PIXEL FINANCIAL MANAGEMENT

County Councils Network (CCN)

Independent Analysis of Full Business Rate Retention in County Areas

Introduction

1. In the Spending Review (25 November 2015) the Chancellor confirmed that local authorities will be allowed to retain 100% of their business rate income by the end of the current parliament. This is hugely significant to local government and to rural authorities.
2. The Government has proposed increasing the proportion of business rates retained by local government from 50% to 100%. There will be changes to the relative shares retained by different types of authority, new services will need to be devolved, and there will need to be a reset of the rates baseline. A Steering Group has been set up to implement these changes and its membership includes the DCLG, the LGA and other representative groups, including CCN.
3. This report is intended to act as an internal report to support CCN's stance at the Steering Group and it's responses to the formal consultations that are issued by DCLG. We will identify the features of the retained-rates system that currently benefit CCN members, and where reform or changes would benefit CCN members. We are aware that there are differences within the membership, such as potential to increase rateable income, and we will use the analysis to indicate where there are differences.
4. The operation of the current business rate retention regime and the proposals to move to 100% retention are explained in **Appendix 1**.

Scope

5. This report addresses a range of questions about how the current and future rate-retention regimes work. The answers to these questions will help us to understand how CCN authorities have fared in the current system, and how they might fare under changes to the system.
6. Specific outputs in the report will include:
    - Analysis of each element of business rate income, including rateable value, gross rates payable, reliefs, net rates payable and appeals. Understand the characteristics of the CCN authorities compared to other groups of authority (London, Mets, Unitaries).
    - Undertake more granular analysis of the 37 CCN members, and explore the diversity within the CCN membership.
    - Explore implications of move to 100% retention, and an assumption that there will be an increase in retention for county councils. Comment on type of services that could be devolved and impact for CCN members
    - Link analysis of potential growth in business rates in CCN areas with future cost pressures. Concentrate on growth from current services, and use LG Futures' *Social Care and Health* report to indicate pressures, particularly from social care;
    - Comment on potential for redistribution within an area, and on the impact of combined authorities on business rates retention; and

- Review the control of multiplier or reliefs in a two-tier system, who pays for cost and who sets the overall economic development strategy. There ought to be alignment between these elements of the system.

Methodology

7. We have used the business rates benchmarking model. Data in the model uses the NNDR1 and NNDR3 returns that are published by the DCLG. NNDR3 returns have been used for the period 2010-11 to 2014-15, and NNDR1 for 2015-16.
8. Data has been aggregated together so that the analysis is at upper tier rather than billing authority level.
9. We have adjusted gross rates, net rates and reliefs for changes in the multiplier; changes between 2010-11 and 2015-16 and shown on a real-terms basis.

Overall analysis for CCN

10. Growth in rateable value since 2010-11 (when the current rating list was introduced) has been modest on average in each of the major local authority classes.
11. On average, rateable values in CCN authorities have grown by only 2.0% between April 2010 and the end of 2015-16 (**Chart 1**). This is marginally higher than in most of the other authority groups, with the exception of Unitary Authorities, where growth over the period has been 2.1%. For most authority groups the largest increases in RV occurred towards the start of the period (2011-12 and 2012-13). It should be noted that changes in RV over time will be a combination of the underlying change in rateable values (growth, demolitions) and appeals. Successful appeals will reduce RV and can be applied at any time. This means that the change in RV for any authority – or class of authority – will be a combination factors. As an example, high-growth areas with a high level of successful appeals might appear to have low or modest growth, and vice versa. As we will see below (Chart 12), CCN authorities tend to have relatively low levels of appeals, which will have the effect of making CCN authorities look like they are more "high-growth" than they really are.
12. **Chart 2** shows the average growth in each local authority class (since 2010-11) compared to the England average (1.6%). CCN authorities have experienced higher growth than most of the other classes, particularly Mets and Outer London boroughs.
13. Growth since 2010-11 varies widely within the CCN membership. The county council average – at 1.7% - is marginally above the national average. But the growth in the unitary councils in CCN is much greater, at an average of 3.7%. We will explore the growth in individual authority later on, but this illustrates the variation in business rates growth within the CCN group. It should also be noted that the number of unitaries in CCN is relatively small (10 out of 37) and so strong growth in a few members can skew the average.
14. Gross Rates Payable (GRP) and Rateable Value (RV) are the two top-level indicators of the amount of rates that is generated in an area, and the broad direction of travel. There are numerous adjustments between gross rates and the amounts that authorities can recognise in their budgets (reliefs, losses on collection, levies), but the gross position gives the clearest broad indicator of overall change in the ratebase. Gross RV per head (**Chart 3**) and gross rates payable

per head (**Chart 4**) shows that rates payable relative to the population is much, much greater in Inner London than anywhere else in the country. For instance, GRP is £1510 in Inner London compared to an average in the rest of England of £354 per head. Every class of authority except Inner London is similar to the national average.

15. Although it is not immediately apparent from either **Chart 3** or **Chart 4**, there is actually a noticeable variance in both RV and GRP per head between CCN counties and CCN unitaries. For GRP, for example, the overall CCN average is £346 per head – close the national average – but the CCN county average is £352 and the CCN unitary average is £310.

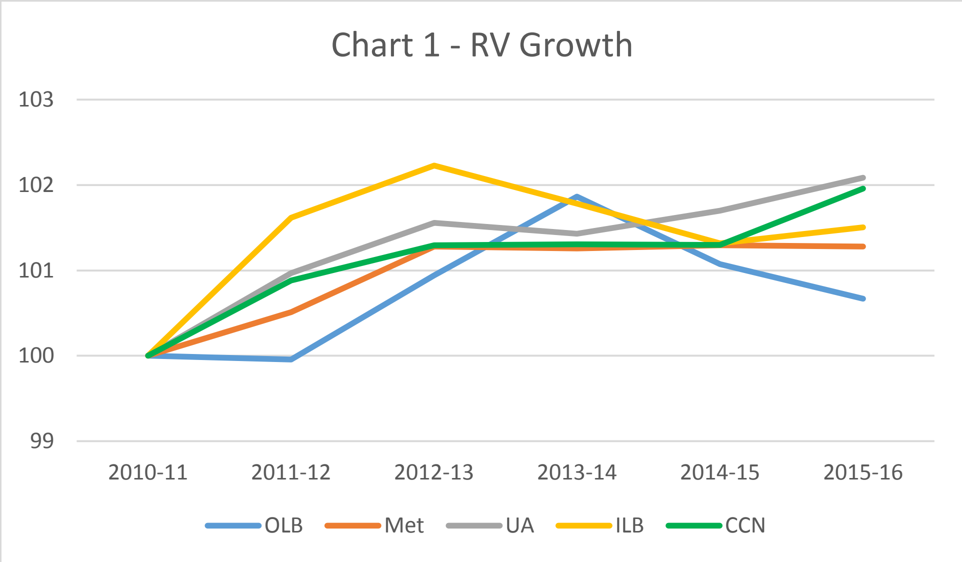

Chart 1 - RV Growth
103
102
101
100
99
2010-11
2011-12
2012-13
2013-14
2014-15
2015-16
OLB
Met
UA
ILB
CCN

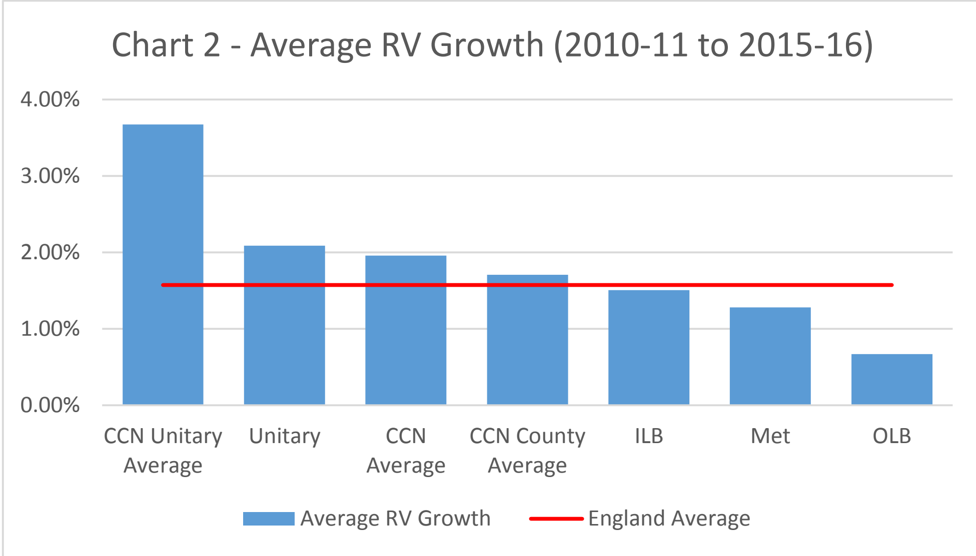

Chart 2 - Average RV Growth (2010-11 to 2015-16)
4.00%
3.00%
2.00%
1.00%
0.00%
CCN Unitary Average
Unitary
CCN Average
CCN County Average
ILB
Met
OLB
Average RV Growth
England Average

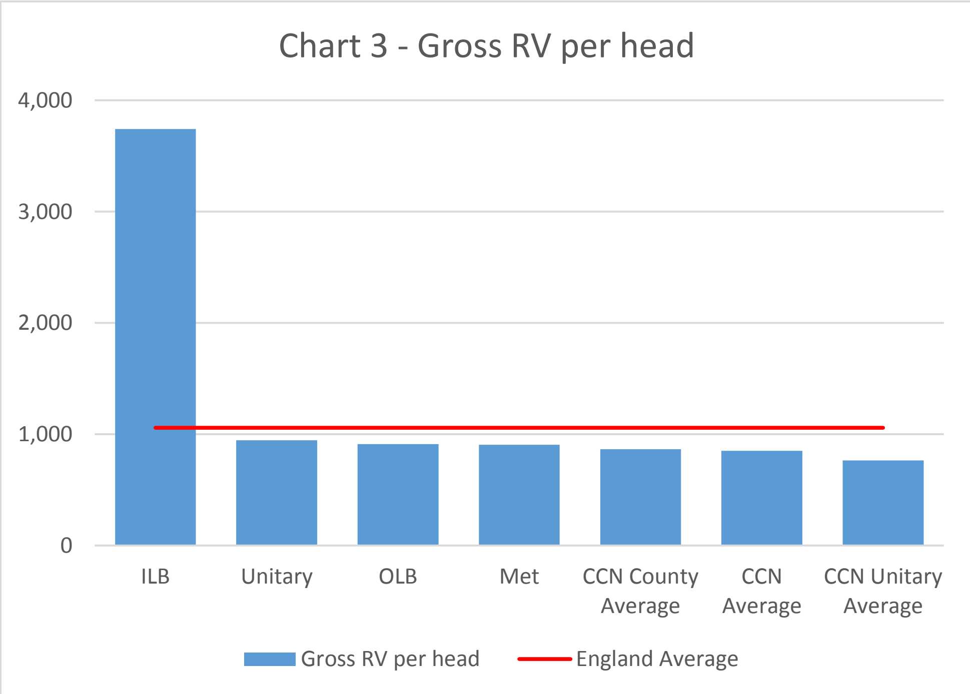

Chart 3 - Gross RV per head
4,000
3,000
2,000
1,000
0
ILB
Unitary
OLB
Met
CCN County Average
CCN Average
CCN Unitary Average
Gross RV per head
England Average

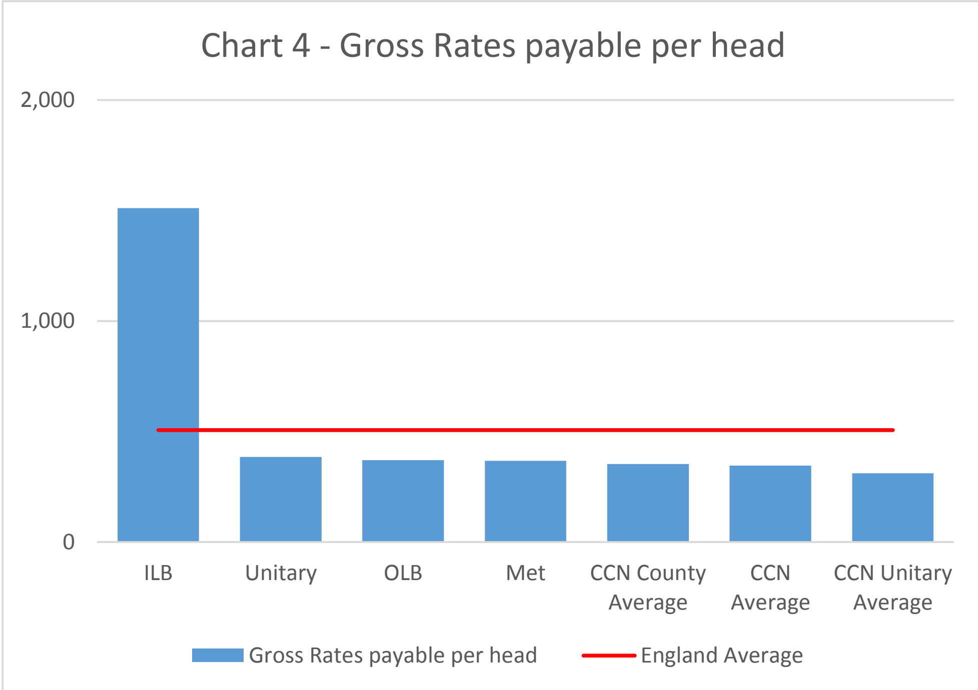

Chart 4 - Gross Rates payable per head
2,000
1,000
0
ILB
Unitary
OLB
Met
CCN County Average
CCN Average
CCN Unitary Average
Gross Rates payable per head
England Average

16. Growth in RV and GRP does not necessarily get converted into income that is retained by local authorities. Some businesses and organisations will be eligible for mandatory or discretionary reliefs. Net Rates Payable (NRP) is the amount that is paid by businesses after all the various reliefs have been applied. A summary of the reliefs that are available is provided at **Appendix 2**.

17. The proportion of reliefs relative to GRP is important to local authorities for two reasons.

    - The local authority pays for 50% of any increase in reliefs (and will pay for 100% of the cost when full retention is introduced). This is an unfair burden when some of the reliefs are mandatory and reflect Government policy. The cost is mitigated in some circumstances by grant funding (Section 31 grant), and of course authorities get the benefit if reliefs reduce.

    - Authorities where reliefs make up a relatively large proportion of their rateable value struggle to convert growth in rateable value into growth in net rates payable. Typically these are authorities with a large proportion of charitable or small businesses, and they are often the more rural authorities. A higher rate of reliefs indicates where business viability is more marginal and requires support from reliefs. It can also indicate that there is a higher level of "empties" due to business closures. Major urban centres have much higher proportion of NRP relative to GRP, because their reliefs and (usually) their "empties" are lower.

