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Communities & Local Government Select Committee Business Rate Retention Inquiry submission

Executive Summary

- 100% business rate retention and the Fair Funding Review comes at a time when county and county unitary authorities in England face unfunded cost-pressures of £2.54bn by 2020/21 and when there has been a 93% drop in funding between 2010 and 2020.

- CCN, alongside the wider sector, have been supportive of the move towards 100% business rates retention. However, CCN believe that the current pressures facing services are unsustainable moving forward and action is needed immediately to provide additional support to county authorities.

- We therefore hope that government carefully considers the specific implications of BRR and the fair funding review and the delay in implementation gives a greater opportunity for local government to be given assurances we need on how government will support local authorities moving forward.

- Research show that despite Shire Counties producing 41% of GVA in England, they have much larger numbers of business ratepayers claiming reliefs, meaning CCN authorities receive dramatically less business rate income per head compared to urban areas.

- Modelling shows a higher share of business rates for county councils – potentially as high 80% – would help reduce the funding gap by £150m and ensure a more balanced system between tiers and types of local authorities.

- Any fair funding measure which fails to take into account the impact of inflation and demographic growth will be fundamentally flawed. To arrive at a new fairer method of funding local services, CCN have advocated a formula that funds local authorities on their present and future needs. Any simplified indicators that are selected by the government to determine funding must focus on services, and in particular statutory services and older people's services where there are the greatest levels of increased demand.

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Introduction

1. The County Councils Network (CCN) is the national voice for 37 English local authorities that serve counties. CCN's membership includes both upper tier and unitary authorities who together have over 2,600 councillors and serve 26 million people (47% of the population) across 86% of England. CCN develops policy, shares best practice and makes representations to government on behalf of this significant proportion of the country outside of the big conurbations. CCN is a member-led organisation which works on an inclusive and all party basis.

2. On behalf of our member councils, CCN welcomes this opportunity to submit evidence to this inquiry on 100% business rates retention.

3. Over recent months CCN has undertaken extensive work to understand the specific implications of 100% business rates retention on CCN member councils. This includes two independent research and modelling exercises undertaken by Pixel Financial Management, which are listed below.

    - Independent Study on Business Rates Retention in County Areas[1]:

    - 100% Business Rate Retention: Further Technical Work[2]

4. This submission draws on the independent findings of these reports, alongside a recent post-election statement outlining the position of CCN.[3] We urge the committee to study these reports in full.

5. In addition, CCN has recently commissioned Pixel to conduct a technical analysis of the Fair Funding Review. Once concluded, CCN will share the findings with the Committee at the earliest opportunity.

6. Alongside this written submission, CCN would welcome providing oral evidence to the committee.

The County Context

7. The move towards 100% business rate retention and the Fair Funding Review comes against the background of a significant and growing funding gap for county authorities. The Society of County Treasurers (SCT) recently surveyed county authorities across England on their budgetary position and we have used the results of this survey to estimate that county and county unitary authorities in England face unfunded cost-pressures of £2.54bn by 2020/21, excluding inflation.[4]

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[1] https://www.countycouncilsnetwork.org.uk/new-report-independent-study-on-business-rates-retention-in-county-areas/
[2] https://www.countycouncilsnetwork.org.uk/new-analysis-reveals-100-business-rate-retention-pose-challenges-county-authorities/
[3] https://www.countycouncilsnetwork.org.uk/download/1149/
[4] https://www.countycouncilsnetwork.org.uk/download/1185/

Cost Pressure	Average County	Total CCN
National Living Wage	£22m	£813m
NI Contributions	£3m	£93m
Adult Social Care	£26m	£949m
Children's Services	£9m	£316m
Highways	£4m	£138m
Pension liabilities'	£2m	£66m
Education (inc. SEN)	£5m	£167m
Total Cost Pressure - 2020/21	**£69m**	**£2.54bn**
NB: Columns may not sum due to rounding.		

