from an additional £11-15bn. These forecasts were made pre outcome of the EU referendum and therefore should be revised. The consultation paper quotes £12.5bn additional quantum and given the decision to withdraw from the EU and the need to factor in new domestic fiscal commitment it is important that there is transparency regarding the calculation of the quantum, including a clear statement of the assumptions regarding growth and inflation.

Any transfer needs to be sustainable in the longer term and un-ring-fenced to allow local areas to take the best decisions on service delivery for their residents and businesses. Transfer of the administration of the specific grant as well is not considered an acceptable option as there should be local flexibility (including through negotiated devolution deals) on how it should be utilised.

Solent LEP is in favour of the principle of increasing the local fiscal autonomy of local authorities and in particular, Combined Authorities as a means of securing greater local discretion in shaping investment needs and priorities.

We feel that there are strong arguments in favour of creating a financial regime that provides continuity of funding given that capital investment often requires planning and delivery over the longer term. For that reason we would prefer to see rolling Investment Funds financed from retained business rates as a means of providing real local discretion over investment over the longer term. However given the recent outcome of the EU referendum and the announcement of a new Industrial Strategy , we also believe that the overall value of each Investment Fund agreed under devolution deals needs to be underpinned by central Government.

The consultation states there is *"an opportunity to consider funding some or all of the commitments in existing and future [devolution] deals through retained business rates ie transferring them from grant commitments to being paid through retained rates"* to provide Combined Authorities/Mayors with *"the advantage of fiscal autonomy for these functions"*.

The functions listed are

- Investment Fund as part of devolution deals
- Adult Education budgets
- Transport capital grants such as highways maintenance and bus subsidy
- Local Growth Fund – competitive bidding in 5 year cycles

The consultation document points out that the Mayoral Investment Fund is agreed for 30 years but is only funded for 5 years subject to review, and the LGF is funded by competitive bidding. All devolution deals have the flexibility to incorporate the LGF with the Investment Fund but the implication is that DCLG questions (3.21) whether either fund, operating in 5 year cycles, can permanently be embedded in the local government finance system.

Solent LEP favours greater local autonomy and financing an Investment Fund from retained rates on a rolling basis. However given the current concerns from businesses about the need for reform of the business rate system, the fact that the LGF is a competitive fund, the clear tension between supporting local growth and supporting the increasing demand for public services in an area as well as the recognition that infrastructure programmes of this nature take time to plan and activate, Solent LEP does not support the proposal to permanently embed the Local Growth Fund within the local government finance system. Instead we would support the need to align the Local growth fund with investment funds as part of devolution deals, the adult education budget and transport capital grants.

As a result Solent LEP does not support the proposal that the current Local Growth Fund could be supported from retained rates and therefor should be permanently embedded in the local government finance system. Solent LEP recognises and supports the discipline of competitive bidding for capital resources and we note that sourcing the LGF from retained rates could change the balance of responsibility for LGF from Local Enterprise Partnerships to local government members of Combined Authorities. There may be arguments in favour of merging LGF and Investment Funds but Solent LEP does not want this to occur simply as a consequence of redesign of the rating system. Equally the board are committed to ensuring that decisions around the use of the Local Growth Fund remain business-led and that the fund provides an opportunity to under pin transformational growth projects without being exposed to the uncertainty that may occur during periods of reset or as a result of affordability considerations in the event that demand for local public services mean that funding for local growth is curtailed.

5: Do you agree that we should continue with the new burdens doctrine post-2020?
Yes

6: Do you agree that we should fix reset periods for the system?
7: What is the right balance in the system between rewarding growth and redistributing to meet changing need?
8: Having regard to the balance between rewarding growth and protecting authorities with declining resources, how would you like to see a partial reset work?

As a matter of principle, Solent LEP believes that the partner local authorities with which it works to strengthen the economy of the Solent area should be able to benefit from the product of growth over the longer term. Solent LEP is acutely aware that strategic investment, such as major road infrastructure or city regeneration projects, may take many years to have an impact and local authorities may be borrowing over the longer term in expectation of improved receipts. A full reset every 5 years provides too little incentive to local authorities to grow their economic base.

Any rates reset therefore needs to recognise the long term nature of infrastructure investment and in areas where a levy has been agreed a straight forward reset would impact on the returns on such investment and the growth benefits of the levy and subsequent investment in infrastructure would not be returned to the area. Therefore a partial reset is favoured and it should be fixed (albeit 5 years does seem too short) and this should be modelled as part of the piloting phase.