18. It should be noted that the Government currently pays grant (Section 31 grant) to authorities to compensate for some reliefs, with the largest amount of funding for small business rates relief. Grant is not paid for charitable relief or rural relief, or for unoccupied reliefs (which are effectively empty properties).

19. **Chart 5** shows that NRP per head is much higher in Inner London than the rest of the country, and that the rest of the country has a similar level of NRP per head. This pattern is similar for NRP and GRP. Again there is a divergence between the CCN county and unitary averages: £305 per head for the CCN counties, and £260 per head for the CCN unitaries.

20. **Chart 6** shows NRP as a proportion of GRP. A higher proportion indicates that the reliefs given to local businesses and organisations account for a smaller proportion of GRP. The highest proportion is in Inner London, where NRP is 92% of GRP (i.e. GRP is only reduced by 8% for reliefs). CCN authorities are towards the lower end of the range: the CCN average is 86%. Again we see a divergence between the CCN county councils (87%) and the CCN unitaries (84%). NRP is also a low proportion of GRP in the Mets. "Empties" reliefs are higher in Mets, whereas charitable relief and small business rates relief is higher in most CCN authorities.

21. **Chart 7** shows the increase in charitable reliefs. Charitable reliefs have increased much more quickly in rural areas than in urban areas, as well as representing a higher proportion of gross rates. CCN authorities have had some of the highest increases in the country, particularly the unitary CCN authorities. Growth in inner London in particular has been very low indeed. This is a clear indicator that the burden of funding charitable reliefs – which are mandatory and over which the authority has no choice – is falling disproportionately outside London and particularly in the most rural parts of the country.

22. Discretionary reliefs shows a more extreme pattern to mandatory reliefs. CCN authorities have by far the highest discretionary reliefs as a proportion of GRP (**Chart 8**). Indeed the CCN unitaries are awarding discretionary reliefs at nearly twice the national average rate relative to

GRP (0.76% compared to 0.39% nationally). The value of discretionary reliefs is relatively low (less than 10% the value of mandatory reliefs).

23. It could be argued that CCN authorities have awarded more discretionary relief in the past (partly at their own cost) and it is their choice to support local organisations and businesses. If they want to reduce the cost to the rates they retain, then they have the option of reducing the discretionary relief that is awarded. The counter-argument from CCN authorities could be that their businesses need more support, and provision of services is more likely to be from charitable or community organisations in CCN areas.

24. Urban areas have the highest rates of unoccupied reliefs (**Chart 9):** Met areas (1.8% of GRP), London (1.7%). This suggests that urban areas have a higher proportion of unoccupied reliefs and that, as a result, they are more exposed to the economic cycle. If the economy continues to improve, the unoccupied reliefs will continue to fall in these areas, to the financial benefit of the local authorities. CCN authorities have the lowest levels of unoccupied reliefs and are therefore less exposed to the economic cycle.

25. Changes in Net Rates Payable (**Chart 10**) are difficult to calculate with complete accuracy because of the impact of appeals and transitional relief. Our estimates take into account the following elements:

   - Transitional relief. When the 2010 rating list was introduced in 2010-11, businesses with large increases in rateable value as a result of the revaluation were paid transitional relief. Those with large reductions saw these introduced over a period of time. If the NRP is not adjusted for transitional relief then the amount collected – particularly in the early years of the rating list – will be under-stated and the overall increases overstated. This is particularly the case in London where rateable values increased the most in 2010.
   - Section 31 grants. The government pays grants for certain reliefs (small business rate relief, retail relief). These grants have to be added back.
   - Appeals. Net Rates in later years includes cash repayments for successful appeals in respect of earlier years, thus overstating the impact of appeals and understating growth. It is not possible to identify these repayments from the NNDR returns.
   - Growth/ demolition of business premises. The balance of any change in NRP will be due to the underlying growth or contraction in the rate base.

26. Overall the adjusted NRP indicates that yield has fallen by 5.4% (real terms) between 2010-11 and 2015-16. A net reduction is not unexpected: the Valuation Office Agency (VOA) estimated that there was a reduction of 7.34% in the 2005 rating list from a combination of successful appeals and other deletions. If this is also the case in 2010 – and it almost certainly is – then the net underlying growth in the ratebase is at least 2% in real terms and probably higher because of the effect of the repayment of successful appeals in respect of earlier years. When the baseline are set, there would normally be an allowance that reflects the potential impairment in the rate base.

27. The reductions in NRP (**Chart 10**) have been lowest in inner London, followed by the Mets and outer London; the CCN average is much lower than the national average (-6.6% compared to -5.4%).

28. Clearly the level of appeals is an important factor in the change in adjusted NRP. Authorities have to make an assessment of their future losses from appeals. Appeals are where a business disagrees with the valuation on its property and appeals to the Valuation Office Agency (VOA). Successful appeals are reflected in reductions in rateable value and NRP. The level of provision that authorities make for appeals reflects the proportion of their ratebase that is under challenge, and the turbulence in their ratebase (it is effectively a provision to cover the cost of future losses from appeals). By far the highest levels are in inner London (£204 per head) and and the Met areas (£49 per head): appeals tend to be greatest in urban areas where there is more business turnover and more development (**Chart 11**). CCN authorities have much lower levels of appeals provision, which indicates that their less-urban ratebases tend to be more stable. (Provisions are higher in county councils which are the sum of the district council provisions.)

29. **Chart 12** shows the reduction in NRP and the appeals side-by-side. Inner London is clearly different from the rest of the country: it has had the smallest reduction in its NRP whilst having large appeals: this suggests that the bulk of the underlying growth has taken place in London. Met areas are similar: average reductions in NRP but high levels of appeals. On average, CCN authorities have much lower appeals and also greater reduction in NRP: this suggests that compared to inner London and much of the rest of the country underlying growth in NRP is lower in CCN authorities. On average, CCN unitaries have higher growth, but this is driven largely by outliers such as East Riding of Yorkshire.

30. Part of the explanation for below-average growth in CCN authorities is the effect of reliefs: reliefs have increased by more in CCN areas. This demonstrates how difficult it has been for many CCN authorities to convert increase in rateable values into growth in business rates income, with much of it being consumed by reliefs.

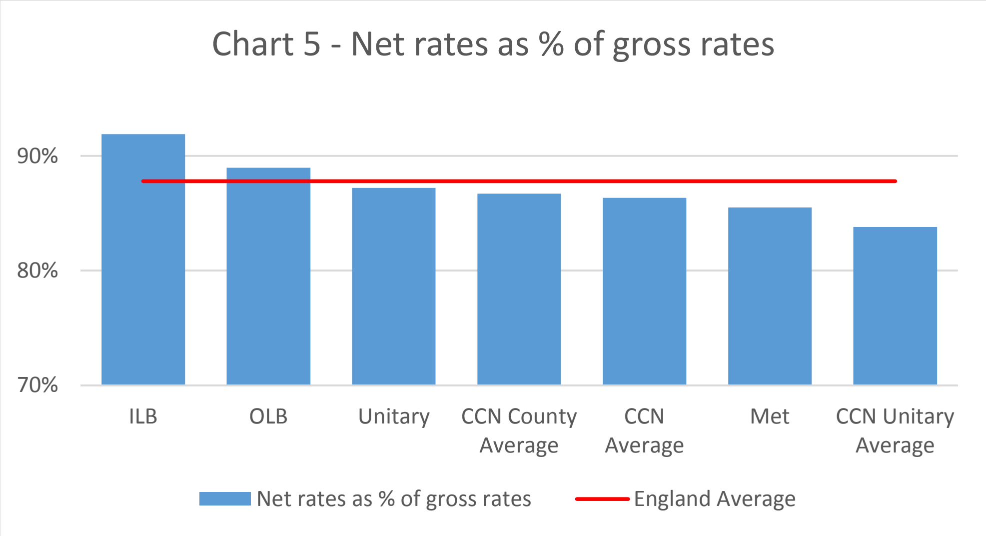

Chart 5 - Net rates as % of gross rates
90%
80%
70%
ILB
OLB
Unitary
CCN County Average
CCN Average
Met
CCN Unitary Average
Net rates as % of gross rates
England Average

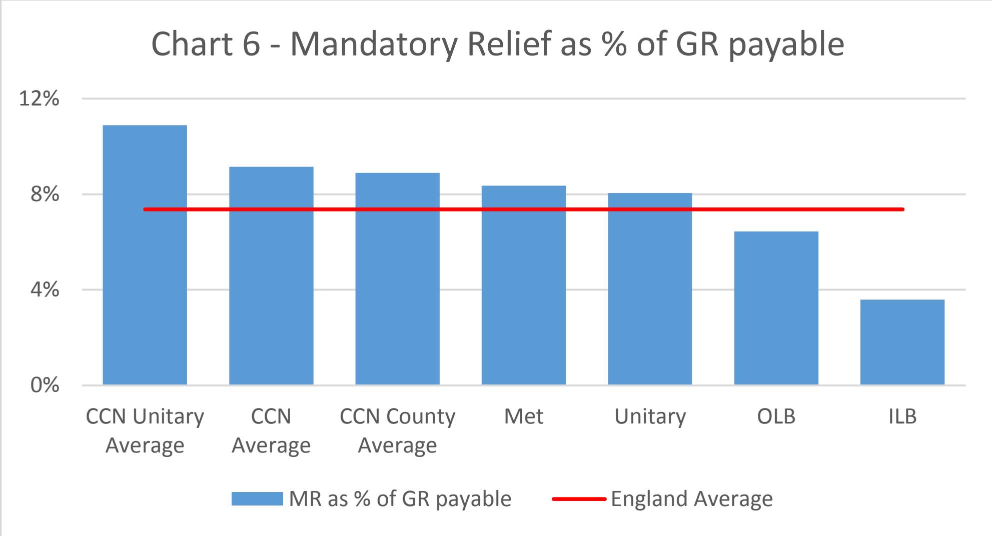

Chart 6 - Mandatory Relief as % of GR payable
12%
8%
4%
0%
CCN Unitary Average
CCN Average
CCN County Average
Met
Unitary
OLB
ILB
MR as % of GR payable
England Average

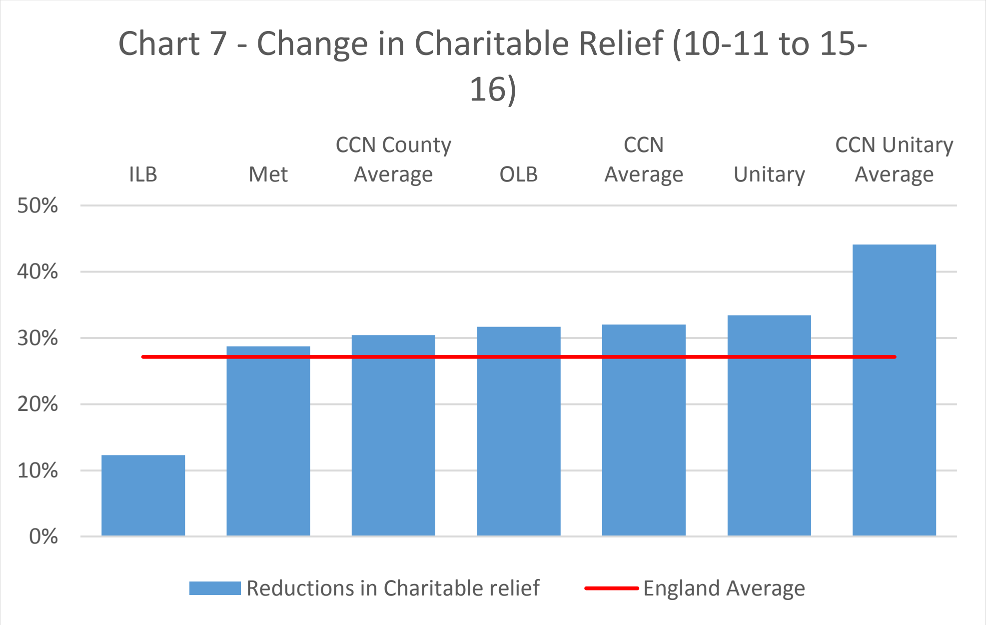

Chart 7 - Change in Charitable Relief (10-11 to 15-16)
ILB
Met
CCN County Average
OLB
CCN Average
Unitary
CCN Unitary Average
50%
40%
30%
20%
10%
0%
Reductions in Charitable relief
England Average

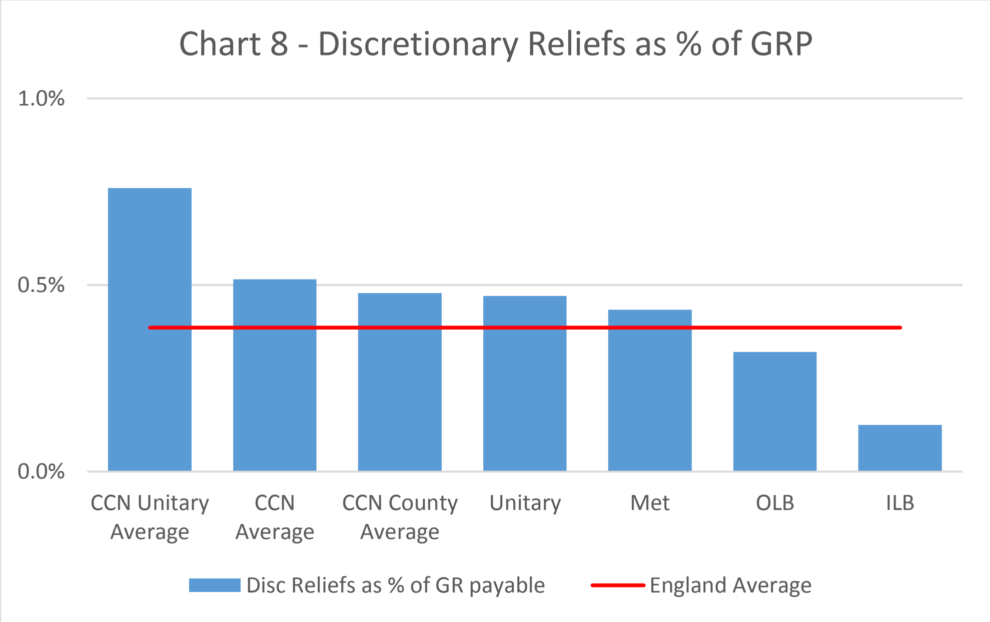

Chart 8 - Discretionary Reliefs as % of GRP
1.0%
0.5%
0.0%
CCN Unitary Average
CCN Average
CCN County Average
Unitary
Met
OLB
ILB
Disc Reliefs as % of GR payable
England Average