8. In addition, county and county unitary authorities face a growing funding crisis in the adult social care provider market. Recent research by Laing Buisson showed that there remains a £670m funding gap in the provider market, over and above core budget pressures.[5]

9. These findings support the LGA estimates that local government as a whole faces a funding gap of £5.8bn by 2019/2020. Between 2010 and 2010 there has been a reduction in central government funding for local authorities of £16bn between 2010 and 2020.[6]

10. Counties are being exposed to particularly acute funding and demand-led pressures. For example, CCN members have some of the fastest rising represent the largest and fastest growing older populations, of both over 65s and over 85s. The older population of counties is expected to increase by 2% year on year, and CCN members are seeing a significant rise in referrals to social care, in comparison to overall reductions in other types of authority.[7]

11. Counties have been hit particularly hard, with a 93% drop in funding between 2010 and 2020. We believe this is part attributable to the distribution of Revenue Support Grant (RSG) through the Relative Needs Formula, which has consistently underfunded CCN members. This is mainly due to the weighting within existing funding formulae, which gives significantly less weight to factors such as population growth and demographic trends, sparsity and concentrated pockets of deprivation. This has historically led to funding being increasingly directed towards more built-up areas, particularly inner London.

12. The current system therefore leaves counties in a position where they receive less funding per head than all other council types, as shown in the table below:

Council type	Average funding per head
Inner London	£1,190
Outer London	£944
Metropolitan Borough	£825
Non-CCN unitary council	£675
County areas	£650

[5] https://www.countycouncilsnetwork.org.uk/download/1179/
[6] https://www.local.gov.uk/sites/default/files/documents/5.20%20budget%20submission_06.pdf
[7] https://www.countycouncilsnetwork.org.uk/health-social-care-in-counties-funding-demand-cost-pressures/

13. As outlined in the sections below, the financial position of CCN member councils could be significantly worsened if Government does not carefully consider the specific implications of BRR and the fair funding review. It is important to note here that Counties are not convinced that full BRR alone will provide a solution to meet the growing funding gap facing counties. Only 40% of our Leaders in a recent survey believed that 100% BRR was either effective or very effective at migrating against continuing reductions in core government funding.

Please find below our answers to the questions raised by the Committee.

What are the consequences for councils of the longer implementation period for 100% retention in the context of the four-year settlement?

14. CCN, alongside the wider sector, have been supportive of the move towards 100% business rates retention. As a stakeholder on the DCLG/LGA steering group, counties have played an active part in national discussions to-date, working closely with the SCT.

15. However, given research findings during the past 12 months CCN has consistently highlighted the challenges of implementing a system that provides sustainable long-term funding for all parts of local government, alongside incentives to drive growth locally. Similar concerns have been raised by metropolitan authorities through SIGOMA.[8] In addition, we have committed to working with the District Councils Network (DCN) and Rural Service Network (RSN) to jointly explore the implementation of BRR in two-tier local authority areas, including considerations of tier shares.

16. Recent discussions at the DCLG/LGA steering group have highlighted that both central and local government have considered this a useful time to reflect on the objectives and design of business rate retention, and the wider sustainability of local government funding.

17. Many aspects of greater local business rate retention are still possible without primary legislation and there is appetite within central and local government for increased local retention business rates; albeit exploring a broader range of options which may or not result in 100% retention. From our most recent members' survey, there continues to be majority support for the implementation of full BRR. Some 55% of Leaders agreed with the continuation of full BRR post-election, with 27% 'neutral' and 18% disagreeing.

18. The lack of universal support is reflective of the findings of Pixel's independent research showing that 100% retention will present a number of challenges to ensuring long-term financial sustainability for all councils and the right incentives to drive growth. The delay in the implementation gives a greater opportunity for local government to be given assurances we need on how government will support local authorities moving forward. Failing to manage the switch to 100% retention right could leave CCN members further exposed financially.

[8] http://www.sigoma.gov.uk/__documents/consultation-responses/SIGOMA-response-to-100-per-cent-rate-retention-CLG-enquirey.pdf

19. Firstly, our research with Pixel Financial Management in July 2016 profiled business rates in county areas and showed a wide variation and uneven growth of business rates income.

20. The report shows that income from business rates in urban areas, particularly London, far outstrips the amounts raised in rural counties. The research also revealed a wide variation in business rates across a county area, with individual districts within a single county seeing markedly different income from business rates since 2010.

21. The findings show that despite Shire Counties producing 41% of GVA in England, they have much larger numbers of business ratepayers claiming reliefs, meaning CCN authorities receive dramatically less business rate income per head compared to urban areas, especially London. Rateable values per head in the capital now average £3,700 compared to £851 in county areas.

22. If the new system is not properly designed, it could leave underfunded services for the vulnerable and elderly in county areas worse off at a time of growing demand. The study reveals that while spending pressures on services such as adults and children's social care are set to increase most in shire counties, income from business rates is unlikely to keep up.