9: Is the current system of tariffs and top-ups the right one for redistribution between local authorities?
10: Should we continue to adjust retained incomes for individual local authorities to cancel out the effect of future revaluations?

No comment

11: Should Mayoral Combined Authority areas have the opportunity to be given additional powers and incentives, as set out above?

There is potentially a wide disparity in the level of need between the authorities making up the possible Solent Mayoral Combined Authority and the practicality of a single needs baseline would need to be tested. In principle, Solent LEP favours the maximum local discretion to determine priorities and distribute resources.

12: What has your experience been of the tier splits under the current 50% rates retention scheme? What changes would you want to see under 100% rates retention system?
13: Do you consider that fire funding should be removed from the business rates retention scheme and what might be the advantages and disadvantages of this approach?

No comment

14: What are your views on how we could further incentivise growth under a 100% retention scheme? Are there additional incentives for growth that we should consider?

Solent LEP sponsors the Solent Enterprise Zone and welcomes the way in which long term local ownership of business rates in EZs is underpinning prudential borrowing for investment. Our EZ is aimed at regeneration of a major site in a disadvantaged area: similar initiatives aimed at city regeneration initiatives could be of significant benefit to Solent LEP's City Council partners.

Under 100% rates retention, the Government intends that Enterprise Zones will continue to operate as now and, therefore, will be guaranteed 100% of business rates growth for 25 years. This means that the Government intends that any income above current baselines in Enterprise Zones will be disregarded for the purposes of calculating "cost neutrality" when devolving new responsibilities to local government and for the purposes of working out tariffs and top-ups. On this basis the retained rates from the Solent Enterprise Zone will continue to operate as now and we support this.

15: Would it be helpful to move some of the 'riskier' hereditaments off local lists? If so, what type of hereditaments should be moved?
16: Would you support the idea of introducing area-level lists in Combined Authority areas? If so, what type of properties could sit on these lists, and how should income be used? Could this approach work for other authorities?

On a broader level and taking into account the wider business landscape and reflecting on feedback we have had from the private sector there is also an opportunity to look again at the rating list system that operates in England. Under the current system, local authorities only benefit from any growth in income from ratepayers on local lists. Some local authorities have flagged that the highest risk hereditaments should be removed from local lists. These might include power stations, oil refineries and national airports, which could be moved onto a refreshed national level list (i.e. the current central list). Alternatively, some authorities have advised that they would welcome the opportunity to manage some of the riskier properties at a broader 'area level' – sharing the risk that these properties bring, but also receiving an element of reward from any growth. We support this and would want to explore this option if the Solent was to become a pilot area.

Solent LEP's area has also been subject to economic shocks such as the closure of the Ford manufacturing plant with loss of business rate income by Southampton City Council and the demise of Royal Navy shipbuilding at Portsmouth. Solent LEP would support a methodology whereby recovery funds could be put in place quickly to address unplanned events and support the longer term cost of remedial investment. Given the scale of such effects on individual local authorities, this may require national intervention funded from the central list.

17: At what level should risk associated with successful business rates appeals be managed? Do you have a preference for local, area level (including Combined Authority), or across all local authorities as set out in the options above?
18: What would help your local authority better manage risks associated with successful business rates appeals?

No comments

19: Would pooling risk, including a pool-area safety net, be attractive to local authorities?
20: What level of income protection should a system aim to provide? Should this be nationally set, or defined at area levels?

Solent LEP's experience is that while the effect of an economic shock can be most severe in one locality (eg the closure of a plant) they ripple outwards so that all local authorities in an area may be affected. For that reason, our view is that local pooling may not be sufficient to mitigate against major risks without an effective safety net.

21: What are your views on which authority should be able to reduce the multiplier and how the costs should be met?
22: What are your views on how decisions are taken to reduce the multiplier and the local discount powers?
23: What are your views on increasing the multiplier after a reduction?
24: Do you have views on the above issues or on any other aspects of the power to reduce the multiplier?

Solent LEP would expect any reduction in the multiplier to be a decision taken collectively by a Combined Authority in the light of a prospectus/ business case issued for consultation with all relevant parties.