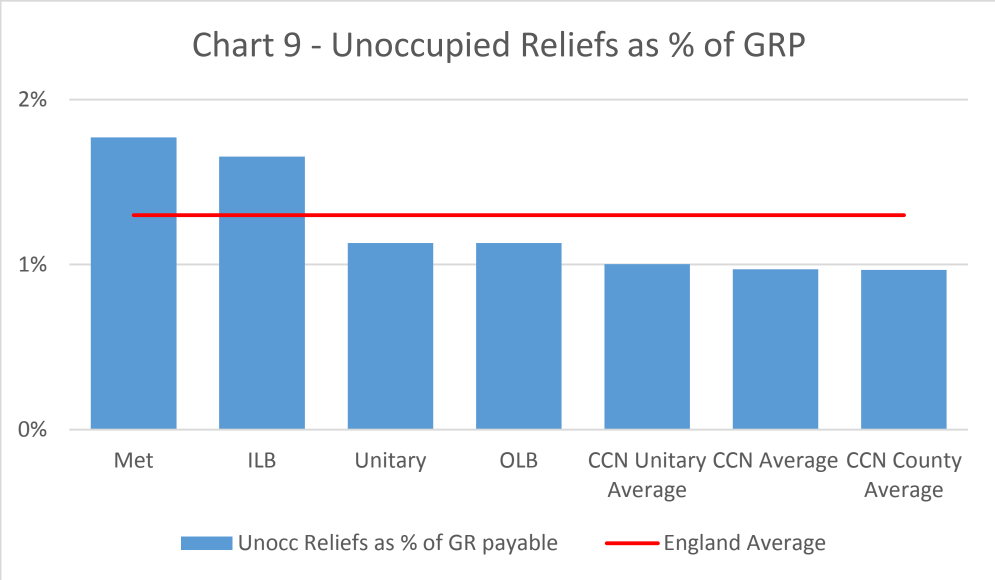
Chart 9 - Unoccupied Reliefs as % of GRP
2%
1%
0%
Met
ILB
Unitary
OLB
CCN Unitary Average
CCN Average
CCN County Average
Unocc Reliefs as % of GR payable
England Average

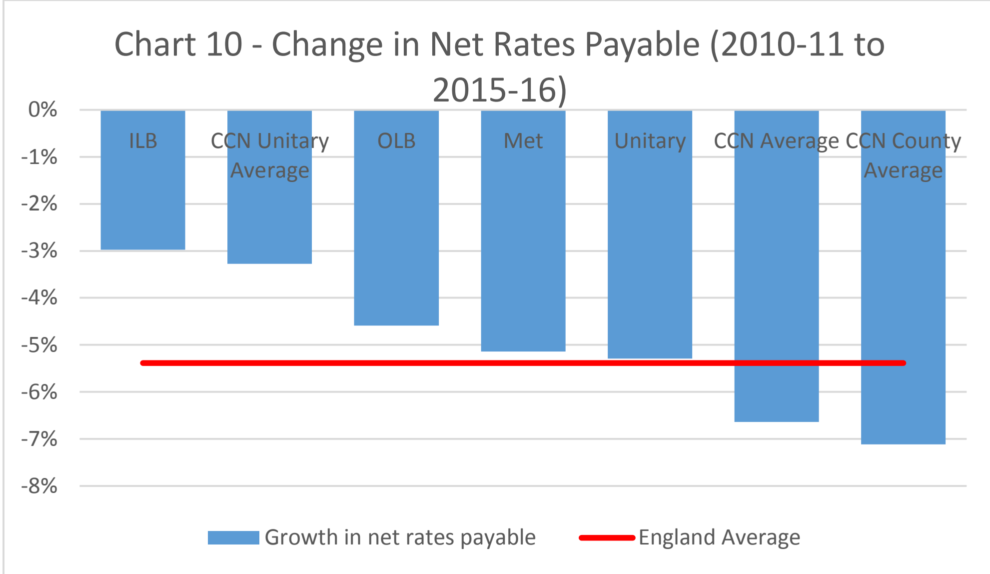
Chart 10 - Change in Net Rates Payable (2010-11 to 2015-16)
0%
-1%
-2%
-3%
-4%
-5%
-6%
-7%
-8%
ILB
CCN Unitary Average
OLB
Met
Unitary
CCN Average
CCN County Average
Growth in net rates payable
England Average

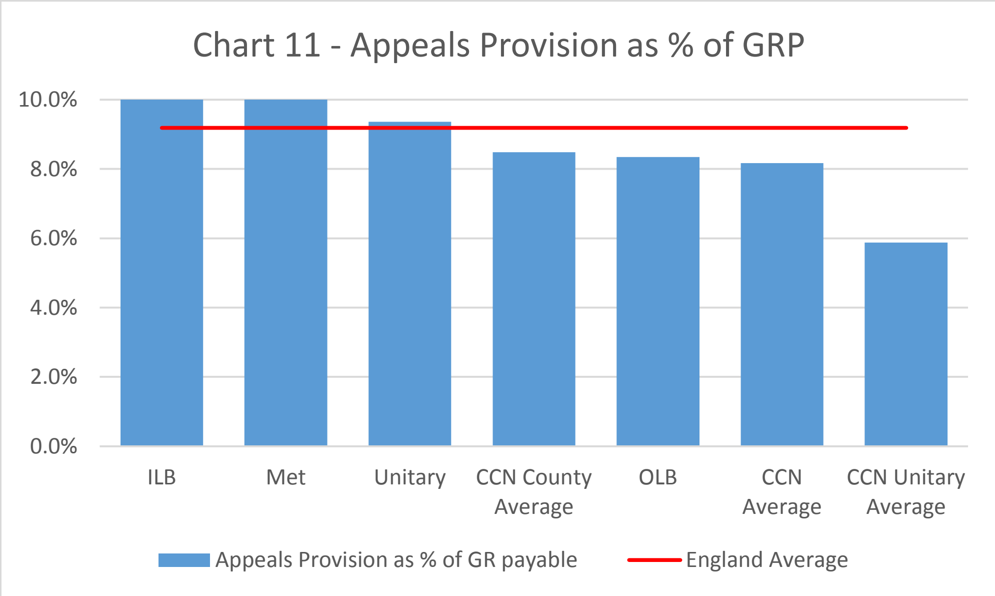
Chart 11 - Appeals Provision as % of GRP
10.0%
8.0%
6.0%
4.0%
2.0%
0.0%
ILB
Met
Unitary
CCN County Average
OLB
CCN Average
CCN Unitary Average
Appeals Provision as % of GR payable
England Average

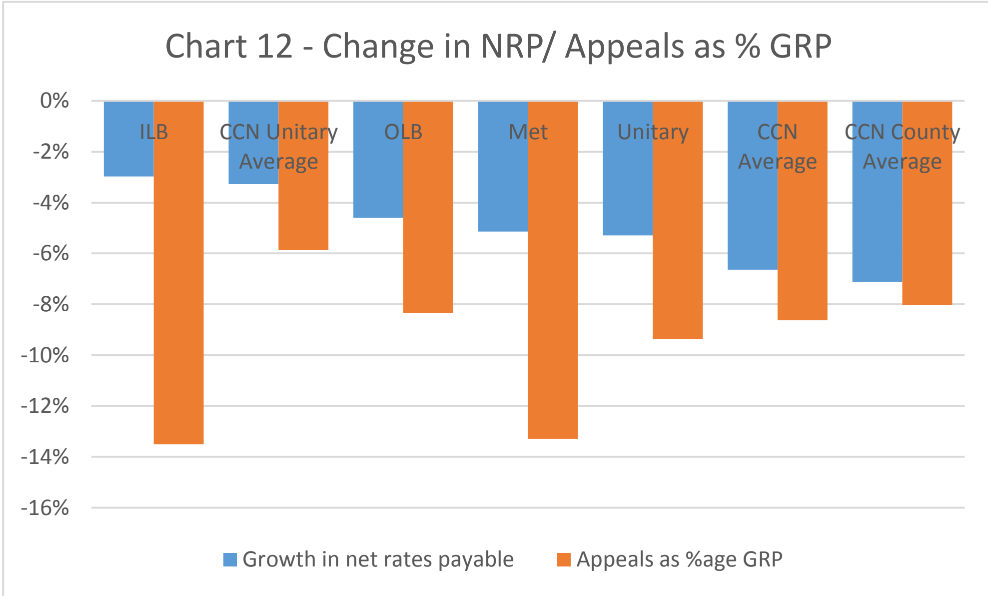
Chart 12 - Change in NRP/ Appeals as % GRP
0%
-2%
-4%
-6%
-8%
-10%
-12%
-14%
-16%
ILB
CCN Unitary Average
OLB
Met
Unitary
CCN Average
CCN County Average
Growth in net rates payable
Appeals as %age GRP

Analysis at authority level

31. **Chart 13** shows that every CCN authority – with the exception of Chester & Cheshire West and Oxfordshire – has rateable value per head that is lower than the national average (£1,058 per head). We can undertake some further research to establish the factors that this is correlated with but broadly the more rural authorities have lower rateable value per head, and those who are closer to urban centres to have higher rateable value per head. There are some exceptions for which there might be specific circumstances (for instance, we would expect Cumbria to have lower RV per head but it is possibly boosted by some very large local businesses such as Sellafield or BAE Systems in Barrow). Durham UA has the lowest RV per head which could be a combination of sparsity in the west of the authority and lower industrial values in the east.

32. Similar but more extreme patterns emerge in the comparison of NRP and GRP (**Chart 14**). Again, only a small number of CCN members are above the national average, albeit different authorities from the analysis of RV per head. On this occasion, the most rural authorities have by far the lowest proportion of NRP to GRP, especially those who are also distant from urban centres. There is a distinct cohort of authorities (with NRP under 84% of GRP) who could be characterised as the most-rural and most-sparsely populated authorities. Low proportions of NRP in these authorities will be largely caused by high levels of mandatory reliefs particularly for charitable organisations. Cornwall UA has a strikingly low rate of NRP to GRP (only 77%) which suggests that this county has a rate-paying organisations that are very reliant on mandatory reliefs (both charitable and small business reliefs).

33. **Chart 15** shows change in NRP between 2010-11 and 2014-15. This takes into account changes in rateable values (growth, closure), the impact of successful appeals, and changes in reliefs, including unoccupied relief. It is also adjusted for transitional relief. The range in growth within the CCN membership is huge (although we would expect to see a similar range in most groups of authorities). For those with the highest level of growth, in large measure this will be driven by a change in valuation at a specific hereditament (e.g. Sizewell power station in Suffolk).

34. There is no particular pattern to those that have seen growth and those that have not. There is no clear division between, say rural and urban, or with those authorities who are close to or further away from urban centres. But most CCN members have below-average growth in NRP (only 12 CCN authorities above the national average) and almost half (18 out of 37) have actually seen a reduction in NRP.

35. Understanding the diversity within the CCN membership is important. The funding system is now set up to benefit those with taxbase growth and to incentivise further growth. Creating a balanced lobbying position that reflects the range of CCN members' characteristics is no longer just about "needs" but has to also take the varying levels of growth into account.

36. We have looked in more detail at a number of county areas to show the range within individual counties. Eight counties have been selected to illustrate the range across the country (**Charts 16a to 16h**). The metrics we have shown for each county are:

- Change in rateable value. Many counties show very wide variations (see Worcestershire, with 20+% growth in Bromsgrove and 4% contraction in Redditch). Some counties are more closely clustered (see Northamptonshire). The more urban authorities tend to have lower growth than the surrounding rural area (see both Cambridge and Exeter). This urban effect is largely caused by the impact of appeals which are typically higher in these areas.

- Change in adjusted net rates payable. Patterns broadly reflect change in RV but also reflect repayments of appeals in respect of previous years. Some rural authorities experiencing large reductions as well as urban areas. The variation between counties is also interesting to note (Northamptonshire districts all have large reductions; increases or modest reductions in North Yorkshire).

- Appeals as a percentage of gross rates payable. Some significant outliers where there have been very large appeals relative to gross rates payable (Richmondshire, Tewkesbury).

- Percentage of net rates payable to gross rates payable. Rural authorities have higher reliefs (NRP compared to GRP), with somewhere like Torridge having reliefs that are worth almost three times more than Exeter. The exception to this is Cambridge, where reliefs are very high, but this could reflect the specific circumstances and organisations in Cambridge.

37. A note of caution – will future growth be the same as past trend? It probably will if it has not been distorted by a single revaluation in one property. We have been surprised by the growth (or lack of it) in some areas, especially in the Home Counties those around London; we were expecting counties such as Surrey to have grown more rapidly, for instance. A broader question is why economic growth generally – which is clearly very strong in the South-East – does not convert into growth in business rates?

38. A full schedule of all the relevant data for each CCN authority is supplied in **Appendix 2**.

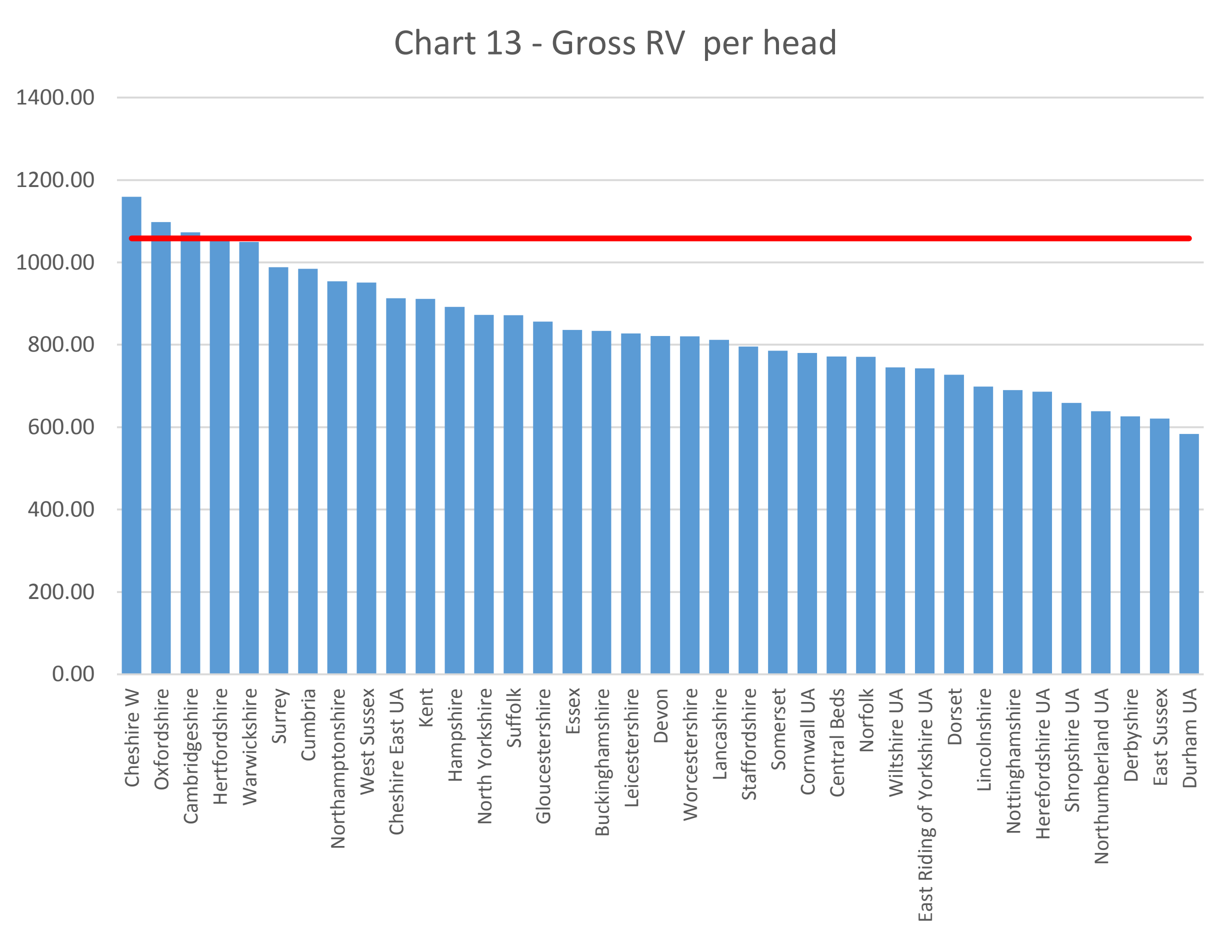
Chart 13 - Gross RV per head
1400.00
1200.00
1000.00
800.00
600.00
400.00
200.00
0.00
Cheshire W
Oxfordshire
Cambridgeshire
Hertfordshire
Warwickshire
Surrey
Cumbria
Northamptonshire
West Sussex
Cheshire East UA
Kent
Hampshire
North Yorkshire
Suffolk
Gloucestershire
Essex
Buckinghamshire
Leicestershire
Devon
Worcestershire
Lancashire
Staffordshire
Somerset
Cornwall UA
Central Beds
Norfolk
Wiltshire UA
East Riding of Yorkshire UA
Dorset
Lincolnshire
Nottinghamshire
Herefordshire UA
Shropshire UA
Northumberland UA
Derbyshire
East Sussex
Durham UA