23. Secondly, our second research project with Pixel showed that alongside divergent income within counties, 100% retention will present a number of challenges to ensuring long-term financial sustainability for all councils and the right incentives to drive growth.

24. In particular, the research showed a severe growing divergence between service needs and business rate income over time for county authorities. Pixel found that under full business rate retention, the funding gap for county authorities could widen over time, increasing by £700m by 2029 on top of any existing gap at that point.[9]

25. System design in two-tier areas will also be key, such as tier shares and the levy on growth. Pixel's independent findings show that a higher retention share for county councils could be important in balancing a full locally retained system across local authority types and regions, and ensure a fairer distributed of resources between district and county councils.

26. Moreover, Pixel found that retaining a reformed levy to simply ensure no council was able to build up disproportionate retained rates above their needs base could bring greater fairness and balance in a 100% retention system.

27. For CCN members this picture is further complicated by the need for upper and lower tier authorities to share the proceeds of business rates.

28. Pixel's modelling shows a higher share of rates for county councils – potentially as high 80% – would help reduce the funding gap by £150m and ensure a more balanced system between tiers and types of local authorities. This would be more closely aligned to the relative needs for the continuing provision of services, and would result in less redistribution required through top up and tariffs.

[9] https://www.countycouncilsnetwork.org.uk/download/1132/

29. The government is also currently pressing ahead with pilots for 100% retention. CCN welcomed the announcement of a second phase of pilots, and specifically the focus on extending the opportunity to pilot the scheme in two-tier areas and to test key aspects of the new system.

30. In approaching the pilot schemes from next year, testing sustainability, and considering the implications for the future design of the system, one issue CCN would stress is need to ensure that key decisions, such as tier shares, are not predetermined by proposals put forward by local areas.

31. In putting forward proposals, a significant degree of compromise has taken place with district councils regarding tier shares within a very limited time for negotiations. Moreover, it must also be acknowledged that with only Revenue Support Grant (RSG) and Rural Service Delivery Grant (RSDG) included in the second phase of pilots, it is likely the tier share for county councils will be lower in these pilots than if a wider range of grants, such as public health and iBCF, were included.

32. It is our view that under 100% retention, the share for county councils will be significantly higher than under the current system. Therefore, given the limited nature of these pilots and uncertainty regarding whether 100% will be implemented in the future, tier shares agreed in these pilots should not predetermine those for all two-tier areas when reforms to business rates are introduced across the whole of England.

33. As part of this pilot process, we hope that the government will listen carefully to local government about what the impact has been and if any mitigations ought to be put in place.

What are the consequences for councils of implementing the outcome of the Fair Funding Review in 2020-21?

34. The reality facing the sector and local communities is that a significant proportion of statutory local government services are underfunded. CCN believe that the current pressures facing services are unsustainable moving forward and action is needed immediately to provide additional support to county authorities, particularly in the context of the uncertainty surrounding local government finance following the fall of the Local Government Finance Bill.

35. As outlined above, 100% business rate retention could potentially decouple council finances from their spending needs and means that some councils will disproportionately benefit from the switch whilst some local authorities could lose out. As such 100% business rate retention means that there needs to be redistribution elsewhere in the system, to be determined by the Fair Funding Review.

36. The CCN and our members have long supported the Fair Funding Review, which we will hope will tackle some of the imbalances in the way that local government funding is distributed in England. Failure to do so means there is a substantial risk of embedding the current unfairness in funding into Business Rates baselines under the new system. Some 77% of Leaders in our recent survey strongly agreed that a new local government funding formula will be central to making full business rate retention work.

37. As we stated in paragraph 11, an inherent problem with the RSG methodology is its failure to fully reflect needs and demand. This imbalance funding means that some authorities have received historically higher grants, creating perverse and unfair disparities in council tax rates, as set out in our publication A Fair Deal for Counties.[10] For example, while Westminster can charge approximately £700 for an average property, the average for a county is £1,600. Given changing demographics, the current funding formula and the social care precept, this gap is likely to widen without funding reform.

38. While CCN recognises the need for some sort of spending power measure, any measure which fails to take into account the impact of inflation and demographic growth is fundamentally flawed. In the short-term this leads to disproportionate reductions for CCN member councils.