It is also important to ensure that any new system brings forward a structure that ensures stability and therefore recognises that local authorities will want flexibility to determine their own income base and equally business will want to see consistency, clarity and stability in the system.

25: What are your views on the flexibility levying authorities should have to set a rateable value threshold for the levy?
26: What are your views on how the infrastructure levy should interact with existing BRS powers?
27: What are your views on the process for obtaining approval for a levy from the LEP?
28: What are your views on arrangements for the duration and review of levies?
29: What are your views on how infrastructure should be defined for the purposes of the levy?
30: What are your views on charging multiple levies, or using a single levy to fund multiple infrastructure projects?
31: Do you have views on the above issues or on any other aspects of the power to introduce an infrastructure levy?

Solent LEP supports the principle of empowering Combined Authorities to introduce an infrastructure levy subject to caveats: exemption for small businesses; publication of a full business case; time limited; and subject to wide consultation.

Solent LEP welcomes the intention that any levy should be subject to the agreement of a majority of business board members. In terms of a process for obtaining approval from the LEP there should be a requirement for the following:

- Submission of a outline business case setting out the alignment with the Strategic Economic Plan of the LEP, Economic case, Financial and Management case and Risk assessment; and
- The levy should be for strategic infrastructure investment only and should come forward as a defined project or defined programme of capital proposals; and
- Business consultation should be an obligation on all LEPs where they are asked to decide on a levy proposal and the outcome of the consultation should inform the decision.

LEPs already play a strategic role in determining the priorities for infrastructure investment through the Strategic Economic Plan (SEP), and therefore are in a position to act as representatives of local business communities to ensure that proposed infrastructure projects will benefit ratepayers. It has also been suggested though that there should be additional safeguards for ratepayers, for example consultation beyond the LEP. Solent LEP has undertaken consultation with the wider business community on proposals for devolution and LGF submissions as well as the formulation of the SEP. It would be more effective and beneficial to ensure that the LEP is required to undertake a consultation with businesses more widely on any proposal for a levy as running multiple and independent processes could result in more complex and protracted decision making.

It is clear from the consultation that levy revenues must be used to fund infrastructure projects. Infrastructure could be defined in a similar way to how it is defined for the Community Infrastructure Levy - roads and transport, flood defences, educational facilities, medical facilities, sporting/ recreational facilities, and open spaces – or a different definition could be used to capture different uses. During our discussions with the private sector a number of businesses asked for clarity on what is meant by infrastructure and there was a view that there should be some local flexibility to review the current definition to reflect new requirements such as for 4G/5G Blue infrastructure or new energy requirements. This is particularly important if the system is to be sufficiently responsive to both the changing patterns of property usage and the conditions in the wider economy.

The business community in the Solent have emphasized the importance of establishing a framework that provides stability and certainty and there was a concern that bringing forward multiple levies at different times may create uncertainty whereas a single levy to cover a programme of infrastructure investment across the combined authority area was favoured.

Solent LEP believes that there should be a single levy and it should be used in exceptional circumstances for particular named, strategic and deliverable project(s) /programme and evaluated in the same way as a major business decision. The sensible geographic area for any levy would be the area benefitting from the specific strategic investment proposed, whether that is a Combined Authority or LEP geography.

32: Do you have any views on how to increase certainty and strengthen local accountability for councils in setting their budgets?
33: Do you have views on where the balance between national and local accountability should fall, and how best to minimise any overlaps in accountability?
34: Do you have views on whether the requirement to prepare a Collection Fund Account should remain in the new system?
35: Do you have views on how the calculation of a balanced budget may be altered to be better aligned with the way local authorities run their business?

36: Do you have views on how the Business Rates data collection activities may be altered to collect and record information in a more timely and transparent manner?

Solent LEP recognises that local authorities are major businesses in their own right and observes that any increase in self-sufficiency and local autonomy in financing brings with it a requirement for enhanced accountability at the local level.

Fair Funding Review: call for evidence

Solent LEP does not feel able to comment on all the questions set out in the consultation document. However, we have commented above on two points:

- the difficulty of setting a single assessment of need for a Combined Authority that may have significant disparities between constituent members;

- the need to incentivise local authorities to growth and enable them to benefit from longer term investment in their local economies. The experience of Solent LEP is that strategic investment to promote growth and improve productivity requires long term planning and delivery and a commitment to structural change.