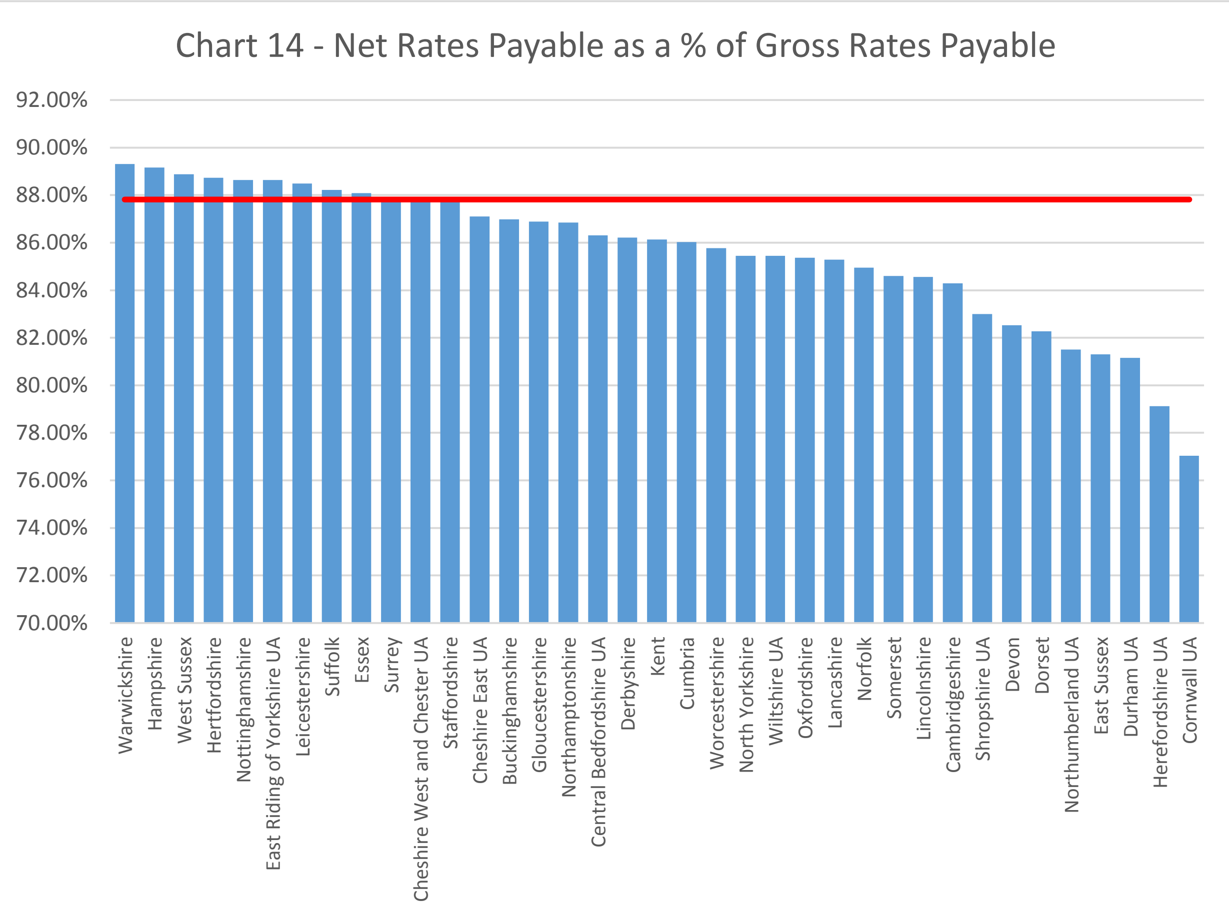
Chart 14 - Net Rates Payable as a % of Gross Rates Payable
92.00%
90.00%
88.00%
86.00%
84.00%
82.00%
80.00%
78.00%
76.00%
74.00%
72.00%
70.00%
Warwickshire
Hampshire
West Sussex
Hertfordshire
Nottinghamshire
East Riding of Yorkshire UA
Leicestershire
Suffolk
Essex
Surrey
Cheshire West and Chester UA
Staffordshire
Cheshire East UA
Buckinghamshire
Gloucestershire
Northamptonshire
Central Bedfordshire UA
Derbyshire
Kent
Cumbria
Worcestershire
North Yorkshire
Wiltshire UA
Oxfordshire
Lancashire
Norfolk
Somerset
Lincolnshire
Cambridgeshire
Shropshire UA
Devon
Dorset
Northumberland UA
East Sussex
Durham UA
Herefordshire UA
Cornwall UA

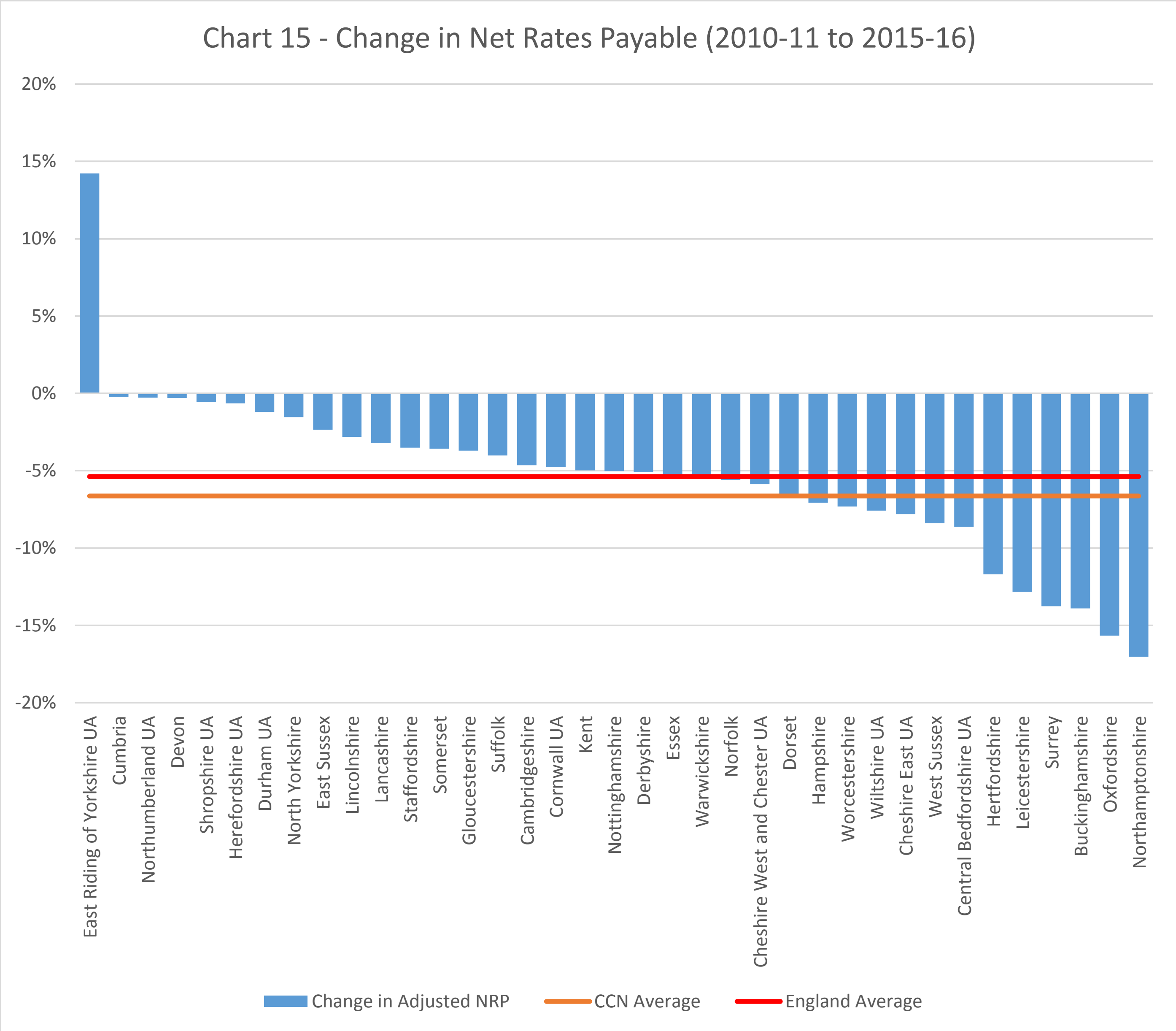

Chart 15 - Change in Net Rates Payable (2010-11 to 2015-16)
20%
15%
10%
5%
0%
-5%
-10%
-15%
-20%
East Riding of Yorkshire UA
Cumbria
Northumberland UA
Devon
Shropshire UA
Herefordshire UA
Durham UA
North Yorkshire
East Sussex
Lincolnshire
Lancashire
Staffordshire
Somerset
Gloucestershire
Suffolk
Cambridgeshire
Cornwall UA
Kent
Nottinghamshire
Derbyshire
Essex
Warwickshire
Norfolk
Cheshire West and Chester UA
Dorset
Hampshire
Worcestershire
Wiltshire UA
Cheshire East UA
West Sussex
Central Bedfordshire UA
Hertfordshire
Leicestershire
Surrey
Buckinghamshire
Oxfordshire
Northamptonshire
Change in Adjusted NRP
CCN Average
England Average

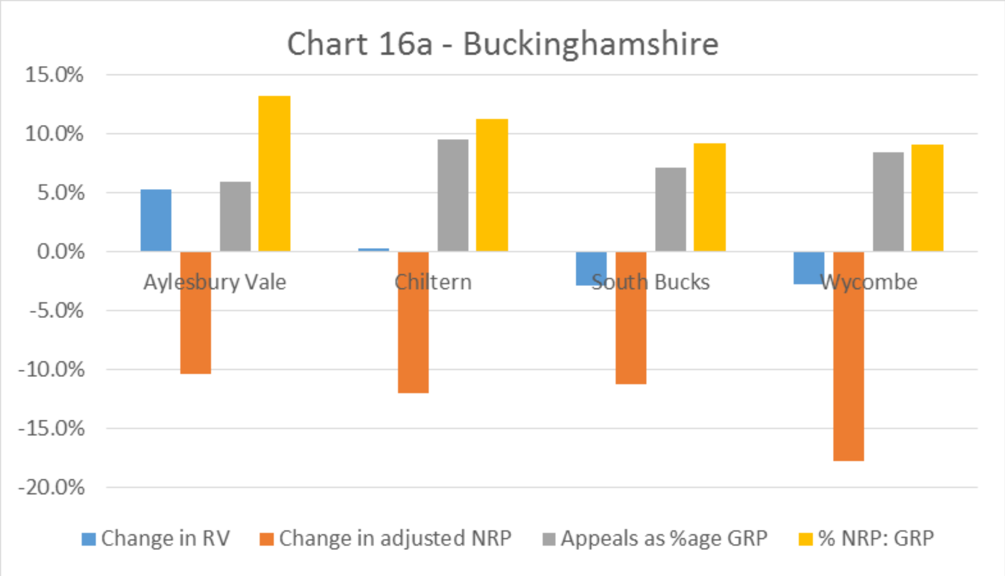
Chart 16a - Buckinghamshire
15.0%
10.0%
5.0%
0.0%
-5.0%
-10.0%
-15.0%
-20.0%
Aylesbury Vale
Chiltern
South Bucks
Wycombe
Change in RV
Change in adjusted NRP
Appeals as %age GRP
% NRP: GRP

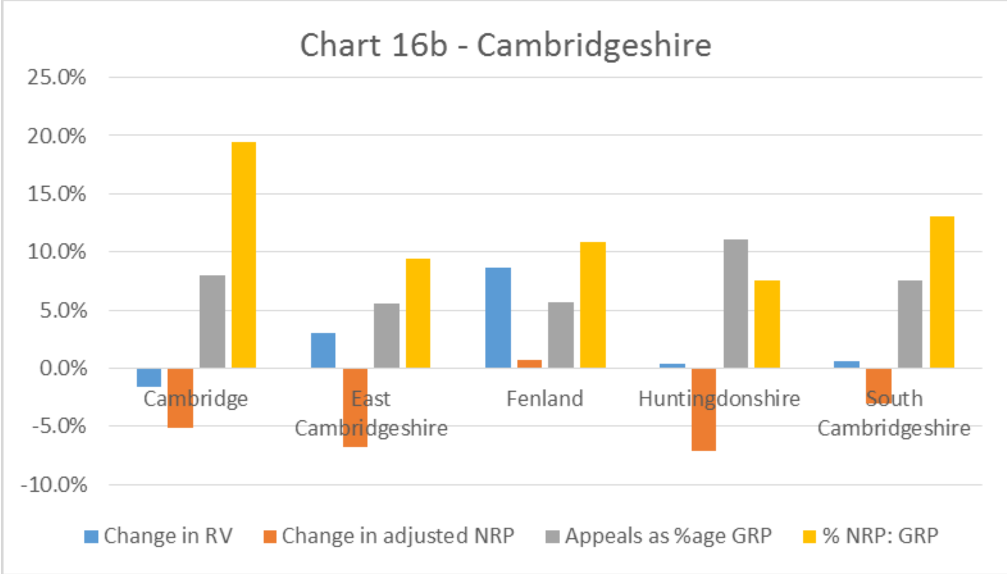
Chart 16b - Cambridgeshire
25.0%
20.0%
15.0%
10.0%
5.0%
0.0%
-5.0%
-10.0%
Cambridge
East Cambridgeshire
Fenland
Huntingdonshire
South Cambridgeshire
Change in RV
Change in adjusted NRP
Appeals as %age GRP
% NRP: GRP