39. In supporting the Fair Funding Review, we do not believe it would be practical or appropriate for a new system to be based on complete parity of funding on a per head basis. Rather, we want to see a system that provides fair and sustainable funding for all local authorities in England.

40. To arrive at a new fairer method of funding local services, CCN have advocated a formula that funds local authorities on their present and future needs. Drawing on the model proposed by Leicestershire County Council,[11] an evidence-based, and data driven approach, would focus on cost-drivers of local services, such as the characteristics of the local population, deprivation, sparsity, density and area cost.

41. In further developing this approach, CCN has been supporting cross-sector collaboration through the Association of Local Authority Treasurers, where a strong consensus has been developed on the need to move away from past spend and regression analysis and towards a cost-drivers approach. CCN awaits the publication of the DCLG's forthcoming consultation exploring how to measure relative need and cost drivers.

42. Given the forthcoming consultation, CCN welcomes the publication of the LG Futures research by the Committee and in particular the suggestion that the funding formula is simplified. However, the impact on CCN members will depend on which cost drivers are included as part of any simplified formula. We note with some concern that whilst the overall impact on counties of the alternatives set out by LG Futures would be 0.0%, this masks some significant losses for individual counties who would no doubt want assurances about future reductions in funding given what we believe to be the current position of underfunding amongst counties.

43. Any simplified indicators that are selected by the government must focus on services, and in particular statutory services and older people's services where there are the greatest levels of increased demand. We do not believe that basing a funding formula on a wide range of factors not including need would meet many people's definition of "fair".

44. We also noted that LG Futures recommend updating the Resource Block so that it more closely resembles actual council tax. We are concerned at the impact that this could have on counties, given that the tax base of counties relative to "need" is very high.

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[10] https://www.countycouncilsnetwork.org.uk/download/965/

[11] https://public.tableau.com/views/FairerFundingNewModel/Ourfundingmodelresults?:embed=y&:display_count=yes&publish=yes:showVizHome=no#

45. We hope that the delay in implementing the outcome of the Fair Funding Review will give the government time to ensure that it is able to put in place a Fair Funding formula that is able to achieve this.

How are these changes to the original implementation schedule affecting councils' financial planning from 2020 onwards?

46. Given the current imbalances in the funding given to local authorities, it is unfortunate that the government has not been able to keep to the original schedule, as the combined impact of business rate retention and fair funding looked like it was going to strengthen council finances.

47. While the majority of our member councils accepted the offer of a four year settlement as a 'minimum' funding level, they did so due to the provision of the Transition Grant. This was because of the understanding that business rate retention would be implemented by 19-20 to prevent the move into negative RSG, and the commitment to the needs-based review of local government. We therefore believe that the Transition Grant needs to remain in place until we move to 100% business rate retention and the implementation of the Fair Funding Review

48. It is difficult for the CCN and members to provide a specific analysis of what the impact will be until we see the results of the local government funding settlement expected in December 2017. We are happy to provide the Committee with information about how the settlement – and the further information on the delay in implementation – impacts on counties after we have had time to analyse the settlement. However, it was disappointing that the Autumn Budget provided no further funding for adult social care, which is a particularly acute pressure point for upper tier authorities.

49. The move to full business rate retention in 2019/20 and implementation of the Fair Funding Review was seen as an opportunity to address the long-term funding arrangements for local government. Now that this implementation date is no longer viable, central and local government need to develop timely solutions to funding in the interim period

50. We hope that the government will be able to use the time resulting from the delay to ensure that a sustainable long-term fair funding mechanism can be put in place. With the fall of the Local Government Finance Bill, councils face uncertainty regarding how they will be funded beyond 2019/20. Under the four year settlement counties will see their RSG reduced by 93% - higher than the England average of 77% - with some 14 county authorities even entering 'negative RSG'.

51. We therefore believe it is essential Government consider extending transitional grant payments to CCN member councils up to 2020/21 to provide scope to maintain highly valued services, both discretionary and non-discretionary. This will help off-set the reductions in RSG and bridge the gap between the conclusion of the fair funding review and expected introduction of greater local retention of business rates by 2021.

52. However, the uncertainty surrounding this process is not helpful and is hampering the ability of local authorities to properly plan for their longer-term financial stability. All local authorities need clarity from the government about what their intentions are, including a

clear indication about whether they are going to legislate for 100% retention and when this might be expected to take place.