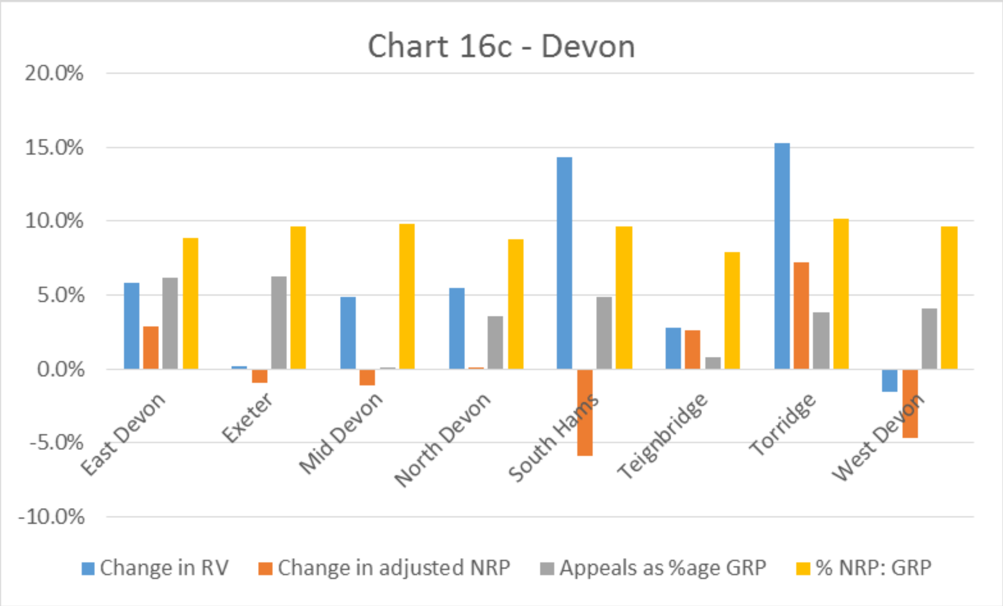
Chart 16c - Devon
20.0%
15.0%
10.0%
5.0%
0.0%
-5.0%
-10.0%
East Devon
Exeter
Mid Devon
North Devon
South Hams
Teignbridge
Torridge
West Devon
Change in RV
Change in adjusted NRP
Appeals as %age GRP
% NRP: GRP

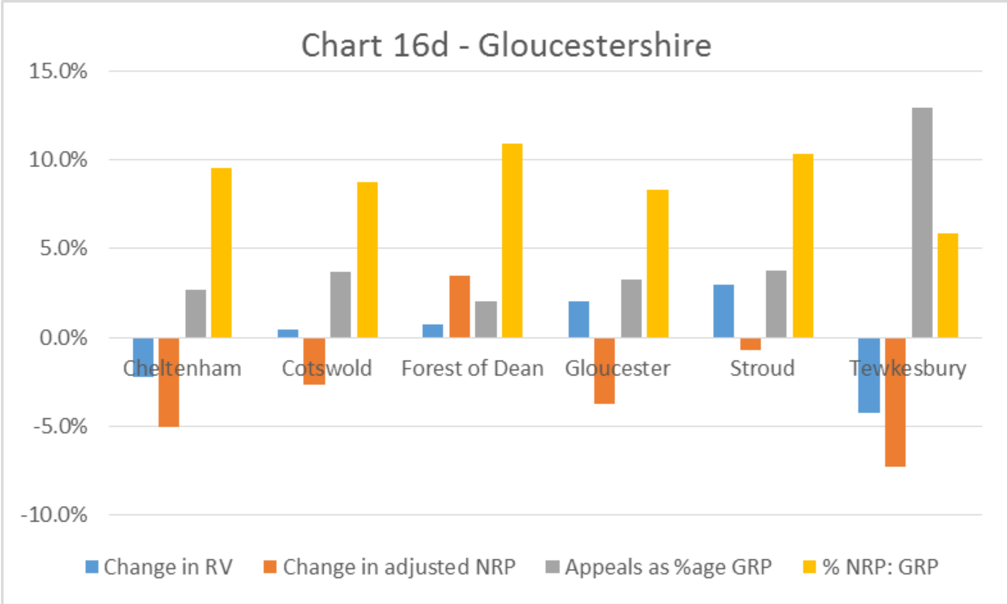
Chart 16d - Gloucestershire
15.0%
10.0%
5.0%
0.0%
-5.0%
-10.0%
Cheltenham
Cotswold
Forest of Dean
Gloucester
Stroud
Tewkesbury
Change in RV
Change in adjusted NRP
Appeals as %age GRP
% NRP: GRP

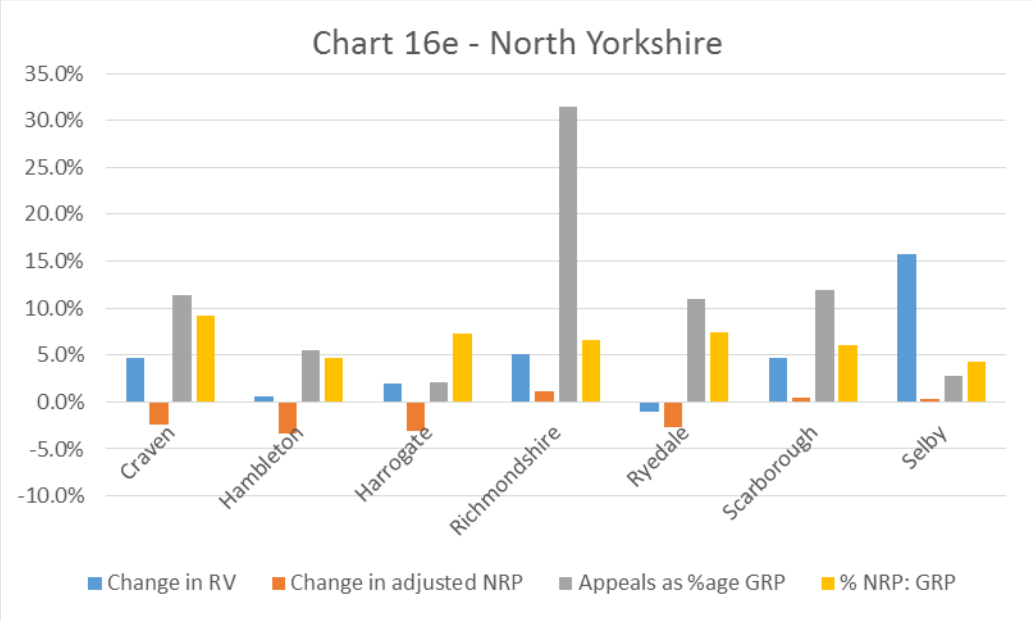
Chart 16e - North Yorkshire
35.0%
30.0%
25.0%
20.0%
15.0%
10.0%
5.0%
0.0%
-5.0%
-10.0%
Craven
Hambleton
Harrogate
Richmondshire
Ryedale
Scarborough
Selby
Change in RV
Change in adjusted NRP
Appeals as %age GRP
% NRP: GRP

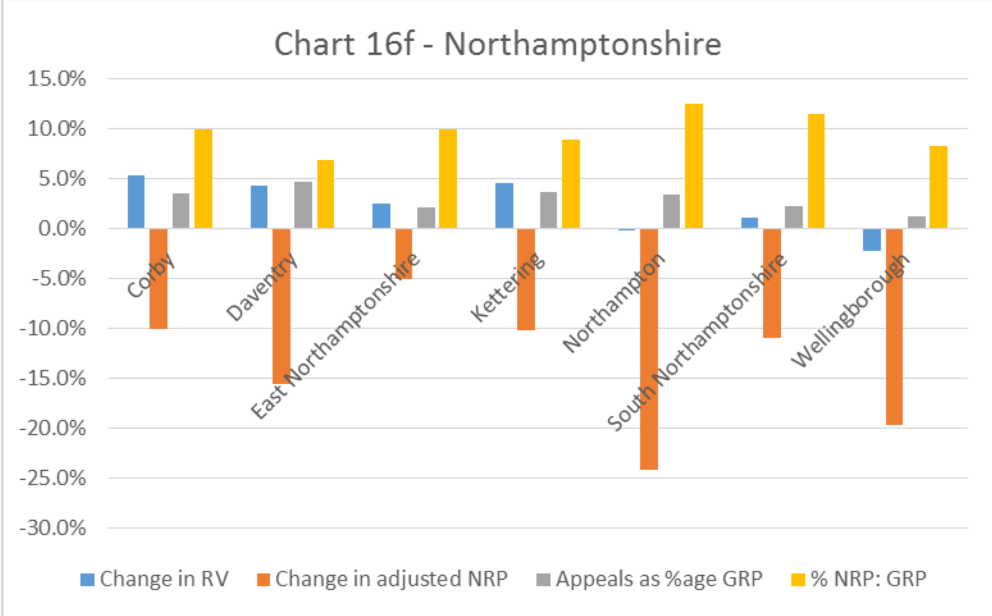
Chart 16f - Northamptonshire
15.0%
10.0%
5.0%
0.0%
-5.0%
-10.0%
-15.0%
-20.0%
-25.0%
-30.0%
Corby
Daventry
East Northamptonshire
Kettering
Northampton
South Northamptonshire
Wellingborough
Change in RV
Change in adjusted NRP
Appeals as %age GRP
% NRP: GRP

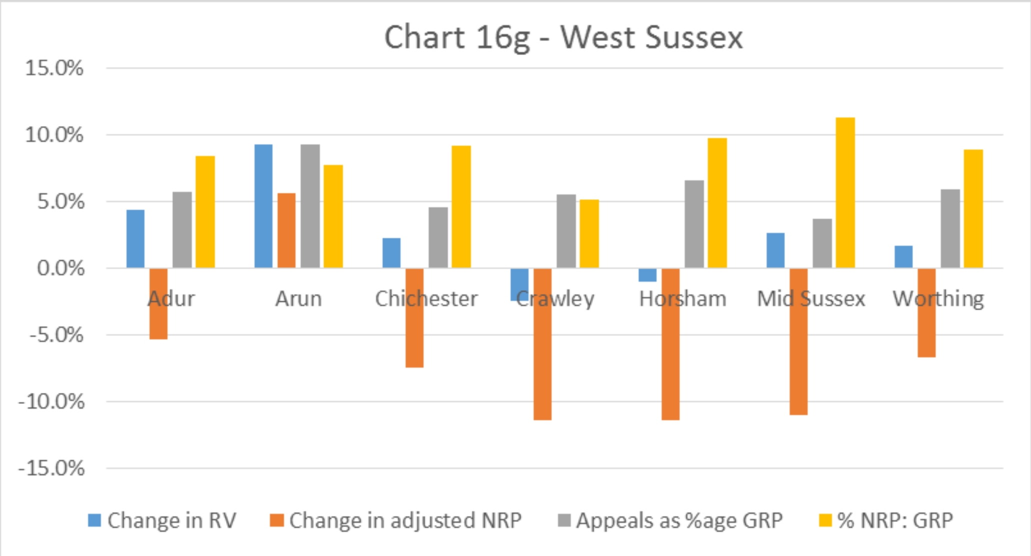
Chart 16g - West Sussex
15.0%
10.0%
5.0%
0.0%
-5.0%
-10.0%
-15.0%
Adur
Arun
Chichester
Crawley
Horsham
Mid Sussex
Worthing
Change in RV
Change in adjusted NRP
Appeals as %age GRP
% NRP: GRP

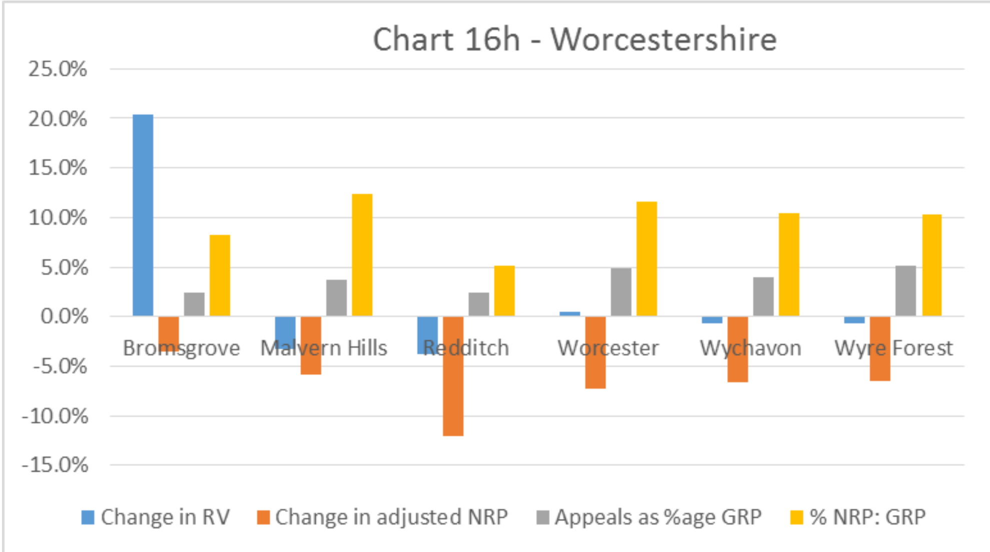
Chart 16h - Worcestershire
25.0%
20.0%
15.0%
10.0%
5.0%
0.0%
-5.0%
-10.0%
-15.0%
Bromsgrove
Malvern Hills
Redditch
Worcester
Wychavon
Wyre Forest
Change in RV
Change in adjusted NRP
Appeals as %age GRP
% NRP: GRP

Operation of retained rates system

39. With the exception of four authorities, all the CCN authorities are top-up authorities.[1] CCN authorities in aggregate have a funding baseline (2014-15) of £2.9bn, of which in aggregate £1.7bn is provided through a top-up. The average top-up for the CCN authorities in aggregate is 59%.

40. When growth is low, negative or volatile, being in a top-up position is beneficial. It means that, on average, 59% of the income to CCN authorities through the rates system is provided via a transfer payment from other tariff authorities. This income is provided without any variation or any risk. (The downside is that top-up authorities are less likely to benefit from above-target growth.)

41. The move towards 100% retention is likely to increase the share of rates retained by county councils. As the balance changes, it is likely that the top-ups will reduce as well.

42. Top-up authorities do not pay a levy on business rate income that is above target. Again in the few authorities where above-target retained income has occurred, all the growth can be retained. The Government is proposing that levies will be abolished when 100% retention is introduced: CCN authorities in the main will not experience any benefit from this change; the exception will be the four tariff authorities.

43. The only CCN authorities who have paid a levy on above-target growth are unitary councils (Central Bedfordshire, Cheshire East, Chester and Cheshire West, and Wiltshire). These councils are the four tariff authorities and they would be the only authorities amongst the CCN membership who would benefit from the removal of the levy.

44. Based on our funding model, no CCN authority has received a safety net payment. This is because CCN authorities are relatively large and are top-up authorities, which means that the percentage reduction in rates would have to be very large indeed to exceed 7.5% of an authority's funding baseline. In addition, large reductions in rates in large authorities have tended to be absorbed.

45. We estimate that 14 out of the 37 CCN authorities were in a business rate pool (2014-15).[2]

Estimating the "quantum" for 100% rates retention

46. The move to 100% rates retention will increase the resources available to local government. The Government wants to ensure that the change is "fiscally neutral" and so will transfer functions or funding responsibilities to local government. In other words, the cost of funding these "new burdens" will transfer from general taxation to local taxation.

47. Estimating the responsibilities that have to transfer will be dependent on a number of factors:

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[1] Central Bedfordshire, Cheshire East, Chester & Cheshire West and Wiltshire. All are unitary councils who are already retaining 49% of their business rates.

[2] Local Government Finance Report, 2014-15.

- Estimated business rates collected by local authorities. We assume this will be based on the actual collection in 2019-20. The amount will depend on change in rateable values, uplift in the multiplier (in line with RPI), change in reliefs, and losses in collection.
- Amounts that have to be retained separately. Authorities are able to keep 100% of the rates for renewable energy and in Designated Areas.
- Impact of revaluation. Revaluation will not result in an increase in yield nationally because the expected increase in rateable values will be offset by a reduction in the multiplier. It will however result in changes in the rateable values in each authority. The effect of appeals on the new rating list is more difficult to estimate.
- Planned cuts in local government funding. Between now and 2020-21, the Government is expecting to make funding cuts. Revenue Support Grant (RSG) will reduce from £9.5bn to £2.1bn.
- Rolling-in other grants. The Government is looking to fund as much as possible from retained rates, so other existing grant funding could also be rolled-in. This could include New Homes Bonus and section 31 grants currently funding business rates reliefs.
- Central list properties. These are large properties (e.g. some power stations) or network properties (e.g. cabling) that is paid centrally rather than through the local lists that are administered by local authorities.

48. The Government's latest estimate is that the "quantum" could be between £8bn and £12bn, and that there is a margin of error of +/-10% across the period of a rating list (i.e. 5 years). The margin of error is largely, we assume, because inflation and the resulting increase in the multiplier is difficult to predict with any accuracy.

49. Based on the approach outlined by the Government, we have made our own estimates and applied this methodology to CCN authorities (**Table 1**). Using these estimates, for illustration, the quantum would be £11.1bn.

Table 1 – Estimated "quantum" for 100% retention

	2020-21
	£m
Collectible rates	27,888
Transitional protection	
Cost of collection	-96
City of London offset	-13
Designated Areas	-26
Renewable Energy Schemes	-24
Non-Domestic Rating Income	**27,729**
Central List	0
Total Rates	**27,729**
Central Share	**13,864**
RSG	-2,130
New Homes Bonus	0

Section 31 grants	*-596*
Total grants	**-2,726**
QUANTUM	**11,139**

50. Converting this methodology into estimates for CCN authorities is dependent on the increase in retention for county councils and district councils. Currently the balance is heavily in favour of districts, who retain 40%, compared to only 9% in county councils (and 1% for fire functions). The balance under 100% retention will depend on Government decisions on:

    - Functions transferred. We discuss these in more detail in the next section. If the transferred functions, particularly growth functions, are "upper tier", then this would imply a corresponding increase in the retention rate for county councils.
    - Financial risk. Many district councils already have retained rates that are very large compared to their Funding Baseline, and increasing district councils' share would increase this risk. For CCN authorities, there is already significant risk in adults and children's social care and waste disposal, and increasing exposure to business rates would increase their overall financial risk.
    - Responsibility for economic development. Given the link to business rate growth the share in retention could be seen to reflect the capacity of the tier to drive and deliver growth.

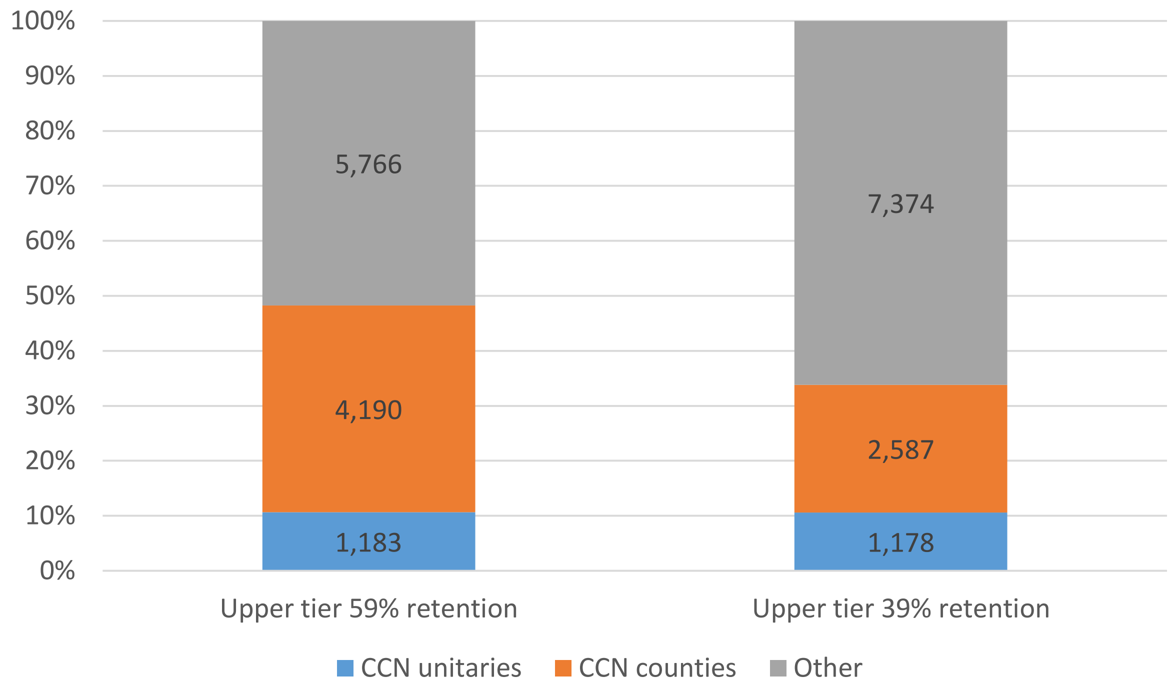
51. We have modelled two scenarios:

    - No increase in district councils' retention rates, with counties increasing to 59%.
    - An increase in district councils' retention rates to 60% and counties to 39%.

52. In the first scenario the "quantum" would be £5.4bn (48.2% of the national total) and in the second the "quantum" would be £3.8bn (or 33.8%) (**Chart 17**).[3] There is no difference for any of the unitaries because their share includes both the upper and lower tier elements (Cornwall and Northumberland would also have a fire share). The difference for county councils is marked, however (£4.2bn compared to £2.6bn).

[3] CCN authorities have about 37% of the rateable value and net rates, so it is surprising that it should have as much as 48% of the increase in quantum. Largely this is explained by having a smaller share of both RSG and Section 31 grants. Some further work will need to be undertaken at finer detail to establish more accurate amounts.

Chart 17 - Estimated "quantum" for CCN authorities (£m)



53. The additional quantum estimated here is much greater than the current top-ups received (in aggregate) by CCN authorities. Aggregate top-ups for CCN authorities are only just over £2bn, so an increase under any of the scenarios above would exceed the existing top-ups. This suggests that CCN authorities – including county councils – will become tariff authorities under 100% retention, unless they get high share of new burdens or change in needs assessments.

54. As an example, CCN authorities receive 35% of public health grant, whilst we estimate that they will receive 48% of potential increase in quantum. If there was no change in the needs formula and CCN authorities received a lower share of new burdens than they did of the additional quantum then it would be likely that this would turn most if not all into tariff authorities.

55. Unless CCN authorities get the "right" new responsibilities, the result of the move to 100% retention might be greater exposure to business rates risk without much in return, other than the potential to gain from growth above baseline. CCN authorities could find themselves making significant transfer payments (through tariff payments) to fund needs and spending elsewhere in the country.

New burdens

56. A number of candidates for transferring to local government have been put forward by the Government. A menu of options is being developed with the focus on getting a list of appropriate new responsibilities rather than trying to match the estimated quantum exactly. The value of the candidates proposed initially (Table 2, Appendix 3) are already much higher, at £17.4bn, than the quantum will be. We have allocated each of the proposed candidates to a category and identified which tier of local government would be take responsibility. A detailed list provided at Appendix 3.

Table 2 – Potential new responsibilities to transfer to local government

Category		Responsibility	Comment
Adult education	£2.2bn	Upper tier	Not demand led
Benefits	£1.8bn	Mostly lower tier	Heavily demand led and tied into national benefits policy. (Attendance Allowance probably upper tier)
GLA Transport Grant	£1.0bn	GLA	Bespoke devolution deal
Highways and transport	£0.6bn	Upper tier	Not fully demand led and ability to control costs. Funding available likely to be higher than £0.6bn
Other	£2.5bn	Various	Only devolution deals amount is of any size
Public health and social care	£4.8bn	Upper tier	Largest potential block of funding and public health is most likely to occur. High risk in terms of demand and policy
Schools	£3.9bn	Upper tier	Early years likely to be demand led
TOTAL	**£17.4bn**		

57. If CCN takes the view that the retention rate for its authorities will increase, then it will want to promote options where :

    - CCN authorities have a high share of the funding and the capacity to drive better outcomes locally. Highways, (potentially) transport and (potentially) adult education are good options, as might some aspects of older people's social care. Benefits in particular should be avoided because funding in deprived areas will be much higher.
    - Spending is not demand-led and can be controlled (to some extent). Again highways, transport and adult education are good options, as is public health. Benefits, social care, and Better Care Fund should be avoided because there is demand risk and policy risk (changes in operation from central government).

58. DCLG and LGA has proposed criteria that new burdens should be assessed against. These are reasonable and sensible criteria.

59. Highways, transport and adult education appear to be the most attractive options for CCN. They should also score well against the criteria that the DCLG has proposed. There is some scope to increase the funding that might be allocated through highways (e.g. by increasing the highways maintenance funds). Highways and transport also link in well with the infrastructure and economic development role of local councils.

60. Public health could be considered as a reasonable option, mostly because spending is not demand led and can be controlled, although the share is relatively low for CCN councils. It is worth noting however that this is not a 'new responsibility' as upper tier councils already deliver public health, it would be a transfer of funding from central to local taxation.

61. Finally, there might be some specific infrastructure proposals that CCN authorities might want to get funded through increased rate retention.

Growth in spending pressures

62. As part of the introduction of 100% retention, the DCLG has an objective of trying to match growth in spending pressures and with growth in business rates income. This is not the same as ensuring fiscal neutrality in every year (only the first year) but it would try to ensure that business rate income could keep pace with increases in local authority spending. This would include both existing spending pressures and the transfer of any new responsibilities.

63. We understand that civil servants would like to minimise both the future grant funding from Government to local government (which suggests rolling-in existing grants where possible) and the necessity for local government to have to ask for additional funding in future. In other words, the move to 100% retention should seek to make local government as sustainably self-sufficient as possible.

64. The underlying real-terms growth in business rates is low:

- Rateable values. Growth in RV was 1.6% between 2010-11 and 2015-16.
- Net Rates Payable (real terms). Reduced by 5.4% between 2010-11 and 2015-16.
- Net Rates Payable (cash terms). Increased by 11.6% between 2010-11 and 2015-16. This includes increases in the multiplier in line with the September RPI.

65. **Table 3** shows an estimate for the increase in net rates for CCN authorities based on actual growth in net rates including the increase for the multiplier since 2010-11. As we have seen above, there has been a reduction in Net Rates Payable in real terms because of the impact of appeals and cash refunds during the period of the rating list. Including the increase in the multiplier means that the median increase in NRP would be 2.4% (based on performance in the 2010 list).

66. However, the range between the highest and lowest cash-terms annual increase is striking, from 6.9% (East Riding of Yorkshire) to minus 2.1% (Northamptonshire). Those with the highest levels of growth would generate substantial real-terms increases in spending power. All authorities would expect to receive an increase in spending power from the natural increase in business rates, albeit real-terms falls in some cases. For some authorities, the cuts in funding would be substantial, albeit supported to a limited degree by the business rates safety net, assuming such a mechanism is in place.

Table 3 – Estimated annual growth in Net Rates (CCN Authorities).

Cash terms growth (incl increase in multiplier)	Increase in Net Rates Payable (2010-11 to 2015-16)	Average annual increase in Net Rates Payable
Max	34.7%	6.9%
Upper quartile	14.6%	2.9%
Median	12.0%	2.4%
Lower quartile	9.0%	1.8%
Min	-2.1%	-0.4%

67. In the context of recent cuts in funding, these increases in spending power look reasonable. They represent cash-terms increases in spending power for every authority, and real-terms

increases for more than half. However there are risks to this position – revaluation, appeals, business closure. To business rates income should be added council tax income (which is more stable than business rates and grows slightly more quickly, on average 0.75% per year).

68. An additional question for CCN authorities – particularly county councils – is whether the growth in business rates and council tax income will match the growth in demand-led services such as social care. In a report for CCN by LG Futures, data was used to show that there will be an increase in demand for social care, and that this will be higher in CCN authorities than the average for the rest of the country for older people:

    - In the five-year period to 2013-14, the number of contacts in CCN authorities increased by 8.5, compared to 2.3% for England as a whole.
    - CCN authorities are projected to grow more quickly than the comparator groups. Over the next five years, the number of older residents in CCN authorities is projected to rise at an average annual rate of 2.0%, compared to the England average of 1.8%. This is also faster than the London boroughs (1.9%), other unitary authorities (1.9%) and metropolitan boroughs (1.5%).
    - To estimate the impact of population growth on local authority spending, it is assumed that there is a one-to-one relationship between growth in the number of older residents and expenditure on older people's social care. This rule of thumb is supported by some statistical evidence.

69. Added to increases in unit costs, the average increase in spending on adult social care for CCN authorities is likely to be somewhere between 4% and 5% per year (2.0% growth in demand and 2%-3% increase in unit costs). For all but three CCN authorities (based on past performance), the growth in business rates income will be less than the growth in adult social care pressures.

70. This is a rough-and-ready approach to estimating the financial impact on CCN authorities, and many more factors will have to be taken into account when judging the financial capacity of authorities to fund the growth in social care. As examples, we would need to see the growth in funding from other sources, the ability to raise more from council tax, and the proportion overall spending that is consumed by social care.

71. But clearly there is a significant mismatch between the growth in a demand-led service such as social care and the growth in business rates and other sources of income available to local authorities. CCN will want to continue to press central government for additional funding for social care but it is likely that any such funding will have to come from outside the rate retention system. A parallel strategy would be to minimise the financial impact of 100% rate retention on local government – including CCN authorities – by asking for new upper tier responsibilities that can be easily controlled, are not demand-led and can be cut back if necessary. This would improve the balance of risk within local authorities, particularly county councils.

Governance and responsibilities

72. The Government is considering whether to operate some elements of the funding system at regional or sub-regional level. This could apply to any or all elements of the funding system, including needs and retained rates. It could operate at various levels: e.g. region, combined authority or county.

- It would make the national funding system simpler: funding allocations would have to be made to fewer funding "blocks", and the difference in need and resources between these "blocks" would be less than the difference between individual authorities. There would be less requirement for transfer payments between "blocks", such as top-ups and tariffs. A simpler system could incorporate a flatter funding methodology which would benefit most CCN authorities.
- Risk and volatility would be reduced because they could be absorbed across a wider area: high-growth areas could offset low-growth areas or large business closures. For CCN, there would be benefits in operating the retained rates system because the uncertainty of the rates system could be shared or pooled.
- Resources would have to be distributed within the region or sub-region. This would include both resources and funding for needs. Of course this raises local political issues where significant decisions have to be made using local governance structures (which might not yet exist). Distribution at this lower level would almost certainly be inconsistent across the country, leading to very different funding per head for the same services in similar areas.

73. In summary, the proposal has merits for CCN. It could potentially lead to a favourable funding settlement and it has practical benefits to authorities because risks and volatility can be shared. Caution should be exercised in the structures that need to be in place and the variation in funding that local decisions could lead to. Individual circumstances should be examined further and an understanding should be gained as to how this would work within the CCN membership before taking it any further. To take a few examples:
    - Is the proposal only workable where there is going to be a formal governance structure to cover the proposed area, e.g. an elected mayor or a combined authority?
    - Can the proposal work at county level, and if so, who takes decisions about funding or allocating resources?

74. A related question is to determine which tier of local government controls any changes in the multiplier or reliefs, who pays for the cost and who sets the overall economic development strategy. Clearly there ought to be alignment between these elements of the system but this may not be easy to achieve in two-tier areas, or where there are devolution arrangements that straddle more than one county or unitary. Here we consider some of the changes that could be made locally, who should make that decision, and who bears the cost or controls the additional income:
    - Multiplier. There will be local powers to increase or reduce the multiplier. It is expected that these powers to raise the multiplier will only be available to elected mayors, but it is possible that they are also available to reorganised counties. The Government is clearly signalling that the power to increase the multiplier is used at the sub-regional level and that it is (rightly) subject to significant scrutiny.

      An increase in the multiplier to fund investment in infrastructure (e.g. business rates supplement used by GLA to fund Crossrail) would involve the combined authority/ mayor/ reorganised county controlling the additional resources generated by the increase in multiplier. The converse would have to be the case for a reduction, with a combined authority/ mayor/ reorganised county compensating the collection fund (and thereby the other councils) for the lost revenue.

- Reliefs. There will be more flexibility over reliefs. This is most likely to be for specific business sectors and in specific areas (i.e. to attract new companies or support existing ones). Also possible but less likely is an overall change in policy on, say, charitable relief.

  Any type of council – district, county, unitary, combined – ought to be able to instigate or sponsor a change in reliefs. The sponsoring council ought to pay the cost, or negotiate a cost-share with other interested parties. Any benefits arising from the reliefs could also be linked (for example, where the relief is designed to attract new businesses; using some or all of the subsequent uplift in business rates might be required to fund the cost of the relief).

- Displacement effects. Reliefs or reductions in reliefs in one part of an area can attract businesses from within an area (say, within a county or within a combined authority). This is difficult to prove and any compensation would only be payable on a voluntary basis.

75. It is difficult to determine the cost of local changes and their allocation between authorities because they interact with each other. For example, reducing the multiplier (which could be an upper tier or combined authority decision) will reduce the cost of an area-based relief (potentially a district council decision); untangling the allocation of costs is almost impossible and will be costly in operational terms. Simplicity is better if it is possible and acceptable to all parties. It could operate using a simple estimates system updated annually for some agreed data; the responsible council would either make an agreed contribution to the collection fund, or precept an agreed amount on the collection fund to invest in agreed outcomes. There would be some rough justice but there would be a reasonable balance between fairness and simplicity.

76. Reliefs are much more flexible and targeted, and are almost certainly better suited to attract new businesses or to support those that are already there. They can, for instance, be targeted at a specific location, at certain types of business and even at relocating businesses. Changes in the multiplier are better suited – in most cases – to raising additional resources to reinvest. Any changes in multiplier are more likely to be increases rather than decreases.

77. Decisions about setting the multiplier or introducing local reliefs should really line up with responsibilities for economic and business development in two-tier areas. Having potentially conflicting changes in reliefs and multiplier could hamper efforts at economic development or attracting new businesses. In addition, conflicting or poorly designed schemes are not good value for money for the local taxpayer.

78. It is difficult though to draw clean lines of responsibility in two-tier areas without excluded either counties or districts entirely. Of paramount importance will be having an economic and business development plan that coordinates the efforts of counties and districts. Any new reliefs or changes in the multiplier should fit with this overarching plan. Some pointers to how the responsibilities would be allocated: decisions about the multiplier to be taken at a regional or sub-regional level (with the county being the lowest level at which this could reasonably be taken); there might be occasions when a district council might want to increase the multiplier in

order to invest, but this can be handled through a Business Improvement District); and both county councils and district councils should be able to introduce local reliefs.

79. Getting parity between upper and lower tier retention rates would help as well with costs more evenly shared without any further intervention. We have exemplified the effect of the district/ county (including fire) split being 40/60 and 60/40, but this could equally be 50/50.

Conclusions and recommendations

80. There is a concern for CCN that the future growth in business rates will be concentrated in too few areas of the country, particularly central London. Past growth patterns tell part of the story (it has been higher in London than anywhere else in the country) and future growth is likely to be even more skewed, particularly with growth in central London following Crossrail. Rateable values per head are much higher: £3,700 per head in inner London compared to £851 per head for CCN authorities, indicating that growth will be much more valuable in inner London.

81. Although rateable values have performed relatively well in CCN authorities compared to the rest of the country, growth in Net Rates Payable has been below average. There also is a wide variety of characteristics, from very high levels of growth in the East Riding of Yorkshire to large reductions in Northamptonshire. Many CCN authorities, particularly in rural areas, have many business rate payers claiming reliefs; these are often small or rural businesses. As a result, growth in business premises often does not translate into growth in business rate income received by the local authority.

82. CCN wants to ensure that urban authorities (especially in central London) do not retain too high a share of "national growth". The government has already announced that levies on above-target growth will be abolished, allowing all growth to be retained locally. Clearly this would not favour most CCN authorities, and would result in an unfair and uneven distribution of growth across the country. CCN will want to:

    - Ask government to review its decision to abolish the levy, or at least to review the impact of this decision in the context of other changes to the scheme.
    - Explore options for more-frequent and fuller baseline resets (at least every 5 years) that would allow growth to be more evenly distributed whilst retaining a reasonable incentive-effect. Ideally there would be some relationship between the underlying ability to increase business rates and the proportion that an authority is able to keep.
    - Ensure there is proper allowance within baselines to reflect the impact of appeals over the lifetime of the rating list. The proposal to fund the costs of appeals nationally should be resisted because the benefits will flow much more to inner London and other Met areas than to CCN authorities.

83. Once 100% retention is introduced, local authorities to have to fund any increase in reliefs, such as charitable relief, even where these are mandated by legislation. Reliefs are higher in rural than urban areas, with reliefs accounting for up to 25% of gross rates in Cornwall. On average they account for an average of 10.9% in CCN authorities and only 7.3% nationally. Given the higher proportion of reliefs in many CCN authorities, it would only be fair if the government continues to fund its share of growth in mandatory reliefs. More generally, CCN authorities in

more rural parts of the country will want to make sure that the government continues to support businesses and organisations that are essential in rural areas.

84. In future, all local government spending will have to be funded from a combination of council tax and business rates. It is therefore vitally important that growth in local resources is similar to growth in spending pressures. This is particularly important for CCN authorities where social care is such a large proportion of local budgets. Based on past-years' trends, growth in social care spending is likely to be between 4%-5% (2% for growth, 2-3% for unit costs). On its own, this is likely to be greater than the growth in local taxation. And with the highly variable growth rates in taxbases – particularly business rates – the gap between growth in resources and spending pressures is likely to be very large in some CCN authorities.

85. CCN will want the government to take particular care in forecasting future spending pressures in social care and in waste disposal, and ensuring that these can be properly funded. The government must look at the financial position of every council, including the outliers, and assess whether the councils with the largest reductions in net rates payable (e.g. Northamptonshire, which has the largest reduction of any CCN member) will impair the ability of individual authorities to set balanced budgets.

86. The government is proposing a range of potential services or funding that could be transferred to local government: this is to ensure that the increase in retention to 100% is "fiscally neutral". It is estimated that some £11bn of new burdens will have to be transferred, although this is based on a projections. Most of the proposed new burdens are for upper tier services, such as public health grant or highways. CCN authorities will want to be able to scrutinise these proposals carefully to ensure that they do not place an unfair burden on local finances both at the point of transfer and in future years. Ideally, CCN authorities would prefer transfers where there is local discretion over spending.

87. If the bulk of transfers are to upper tier authorities, then the presumption will be that retention rates will increase for county councils (in two-tier areas) and possibly not at all for districts. This will change the relationship between county councils and the growth risk in its area, and will also expose authorities to greater risk. This opens up opportunities to CCN authorities – particularly where there is the prospect of growth in business rates – but clearly also creates additional risks, which, when combined with social care risk, could be judged too great.

88. If the risk on CCN authorities is increased, then it is reasonable that CCN would be looking for assurances that there are sensible ways of managing risks (e.g. safety net, appeals) or for re-assessing funding more generally. Greater support might be required for authorities with social care responsibilities.

Appendix 1 – Explanation of Business Rates Retention scheme

Operation of the current rates-retention scheme

The current rate retention regime was introduced in 2013-14. Before this, a nationalised business rates system operated whereby local authorities acted as collection agents for central government; business rates were collected locally, pooled nationally and then redistributed to local authorities through Revenue Support Grant (and other grants). Under the rate-retention system introduced in 2013-14, local government retains 50% of business rates, with the remaining 50% being paid over to central Government (and returned to local government through RSG and other grants).

Within local government, different rate retention amounts are set for different functions. District functions retain 40%, upper-tier functions 9% and fire functions 1%. A unitary council with fire functions will retain 50% of rates. A district council will retain 40% of rates. A county council will only retain 9%, unless it still has fire functions, in which case it will retain 10%.

Importantly, there is still rates equalisation in the system, otherwise the authorities with the largest rate bases would have far too much income for their needs, and most of the rest of local government would have too little. To adjust for the massive differences between rates collected and needs, the Government still sets a needs target and a business rates target for each authority.

- Where the business rates target is greater than the needs target, then the authority pays over a **tariff** into the national pool; and
- Where the needs target is greater than the business rates target, then the authority receives a **top-up** from the national pool.

Across the whole country, top-ups and tariffs balance each other out; the system of transfers between authorities balances out the differences between needs and income potential. Top-ups and tariffs – and the underlying needs and rates targets – are fixed until 2020 and only uprated each year by the increase in the national business rates multiplier (usually the Retail Price Index from the previous September).

There is protection – a safety net – for authorities whose business rate income falls significantly in any one year. The threshold for the safety net is set at 92.5% of the authority's baseline funding level.

Levies are also payable by authorities on business rates that are collected above their rates target. The levy rate is calculated by comparing the needs target with the rates target. If the rates target is, say, £25m and the needs target is £20m, then the rates target is 25% greater and the levy for the authority would be 25% (i.e. the authority would pay over to central government 25% of any business rates is collects over-and-above the business rates target). The levy rate is capped at 50%. For any authority whose needs target is lower than their rates target (i.e. all top-up authorities), no levies are payable at all, even if business rate income exceeds the target.

District councils have very large business rates targets (because they retain 40%) relative to their needs targets. As a result they are all tariff authorities, and all pay a levy. Conversely, almost all county councils are top-up authorities and do not pay levies. Because most rural areas have two-tier structures, most of the rates collected in these areas are at risk of being reduced by levies. In contrast, most urban areas – outside the major city centres – are top-up areas, and above-target business rates in those areas are not exposed to levies.

There is a way that two-tier areas can reduce the levies that are payable, and that is by using business rates pools. In these pools, county councils (top-ups) and district councils (tariffs) combine together to reduce the average levy rate on above-target business rates collected. In most cases, the average levy-rate is reduced to zero, although not in all cases. This arrangement does not work for every area or for every district council, which means that many districts – and many rural areas – are exposed to the full levy rate.

The rates baselines that authorities were given in 2013-14 included the reliefs that were given to businesses at that time. These included both the mandatory and discretionary reliefs. However, any change in those reliefs (except those funded specifically by central Government through a section 31 grant) has a financial effect on the local authority broadly equivalent to the function shares outlined above. If the amount of relief awarded (such as charitable or rural relief) increases then the local authority has to pay for its share of the increase; if it reduces, then the authority gets its share of the reduction. There is therefore a financial incentive to reduce the value of reliefs that are awarded locally, but in the case of mandatory reliefs the authority has no choice other than to award the relief to qualifying businesses.

When the Retained Rates system was introduced in 2013-14 it was envisaged that the system would be “frozen” until 2020-21. This meant that the rates targets, top-ups and tariffs would be untouched (other than to increase for inflation every year). Freezing the rates target for 7 years means that there is a reasonable incentive effect for those authorities with growing rate bases (although those with falling rate bases have to suffer the effects for this period as well). There are two problems with this approach:

- Revaluation of rateable values (RV) in 2017-18 – part-way through the freeze – and it is unclear how this would be handled. The revaluation would change the RV of every property in England and change the national multiplier as well. It would cause significant disruption to the system.
- The needs target will remain frozen until 2020, which means that the formulae for assessing needs will not be changed for 7 years, and neither will the underlying data that drive the formulae. “Errors” (perceived or real) could not be corrected during this period; and the formulae cannot respond to changes in demography. For rural authorities, the damping that eroded their “gains” in 2013-14 cannot be addressed or reduced until 2020.

It is unclear how the reset in 2020-21 would be handled: would the new baselines be reset entirely, would authorities be allowed to retain some of their previous gains, and would there be a transitional period?

In practice, the Government could change the targets (and the resulting top-ups and tariffs) if they wished: the mechanics of the system allow ministers to do this; it has been a policy choice to freeze targets and the top-ups and tariffs. At least until now.

100% business rates retention

Under the Chancellor’s proposals all business rates income (£26bn) would be retained locally, although it is unclear whether this includes the £1bn “central list”. 100% retention would apply to the sector as a whole. The Government is still envisaging transfers between local authorities – possibly by using something similar to the current top-ups and tariffs.

It is important to note that what is being proposed is not proper localisation of business rates or self-financed local authorities. The Government will continue to tell every authority how much of their own business rates they can keep, and how much has to be paid over to support other authorities. The amount authorities can keep – and how much they have to spend – will continue to be determined by the Government's assessment of their ability to collect taxation (council tax and business rates) and their need to spend (needs assessment).

A recent Ministerial Statement by the Secretary of State, Greg Clark, confirmed there would be redistribution between Councils – although gave no hint of what that may be. The Statement reads, "Redistribution between Councils will remain important, to reflect the needs of different authorities".[4] The Statement goes on to say, "In developing the reforms we will consider the responsiveness of the system to future changes in relative needs and resources whilst maintaining a strong incentive for authorities to grow their local economies" and "we will also consider how risk and business rates volatility can be better managed and how to protect authorities against significant falls in income".

Phasing of the proposals is still unknown: all that has been promised is that 100% of rates will be retained locally by the end of the parliament. A period of engagement with local government is starting in early 2016, and there will be a consultation paper in Summer 2016 followed (possibly) by primary legislation. With such a timetable it is possible that the transition to 100% retention could start in 2018-19, however.

The increase in locally-retained rates to 100% does not represent "new money" or increased spending power for local government. The increase in Retained Rates will be in return for the elimination of "core" grants (e.g. RSG, and possibly New Homes Bonus) and new burdens. We estimate that local government will have to shoulder around £11bn in new burdens, funded through Business Rates retained income, by the end of the parliament if the increase in retention is going to be fiscally neutral.

The nature of these new burdens will be as important as rates retention itself. Ministers might already have an eye on what these new functions could be (e.g. the expanded childcare offer, new public health responsibilities). Other ideas could take a little more thought (e.g. housing benefit) or be more controversial (e.g. unemployment benefits). Attendance Allowance looks to be a very likely candidate; if this is the case, then it would account for more than half of the additional new burdens (£5.5bn out of the £11bn). What is important for local government for the medium term is whether growth in local business rates matches the growth in spending pressures on these new burdens; this balance will be different for each authority. And it will be important to understand where there will be greater costs of delivery of the new burdens in the rural context.

Another consequence of the increase in retention is that many of the new burdens are likely to be for upper-tier services (social care, childcare). This will increase the share of business rates retained by county councils in two-tier areas (currently districts retains 40% of business rates growth and counties c.10%), as well as its share of future growth (or contraction). Some of them will also be

[4] Written statement (HCWS221), 12 October 2015

much higher per head in higher-need (typically urban) areas, which will increase the amount of rates than needs to be retained in these areas. This could push some urban authorities into the tariff category, and could reduce the levy rates in some rural areas.

With 100% retention, authorities will be able to keep all the growth in their business rate income. The Government wants authorities to promote growth and attract businesses, and in return to benefit from increases in business rates. This suggests that there will be no more levies on above-target growth, but our view is that this is probably unlikely. This leaves the question of what kind of safety net there will be for those with falling business rate income, and how that will be paid for.

It is not clear how ministers will deal with any needs assessments. A freeze in needs was expected until 2020-21. The proposals for increased local business rates retention are not incompatible with the current freeze. Treatment of specific funding streams within RSG – council tax freeze grant and rural services delivery grant – also needs to be watched.

The vexed question of equalisation is left open. There is the suggestion that resources will be equalised once at the start of the new scheme, and possibly not again thereafter; this would allow growing authorities to keep all their future business rate income (this is "point" equalisation). More frequent equalisation of resources (and of needs) would help those with less ability to generate business rates growth (and those with growing needs); but would come at the price of "taxing" growing authorities and reducing the incentive effect on these authorities. Ultimately the balance between equalisation and incentives is one that ministers will have to make.

Appendix 2 – Mandatory and Discretionary Reliefs

Mandatory reliefs	• Small Business Rate Relief (SBRR). Small businesses occupying one property with an RV of less than £12,000 can get relief of 50%. In recent years this has been doubled to 100%, and the Chancellor has announced that it would be extended further (to March 2017) in the Spending Review on 25 November. (There is also a lower multiplier for small businesses.) • Charitable organisations and amateur community sports clubs. These organisations can apply for relief of up to 80%. This relief is mandatory but charities can apply for discretionary relief of up to 100%. • Rural Rate Relief. This is available to businesses with rural populations of less than 3,000. Mandatory relief at 50% is available if the business is the only village shop or post office (with an RV of less than £8,500) or the only petrol station or public house (with an RV of less than £12,500). Further relief (up to 100%) is available at the discretion of the local authority and can include businesses with rateable values of up to £16,500.
Unoccupied reliefs	• Exempted buildings. These include agricultural land and buildings, buildings used for training or welfare of disabled people, and buildings registered for public religious worship, including parish halls. • Empty properties. Business rates are not payable for the first 3 months that a property is empty. • Partial empty relief. Extended relief can be granted for some types of property (e.g. low RV (below £2600), between charitable occupation, industrial premises).
Discretionary reliefs	• Charitable and Community and Amateur Sports Clubs (CASC), and for rural reliefs.

Appendix 2 – List of CCN Members and key data

			Average RV Growth	Needs per head	Gross RV per head	Gross Rates payable per head	Net rates payabe per head	Net rates as % of gross rates	Mandatory Reliefs per head	MR as % of GR payable	Reductions in MR	Unocc Reliefs per head	Unocc Reliefs as % of GR payable
1	Buckinghamshire	County	1.41%	122.21	833.51	398.37	346.53	86.99%	32.67	8.20%	-15.52%	14.08	1.69%
2	Cambridgeshire	County	-0.02%	147.07	1073.30	515.58	434.55	84.28%	64.22	12.46%	-12.83%	10.29	0.96%
3	Central Bedfordshire UA	Unitary	3.07%	142.38	771.91	364.95	314.98	86.31%	33.35	9.14%	-16.44%	10.17	1.32%
4	Cheshire East UA	Unitary	0.89%	149.99	912.90	438.19	381.69	87.11%	36.52	8.33%	-3.23%	12.31	1.35%
5	Cheshire West and Chester UA	Unitary	1.14%	220.00	1159.12	550.05	483.06	87.82%	28.89	5.25%	-29.09%	22.61	1.95%
6	Cornwall UA	Unitary	0.71%	311.59	779.86	377.27	290.62	77.03%	68.04	18.03%	-0.37%	6.50	0.83%
7	Cumbria	County	0.71%	259.59	984.59	473.13	407.03	86.03%	48.53	10.26%	-13.31%	9.08	0.92%
8	Derbyshire	County	1.12%	207.83	626.51	302.56	260.86	86.22%	28.07	9.28%	-15.56%	7.50	1.20%
9	Devon	County	0.52%	234.43	821.61	396.27	327.04	82.53%	49.92	12.60%	-6.10%	9.12	1.11%
10	Dorset	County	1.38%	192.03	727.64	347.24	285.67	82.27%	45.21	13.02%	-8.89%	7.21	0.99%
11	Durham UA	Unitary	1.48%	318.26	583.40	278.77	226.23	81.15%	34.70	12.45%	-5.99%	5.54	0.95%
12	East Riding of Yorkshire UA	Unitary	9.34%	216.63	742.66	360.72	319.72	88.64%	24.52	6.80%	-20.62%	7.40	1.00%
13	East Sussex	County	0.46%	225.48	620.82	297.36	241.74	81.30%	43.50	14.63%	-7.57%	4.96	0.80%
14	Essex	County	-0.17%	184.46	836.07	400.04	352.37	88.08%	31.47	7.87%	-18.78%	8.61	1.03%
15	Gloucestershire	County	0.92%	192.66	856.54	411.97	357.94	86.88%	36.24	8.80%	-17.28%	10.75	1.26%
16	Hampshire	County	0.21%	118.21	891.69	426.17	379.96	89.16%	26.33	6.18%	-24.81%	10.79	1.21%
17	Herefordshire UA	Unitary	3.23%	281.98	685.97	330.60	261.59	79.13%	46.56	14.08%	-8.70%	10.59	1.54%
18	Hertfordshire	County	-0.24%	142.86	1057.55	502.30	445.68	88.73%	34.51	6.87%	-21.38%	12.22	1.16%
19	Kent	County	0.40%	198.63	911.20	434.47	374.24	86.14%	39.09	9.00%	-15.58%	10.36	1.14%
20	Lancashire	County	0.54%	215.79	812.23	386.05	329.23	85.28%	38.14	9.88%	-12.11%	10.56	1.30%
21	Leicestershire	County	0.41%	126.49	827.40	394.72	349.30	88.49%	30.55	7.74%	-19.35%	7.25	0.88%
22	Lincolnshire	County	1.06%	225.96	698.36	336.82	284.82	84.56%	37.88	11.25%	-10.07%	7.29	1.04%
23	Norfolk	County	0.12%	246.22	770.57	370.23	314.50	84.95%	37.95	10.25%	-12.26%	9.27	1.20%

			Average RV Growth	Needs per head	Gross RV per head	Gross Rates payable per head	Net rates payabe per head	Net rates as % of gross rates	Mandatory Reliefs per head	MR as % of GR payable	Reductions in MR	Unocc Reliefs per head	Unocc Reliefs as % of GR payable
24	North Yorkshire	County	0.81%	185.82	872.85	419.53	358.49	85.45%	43.45	10.36%	-8.99%	7.53	0.86%
25	Northamptonshire	County	0.21%	172.80	954.51	458.74	398.40	86.85%	35.26	7.69%	-17.98%	14.51	1.52%
26	Northumberland UA	Unitary	3.44%	303.91	638.57	310.16	252.79	81.50%	38.58	12.44%	-9.28%	9.12	1.43%
27	Nottinghamshire	County	2.69%	191.40	690.11	329.43	292.02	88.64%	26.96	8.18%	-17.96%	5.46	0.79%
28	Oxfordshire	County	-1.00%	135.34	1097.89	525.84	448.89	85.37%	57.04	10.85%	-17.18%	8.89	0.81%
29	Shropshire UA	Unitary	2.24%	255.14	659.12	317.73	263.71	83.00%	40.66	12.80%	-9.13%	5.75	0.87%
30	Somerset	County	0.41%	219.86	785.33	375.27	317.46	84.59%	42.49	11.32%	-9.21%	7.66	0.98%
31	Staffordshire	County	1.04%	162.41	795.98	380.86	334.07	87.72%	26.65	7.00%	-19.20%	12.27	1.54%
32	Suffolk	County	0.32%	208.19	871.49	420.19	370.68	88.22%	33.50	7.97%	-17.82%	8.89	1.02%
33	Surrey	County	0.36%	110.40	988.48	472.75	415.45	87.88%	35.04	7.41%	-21.31%	12.45	1.26%
34	Warwickshire	County	0.53%	158.72	1049.57	509.58	455.10	89.31%	33.85	6.64%	-22.27%	15.05	1.43%
35	West Sussex	County	0.57%	138.69	951.19	456.67	405.92	88.89%	32.77	7.18%	-18.84%	9.67	1.02%
36	Wiltshire UA	Unitary	0.61%	177.44	745.45	349.35	298.49	85.44%	35.63	10.20%	-9.22%	5.78	0.77%
37	Worcestershire	County	-0.17%	167.85	820.36	392.69	336.81	85.77%	35.23	8.97%	-15.91%	11.47	1.40%
	CCN Average		1.06%		851.69	345.89	298.64	86.34%	31.64	9.15%	-14.87%	8.28	0.97%
	CCN County Average		0.79%		866.53	351.94	305.19	86.72%	31.28	8.89%	-15.85%	8.38	0.97%
	CCN Unitary Average		2.93%		764.14	310.22	260.00	83.81%	33.78	10.89%	-9.11%	7.66	1.00%
	ILB		-0.11%		3741.90	1,510.53	1,388.46	91.92%	54.09	3.58%	-35.30%	61.89	1.65%
	OLB		0.71%		910.94	369.54	328.84	88.98%	23.82	6.45%	-20.60%	10.30	1.13%
	Met		0.77%		904.76	367.61	314.31	85.50%	30.71	8.35%	-15.78%	16.03	1.77%
	Unitary		1.11%		946.73	384.67	335.47	87.21%	30.98	8.05%	-17.17%	10.71	1.13%

Appendix 3 – Candidates for New Burdens

Funding	Category	Responsibility	2019/20 (£bn)
Adult Education Budget (AEB)	Adult education	Upper tier	1.5
Support for Adult Education	Adult education	Upper tier	0.2
Advanced learner loans	Adult education	Upper tier	0.5
Careers Guidance	Adult education	Upper tier	-
	Adult education Total		**2.2**
Housing Benefit Admin Subsidy	Benefits	Lower tier	0.2
Localising Council Tax Admin Subsidy	Benefits	Lower tier	0.1
'Universal Support' element of UC	Benefits	Lower tier	0.1
Employment and Support Allowance	Benefits	Lower tier	0.3
Work and Health Programme	Benefits	Not clear	0.1
Attendance Allowance (new claimants)	Benefits	Upper tier	1.0
	Benefits Total		**1.8**
Transport for London Capital Grant	GLA	GLA	1.0
	GLA Total		**1.0**
Highways Maintenance (formula allocation & incentive element)	Highways and transport	Upper tier	
Highways Maintenance (challenge fund)	Highways and transport	Upper tier	
Integrated Transport Block	Highways and transport	Upper tier	0.3
Bus Services Operators Grant	Highways and transport	Upper tier	0.3
	Highways and transport Total		**0.6**
Discretionary Housing Payments	Housing	Lower tier	-
Affordable Housing Programme	Housing	Lower tier	0.6
	Housing Total		**0.6**
Sport England Funding	Other	Lower tier	0.1
Armed Forces Community Covenant	Other	Not clear	-
Valuation Services	Other	Not clear	-
Rural Service Delivery Grant	Other	Upper and lower tier	0.1
Devolution deals (growth fund?)	Other	Upper and lower tier	2.0
Troubled Families	Other	Upper and lower tier	0.1
Youth Justice	Other	Upper tier	0.2
Early Intervention	Other	Upper tier	
	Other Total		**2.5**
Public Health Grant	Public health and social care	Upper tier	3.1
Better Care Fund	Public health and social care	Upper tier	
Improved Better Care Fund	Public health and social care	Upper tier	1.5
Independent Living Fund	Public health and social care	Upper tier	0.2
	Public health and social care Total		**4.8**
Transition support for young people	Schools	Upper tier	-
DSG Early Years block	Schools	Upper tier	3.9
	Schools Total		**3.9**
	Grand Total		**17.4**

PIXEL FINANCIAL MANAGEMENT